

EUGENE WATER & ELECTRIC BOARD
WORK SESSION
EWEB BOARD ROOM
DECEMBER 21, 2005
6:30 P.M.

Board Members Present: Ron Farmer, Sandra Bishop, Mel Menegat, and John Simpson. Commissioner Patrick Lanning was excused.

Others Present: Randy Berggren, Dick Helgeson, Dick Varner, Jim Wiley, Marty Douglass, Jim Origliosso, Debra Smith, Tom Buckhouse, Scott Spettel, Terry Bequette, Mat Northway, and Krista Hince of the EWEB staff; and Ruth Atcherson, City of Eugene minutes recorder.

President Farmer convened the Work Session of the Eugene Water & Electric Board (EWEB) at 5:55 p.m.

REGIONAL ISSUES UPDATE

Power Resources Director Dick Helgeson presented the *Regional Affairs Update* with the aid of power points. He indicated he would focus on three areas of primary interest: the Bonneville Power Administration (BPA) allocation from the Federal Base System (FBS) as it related to new contracts in 2011, what EWEB's current position was regarding approaches to potential changes in allocation, and an overview of staff's work plan over the next three months as staff began to extrapolate the information and project the impacts and outcomes for EWEB might be. Power Management and Planning Manager Scott Spettel and Energy Management Services Manager Mat Northway joined Mr. Helgeson in his presentation.

Mr. Helgeson initiated the discussion on allocation. He said the Regional Power Act and the contracts entered into in 2001 governed EWEB's relationship with the BPA. He stated that under those documents, public agency customers had preference and could place their load growth on the BPA and the BPA would be obligated to serve it. Full requirements customers are those that buy all of their power from BPA, whereas generating utilities like EWEB purchase BPA power to meet their net requirements, or the difference between retail load and their own "declared" resources. He explained that, in either case, the cost of new resources needed to meet utility load growth was melded with the cost of the FBS power and rates slowly rose for everyone. He added that as this happened the higher new resource costs were "masked" by the significantly lower embedded costs for the FBS power.

President Farmer asked if the BPA would no longer be required to provide power to all of the public utilities if the utilities developed power resources. Mr. Helgeson replied that EWEB had the right to choose to place a load on the BPA and if EWEB chose not to place a load on the BPA they were not obligated to do so. He said if EWEB's resources failed to perform the BPA would be its default power supplier.

President Farmer asked if developing new resources placed EWEB at risk of having less allocation from them. Mr. Helgeson responded that EWEB was not necessarily obligated to declare those resources against the load. He noted that under the current contract, any resources developed

over the decade would not factor into an entitlement. He said EWEB had other resources that were undeclared that, under the Regional Power Act, could be marketed off system and were not required to be pledged to EWEB's load. However, there were other resources that EWEB was obliged to declare and pledge to serve large single loads such as the one placed on the utility by Hynix Semiconductor, Incorporated (Hynix).

President Farmer was unclear as to who determined what power was declared. Mr. Spettel agreed that some of the interpretation was "a little gray." He said the 5(b)9(c) policy of BPA that dictated, under the Regional Power Act, that EWEB was obligated to take resources that were available to it prior to 1979 and continue to use them to serve its load. Those were called "5(b) resources." He noted that Stone Creek and Weyerhaeuser were arguably not 5(b) resources. He stated that the BPA disagreed on whether Weyerhaeuser was a 5(b) resource. He related that EWEB had chosen not to fight this interpretation and had decided to use the resource to serve Hynix as EWEB did not have the right to BPA power to serve a new large single load, as Hynix was.

Since then Mr. Spettel related that EWEB had developed some additional resources, such as Stateline. He said there was a provision in the current Slice/Block contract declaring that EWEB did not have to develop resources and, if it did, those resources would not work against future entitlements. Because of this, EWEB would not be decremented any BPA power based on resource development for the duration of the contract.

President Farmer asked if this would be up for reinterpretation after 2011. Mr. Spettel replied that it was a theoretical possibility, but he felt the BPA would have a weak legal case to do so.

Mr. Helgeson thought the discussion would be more likely to center on whether or not additional conservation acquired before 2011 should count against the entitlement.

In response to a question from Commissioner Simpson, Mr. Helgeson said a newly formed public utility would have the right to approach the BPA with a request for power and then the BPA's obligation would be subject to interpretation in regard to the amount of power that should be made available at the lowest cost "preference rate." He noted this was under discussion in the regional dialogue because that issue had not come up and the region had been in a surplus condition for most of the last 20 years. He reiterated that the issue of allocation had not been "on the table" in the way it was today.

Mr. Helgeson reviewed the 2001 Power Supply Objectives. He underscored that the objectives were the basis for the existing power portfolio.

Commissioner Menegat asked what was meant by an average water year. Mr. Helgeson responded that he was alluding to a water year that was 100 percent of normal as extrapolated from the average of the 60-year water record.

In response to a question from Commissioner Simpson, Mr. Helgeson affirmed that the

existing power portfolio represented all of the power the EWEB sold both to its customers and on the trading floor.

Mr. Helgeson discussed the total supply and the average cost of EWEB power resources. He noted that the overall average cost was \$26.63 per mega-Watt hour (mWh) and this cost did not include transmission, ancillary services, or other overhead costs.

In response to a question from Commissioner Simpson, Mr. Helgeson explained that SP stood for the pre-subscription purchase that EWEB was able to sign up for prior to the execution of the new contracts. He noted that it expired at the end of this year and EWEB would pick up an additional entitlement in Block power.

In response to a question from President Farmer, Mr. Spettel clarified that EWEB would lose 25 mWh in the SP purchase and gain 25 mWh in its Block purchase, but there would be a step up in the Block amount to cover some anticipated load growth as well. He said it was a net gain of about 40 mWh.

In response to a follow-up question from Commissioner Simpson, Mr. Helgeson affirmed that the Springfield Utility Board (SUB) had purchased much of its power in the pre-subscription rate.

Mr. Helgeson gave a brief overview of the chart on EWEB's projected load-resource balance. The graph delineated firm resources in relation to medium retail load forecast and showed that the two would be at the same point in 2013.

President Farmer asked if the decline translated to a loss of margin dollars. Mr. Varner responded that the retail prices were currently \$60 to \$65 per mWh and predicted it could increase "in the outer years" to \$70 or \$80 per mWh. He said as long as the market was roughly the same, it did not matter whether it was being sold to a retail customer or sold on the wholesale market. But if the wholesale prices were substantially above this amount, it made a difference. He noted that some of the forecasts predicted electricity prices would rise to \$80 to \$100 per mWh in the market in the "outer years" and if this came about it would impact EWEB because it would be selling more to its native load and less to the wholesale market.

In response to a question from President Farmer, Mr. Varner clarified that when talking about the wholesale market he typically meant the mid-Columbia market. He added that the main trading hub in the northwest was in the Grant/Douglas/Chelan county area of central Washington. He said the prices in the northwest tended to be a little cheaper than prices in the southwest portion of the country, but this remained true only as long as there were constraints on transmission southward.

Mr. Helgeson asked Mr. Varner to project what the "net hit" to the cash flow if the surplus was gone. Mr. Varner estimated that it would translate to a \$10 per mWh loss to the margin.

Mr. Helgeson stated that one reason EWEB could have a long position on the BPA was because under the Slice contract it paid on a monthly basis for a share of the output of the system. He said whatever the system produced, EWEB would receive. He reported that to the extent that loads had fallen off due to some of the industrial loads in the early 2000 and 2001 timeframe, EWEB had the ability to withdraw a portion of its resource capability and could also market it out.

Mr. Helgeson stressed that the projected load/resource balance was not absolute given unknown quantities such as the possibility that certain variables could change how much of the FBS was available.

Mr. Helgeson reviewed the possibilities of a new approach for post-2011 contracts, which included two tiers, one for existing resources and one to pay new resource costs, and that customers could choose to place their loads on the BPA or to develop their own resources. He noted the erosion of the relative cost advantage that BPA power represented over the last 20 years. He expressed some concern at what the cost increase could be in the future if EWEB looked to the BPA to serve load growth.

Mr. Helgeson related that problems had been experienced in the last round of contracts because the power had been oversubscribed by 3000 mW and the BPA had been caught short in the energy crisis. The BPA had then secured power from other sources and this had caused a jump in rates over the last few years.

Mr. Helgeson observed that BPA functions best when acting as steward of the existing low-cost FBS resources. He noted an emerging regional view that BPA's long-term focus should be on maintaining the "tier-one" public benefits of the FBS, and that the agency's role in new resource development to meet future load growth should be reduced accordingly. With allocation and tiered wholesale rates, each utility would receive a long-term entitlement to cost-based FBS power, and would be free to develop new resources or pay the higher "tier-two" rate to meet its own load growth. He expressed his opinion that such an approach would be more likely to preserve the remaining value of the FBS for the region, while creating more appropriate economic incentives for future resource investment.

President Farmer asked if the "fish costs" were tied into Tier One costs. Mr. Helgeson responded that they largely would be because those were obligations associated with the federal dams.

President Farmer asked what the utility would have to do if it needed to gain Tier Two resources. Mr. Helgeson replied that EWEB had several options: it could go to the power market, it could go to the BPA itself, and it could acquire resources to backfill a power gap. He remarked that in a pure marketing sense the BPA was no different than EWEB; if it had a surplus or some secondary power to sell in a good water year the BPA could have an impact on the market.

Regarding the potential allocation, Mr. Helgeson averred that no utility would believe an allocation to be worth much unless the entitlement was reasonably secure and certain.

Vice President Bishop asked how many generating utilities there were. Mr. Helgeson replied that, not including the investor owned utilities (IOUs), there were about a dozen.

In response to concerns expressed by Vice President Bishop, Mr. Spettel commented that the BPA had the power and was “the 800 pound gorilla in the room.” He said a utility could challenge the power allocation and take the BPA to court but it would most likely lose the case. He averred that the balance of power was largely on the BPA side in the context of negotiating contracts and working out technical issues. Nonetheless, he indicated there was a legal framework for such a challenge and offered to provide it to the Board.

Mr. Helgeson said clearly there were resources that would not fall under the provisions of the act requiring declaration.

President Farmer expressed concern that when the contract expired the BPA might be able to require utilities such as EWEB to dedicate all resources to the load. Mr. Helgeson did not believe this would happen. He thought there was enough clarity in the original act that resources acquired over the course of the current contract would not fall under that authority according to a provision in that contract. He listed those resources, as follows: Stone Creek at 7.4 average mW, the Weyerhaeuser unit at 7.5 average mW and rising, and the Stateline Wind Project at 7 mW. He noted that it was a relatively small percentage of the portfolio, adding that he did not think EWEB was at significant risk.

President Farmer asked if any resources acquired between 2006 and 2011 would need to be declared. Mr. Helgeson replied that he was confident that they would not be deducted or required to be declared.

Continuing, Mr. Helgeson stated that the utilities that did business through the Pacific Northwest Generating Cooperative (PNGC), a group of co-ops that purchased power on a Slice contract, had decided based on their assessment that their entitlement would not be adequate. He related that the PNGC power group had argued for a new net requirements determination to increase their entitlement by 60 mW. He said if public power was willing to make this adjustment to the methodology to shunt them another 60 mW, they could make that problem go away. He predicted that more utilities would attempt to argue for larger entitlements and that ultimately utilities were headed toward some form of a new net requirements determination. He remarked that everyone was “struggling to balance their sense of principles and values with the real economic and resource impacts of an adverse outcome in an allocation.”

Mr. Helgeson underscored that the question at this point was what the new allocation would be based on and what strategy EWEB would use to prepare for an “allocation gap.” He said EWEB had work to do over the next quarter and over the next year and reviewed the staff 2006 work plan.

Vice President Bishop asked who would be engaging in the “modeling” of potential outcomes. Mr. Helgeson replied that Mr. Spettel, Mr. Maloney, Brenda Sirois, Resource Planning Analyst, and other staff would be working on it. He predicted staff would be back in April with the first results.

President Farmer said the preferred path was unclear to him. Mr. Helgeson responded that EWEB was in support of an allocation and was looking for an outcome consistent with its principles.

Mr. Berggren commented that ultimately EWEB was seeking to mitigate its risk relative to a potential decrement.

President Farmer asked if EWEB was trying to maintain its “18 long position.” Mr. Berggren affirmed that it was.

President Farmer asked what method was needed to do so. Mr. Helgeson responded that EWEB wanted to retain its allocation. He said EWEB would try to shepherd the process as it progressed and would do what it could to ensure a favorable outcome.

Mr. Spettel commented that if EWEB had to do a forecast as opposed to historical entitlements he would work to make sure the forecasts were not biased. He related that EWEB had been asked to demonstrate that an “internet hotel” for which transformers had been ordered was a real adjustment to the forecast earlier in the year. He hoped that other utilities would not attempt to claim phantom loads. He also expressed concern regarding the validity of some resource adjustments. He noted that some utilities were arguing that when they sold their interest in a 5(b) resource they should receive an entitlement. He added that the law clearly indicated that this would not merit an entitlement.

President Farmer remarked that he wished to see EWEB’s preferred alternatives.

Mat Northway, EWEB’S Energy Management Services Manager, reviewed the *Conservation and Renewables Discount 2002-2006*. He explained that EWEB currently operated conservation programs under two arrangements with the BPA: a rate credit arrangement called C&RD and a purchase of energy conservation called ConAug. He said both programs ended in September 2006, and would be replaced by programs that were similar but would operate under different headings.

Mr. Northway explained that the credit on the wholesale power bill from the BPA could be kept as long as EWEB was engaged in conservation activities that qualified according to them.

Mr. Northway reviewed the changes in principles that would accompany the change from the C&RD to the Conservation Rate Credit (CRC). He also reviewed the shifts in principles that would occur with the change from ConAug to the Conservation Acquisition Agreement (CAA). With both, the payment rates to EWEB were reduced.

In response to a question from President Farmer, Mr. Northway predicted that payment rates would experience a reduction of around \$1 million.

In response to another question from President Farmer, Mr. Northway stated that the 2006 budget assumed that EWEB would receive a \$1 million credit. Mr. Helgeson said the 2007 financial plan assumed that those funds, to the extent they were available, would be used to supplement the baseline rate-funded conservation.

Mr. Spettel clarified that in terms of financial planning EWEB had not counted on the \$1 million from the CAA for 2007 and beyond. He said EWEB had only counted on the CRC.

President Farmer adjourned the meeting at 7:35 p.m.

Assistant Secretary

President