



MEMORANDUM

EUGENE WATER & ELECTRIC BOARD
POWER RESOURCES DIVISION

Rely on us.

TO: Commissioners Farmer, Brown, Cassidy, Cunningham and Ernst
FROM: Eric Hiaasen
DATE: September 8, 2009
SUBJECT: BPA Post 2011 Contract Amendments and Tier 2 Election

Issue Statement

EWEB signed a new twenty year power purchase contract with the BPA in December 2008. The contract includes a requirement that EWEB notify BPA by November 1, 2009 of our decision of whether or not EWEB will purchase power from BPA at the Tier 2 Rate for the first three years of the contract, October 2011 through September 2014.¹

In addition to the Tier 2 decision, BPA has produced contract amendments for both the Power Sales Agreement and Slice Creditworthiness Agreement that EWEB and BPA signed late last year. These amendments resulted from a number of minor issues that were discovered too late to change and still meet the December 2008 deadline. BPA and public power customers agreed to fix these issues via amendments to the contracts, which were finalized recently.

Staff considers these decisions to be straightforward. We will present the issues at the September 15, 2009 Board work session. The resolution to approve will be presented for action at the October 6 Board meeting.

Background

Tier 2

EWEB's current ten year Slice and Block contract with BPA expires on September 30, 2011. In December 2008 EWEB signed a new twenty year power purchase contract with BPA that will start delivery on October 1, 2011 and run through September 30, 2028.

One of the most significant changes in this new contract was the adoption of BPA's Tiered Rate Methodology (TRM), which effectively allocates BPA's existing low cost legacy resources among BPA's public power customers. This allocation of low cost power is referred to as Tier 1 power, and the allocation will not increase for the duration of the contract.

As EWEB needs additional power to serve load, either due to load growth or loss of resources, BPA will only sell us additional power at the higher Tier 2 rate. EWEB has the choice whether to purchase Tier 2 power from BPA or to acquire other resources on our own to supply that need.

BPA created four separate Tier 2 Purchase Periods, with a notification required two to three years in advance of the when deliveries would start to allow adequate time for planning and acquisition.

¹ In BPA parlance, this is known as Fiscal Year or FY 2012 through FY 2014.

The notification deadline for the first Purchase Period covering the first three years of the contract is November 1, 2009.

Clean-up Amendments

In addition to signing the *Power Sales Agreement*, Contract No. 09PB-13041 with BPA last December, EWEB also signed the *Slice Creditworthiness Agreement*, Contract No. 09PB-13254. The latter contract was required of all Slice purchasers and is intended to guarantee the payments owed to BPA.

In the fall of 2008 a number of minor contract issues were discovered too late to change and still meet the December 2008 deadline. BPA committed to fix these issues via amendments to the contracts, so these amendments were anticipated when we signed the contract. BPA ran an open process with public power earlier this year to carefully review the contracts and discuss proposed changes.

The vast majority of changes in Amendment No. 1 to the Power Sales Agreement are minor language changes that help clarify the intent of the contract. A BPA document titled [Background Information Sheet on Regional Dialog Clean-up Amendments](#) lists the reasons and criteria for making changes to the contract. Should you wish to see the actual contract changes, a detailed list in a red-line format along with comments explaining each change is available at BPA's web site as the [Slice/Block Companion Document](#).

The only proposed change that is not trivial is the optional additional language clarifying the methodology by which a public power utility that owns generation, such as EWEB, would have benefits calculated should EWEB choose to participate in the Residential Exchange Program. These changes eliminated inconsistencies between the Residential Exchange Program and BPA's recently adopted TRM that could have allowed a utility to circumvent the intent of Tiered Rates.

The changes in Amendment No. 1 to the Slice Creditworthiness Agreement provide clarifications and additional assurances to BPA that EWEB will be able to meet payment obligations for the Slice portion of EWEB's Power Sales Agreement with BPA as well as addressing concerns of some utilities.

Discussion

Tier 2 Decision

When staff evaluates resource acquisition opportunities there are two very important questions to consider:

1. Does EWEB "need" the power?
2. How does the price compare to alternatives?

There are additional questions that must be answered before staff can recommend acquisition of a resource, but if these first two questions are negative, then there is no point in continuing to analyze that opportunity.

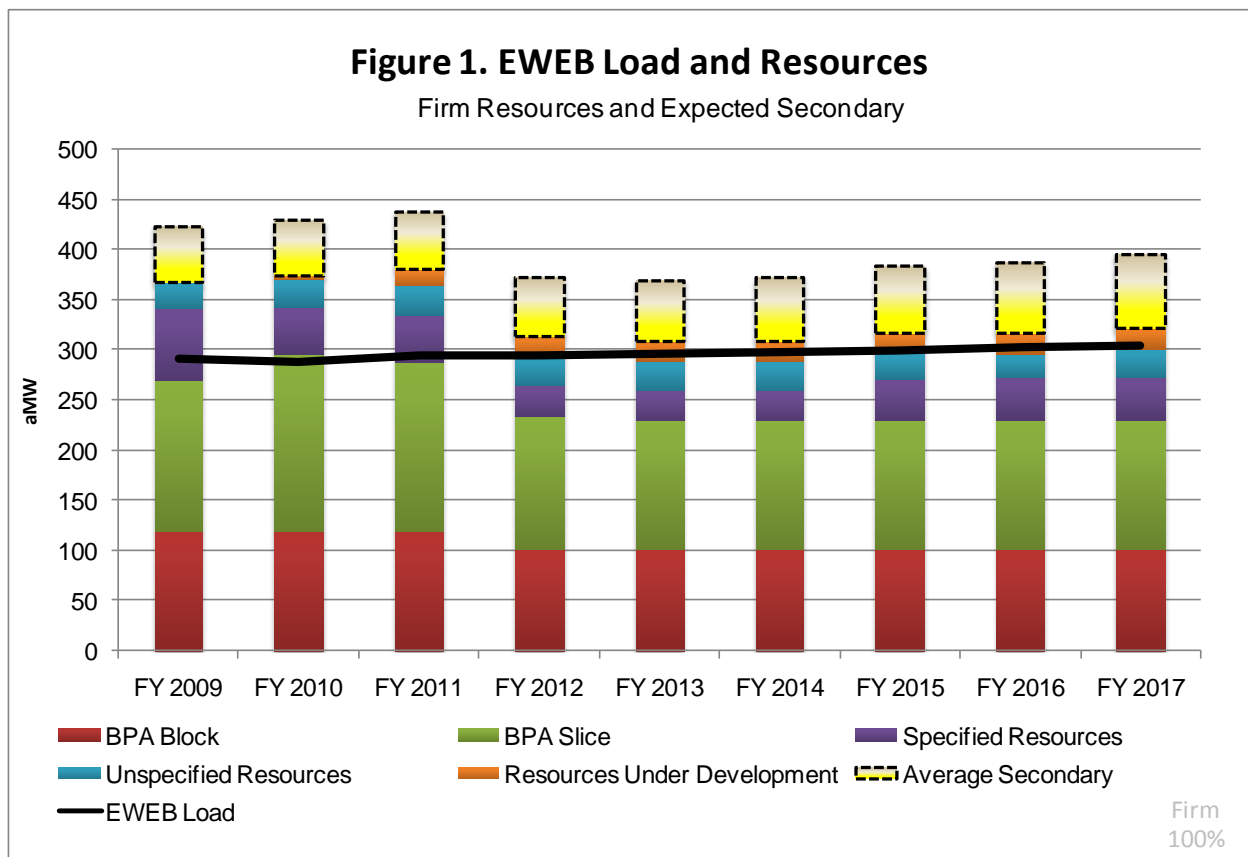
1. *Does EWEB "need" the power?*

EWEB has "need" for power when forecast EWEB load plus wholesale sales exceeds EWEB resources and wholesale purchases. But, the answer to that simple calculation is a function of the time frame. EWEB could simultaneously be surplus using forecast annual average loads and

resources, but also be deficit in winter months using forecast monthly loads and resources². Planning with annual average values can lead to sub-optimal results in terms of costs and risk. EWEB's last two IRP's have taken planning to a monthly level.

But, BPA adopted policies in the TRM that mandate annual average planning based on BPA's Fiscal Year of October 1 through September 30 for determining EWEB's need for power and put those requirements into our power contract. Therefore, the following analysis is presented using annual average values based on the BPA Fiscal Year (FY), rather than a more sophisticated monthly presentation.

Figure 1 below shows EWEB's forecast loads and firm resources in a simple annual average format from FY 2009 through FY 2017. At the bottom of the stack are the *BPA Block* and *Slice* resource, which together comprise about 74% of EWEB's firm resource portfolio in 2012.



EWEB's *Specified Resources* are EWEB's legacy hydro projects and the Foote Creek Rim wind resource that are dedicated to serve EWEB for the purposes of establishing EWEB's Tier 1 High Water Mark (HWM) entitlement.

The *Unspecified Resources* are EWEB's existing resources that EWEB has not dedicated to serve EWEB loads: Stone Creek hydro resource, EWEB's share of the IP Cogen facility, our Stateline and Klondike 3 power purchase agreements. In 2016 EWEB's 10 aMW share of the Wauna biomass cogeneration facility becomes available to EWEB when the 20 year sale to BPA expires.³ EWEB plans to use some or all of these resources to serve our Tier 2 need.

² This occurs if we are surplus in other months more than we are deficit in the winter

³ EWEB and Clatskanie PUD share that resource until April 2021 when the contract ends.

The *Resources Under Development* represent the new Harvest Wind Project with an online date of January 2010, and the Seneca Biomass Project with an online date of January 2011. The Raft River Geothermal Project, is not included in these forecasts because staff believes that resource is too speculative to include.

At the top of the chart the dashed area represents the secondary energy generation produced by EWEB's hydro, and to a small extent, wind resources. Secondary energy is energy production over and above firm generation. Firm hydro generation is based on the driest year on record.⁴ In most years EWEB gets above firm output from our hydro and wind resources, so it is important to factor that additional energy into our planning.

While EWEB acquires sufficient firm resource to meet forecast load, EWEB sets rates and budgets on the worst (lowest) continuous 5 year average generation. Worst 5 year generation is bigger than firm generation. On Figure 1 the yellow portion of the secondary energy is approximately equal to the budgeted generation. The full dashed area represents the expected generation based on the average of the entire 70 water-year record.

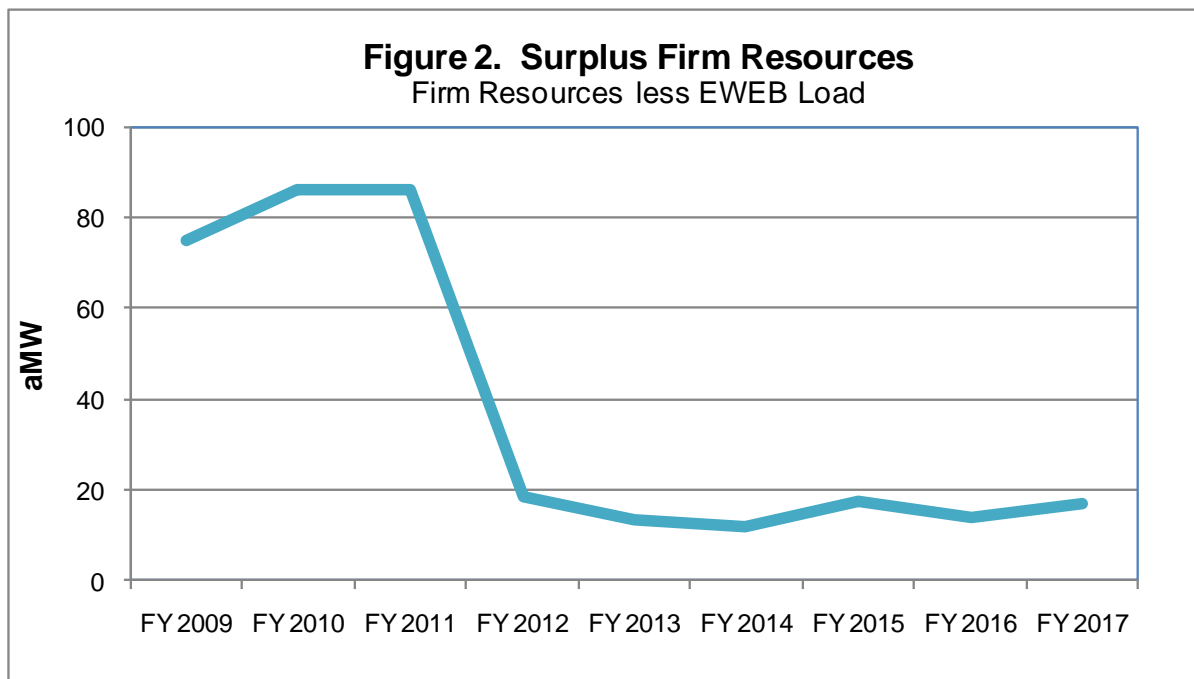


Figure 2 shows staff's forecast of EWEB's surplus firm resources through 2017. Obviously, there is a great deal of uncertainty that is not represented in this simple chart, so it is possible EWEB will need resources sooner than 2017. Loads could be higher than expected because of the repowering of the Hynix chip plant or from rapid adoption of electric vehicles. Or, resources could decline from forecast levels because of an extended outage of the CGS nuclear plant or removal of Snake River Dams.

But this chart also does not reflect potential positive uncertainties. Potential sources of additional resources are from EWEB's conservation programs prior to 2011 providing a credit to our HWM or from the potential Provisional HWM Adjustment due to the extended outage at the IP mill this fall.

⁴ Wind firm generation is derived from the lowest 12 month moving average on record, because we only have a limited number of years for actual wind generation.

Another potential factor that could increase our surplus in the future would be if EWEB increased its conservation acquisition, either voluntarily or due to requirements arising from the recently released Draft 6th Power Plan.

At this time, staff forecasts EWEB will have sufficient resources to meet EWEB's loads during the initial Tier 2 Purchase Period from FY 2012 through FY 2014.

2. *How does BPA's Tier 2 price compare to alternatives?*

Having stated that EWEB doesn't need the power from FY 2012 through FY 2014, should we consider purchasing Tier 2 power from BPA because we believe it is a good deal in the long run? EWEB acquired several resources in this decade despite our existing surplus of power because we anticipated the loss of BPA power when the current contract expired. Our strategy was to acquire resources ahead of need to avoid the possibility of having to scramble for new resources immediately prior to the new contract. We acquired them as good long-term additions to our portfolio.

Staff does not believe that a Tier 2 purchase would provide a similar opportunity over the years FY 2012 through FY 2014.

As a Slice purchaser EWEB is eligible to purchase Tier 2 power from BPA either as *short-term market* rates or as a *vintage resource*. A vintage resource is when EWEB purchases a share of a larger resource that BPA acquires to serve many customers. It is similar to EWEB's 25 year power purchase agreements for portions of Stateline and Klondike 3 wind projects.

EWEB already has the ability to purchase short-term market power without BPA's assistance, and can purchase just the months that we want and purchase at the time we choose. If we purchase short-term Tier 2 from BPA it is delivered as a flat annual block. We will not know what the cost of this purchase will be at the time we sign the Tier 2 contract, because those rates will be set at the end of a future BPA Rate Case, which may be a bad time to lock in prices.

EWEB also already has the ability to acquire shares of a new resource without BPA's involvement. If we believed that BPA could obtain some competitive advantage in the acquisition process then we might be more interested in participating in one of their vintage resource projects, but, so far we have seen no evidence of that. In fact, BPA has only provided "indicative" costs for different resource technologies, which are not attractive, compared to other projects EWEB sees. Actual costs for a vintage Tier 2 resource will be determined during negotiations with project developers.

Contract Clean-up Amendment to the Power Sales Agreement

As stated above, the vast majority of contract changes are minor language changes that help clarify the intent of the contract. The only proposed change that is not trivial is the proposed additional language clarifying the methodology by which a public power utility that owns generation, such as EWEB, would have benefits calculated should EWEB choose to participate in the Residential Exchange Program

The Residential Exchange Program was included in the Northwest Power Act of 1980 that allows a customer of BPA to exchange the cost of its own resources used to serve its residential and small farm customers for the cost of an equal amount of BPA resources. A utility whose average resources cost was above BPA's average resource cost could spread its higher costs among all of BPA's customers.

In the past, it has been primarily the Northwest regional IOUs that participated in the Residential Exchange. That's because the average system cost of most public power utilities' generation, including EWEB, were below BPA's average system cost, so there wasn't any advantage to an exchange.

BPA is providing this new language to clarify how average system cost would be calculated should we elect to enter into an exchange contract with BPA in the future. This election is at EWEB's choice. Therefore, staff sees no risk to including this language in our contract amendment.

Contract Clean-up Amendment to the Slice Creditworthiness Agreement

The changes in Amendment No. 1 to the Slice Creditworthiness Agreement provide contract clarifications and additional assurances to BPA that EWEB will be able to meet payment obligations for the Slice portion of EWEB's Power Sales Agreement with BPA. These changes have been driven primarily by BPA. The proposed changes have been reviewed by EWEB staff and by EWEB's attorneys and found acceptable.

Board Options

Tier 2 Election

The Board can either choose to request no Tier 2 power from BPA, or request all the Tier 2 power we are eligible for, approximately 22 aMW. Or, the Board could choose to purchase any amount between 1 and 22 aMW.

Amendment No. 1 to the Power Sales Agreement

BPA is allowing utilities the choice of whether or not we want to include the language for the Public Residential Exchange. The remaining Clean-up Amendments can not be altered.

The Board has three choices. It can either sign Amendment No. 1 to Contract No. 09PB-13041, the BPA Power Sales Agreement including the Public Residential Exchange. Or, the Board can sign Amendment No. 1 to Contract No. 09PB-13041, the BPA Power Sales Agreement excluding the Public Residential Exchange. Or, the Board can decline to sign the amendment.

Amendment No. 1 to the Slice Creditworthiness Agreement

The Board can either sign Amendment No. 1 to, Contract No. 09PB-13254, the Slice Creditworthiness Agreement, or the Board can choose to not sign.

Recommendations

Staff believes that all three of these matters are straightforward.

Tier 2

Staff does not see any reason to recommend a Tier 2 purchase from BPA for the first three years. First, we do not forecast a need for the power on an annual basis. Second, the costs for any Tier 2 purchase do not look attractive and the rates wouldn't be set until after we have committed to purchase the power. Third, BPA requires EWEB to take the Tier 2 power as a flat annual block, rather than in just the months we require the power. This will force EWEB into more market activity

because we will be purchasing power in the months we need more, and selling the power in the months we don't need the flat block.

The second Tier 2 Purchase Period covers the five year period FY 2015 through FY 2019. The contract requires EWEB provide notice to BPA whether or not we want to purchase any Tier 2 power during those years by September 30, 2011. EWEB will have another opportunity to purchase Tier 2 power from BPA in the future, but with the benefit of two more years to gather additional information.

Staff recommends that EWEB take no Tier 2 power from BPA at this time.

Amendment No. 1 to the Power Sales Agreement

Staff recommends EWEB sign Amendment No. 1 to the Power Sales Agreement, Contract No. 09PB-13041, and include the optional language for the Public Residential Exchange. Having signed the Power Sales Agreement with BPA in December 2008, staff can think no reason not to sign these amendments. Failing to approve would leave EWEB with a less clear contract with inaccurate references and imprecise definitions.

Amendment No. 1 to the Slice Creditworthiness Agreement

Staff recommends the Board sign Amendment No. 1 to, Contract No. 09PB-13254.

BPA has indicated that they will not sign any of these amendments until all Slice customers have signed. BPA is insisting that all Slice customers have identical contracts, so if any Slicer declines to sign, then we will all remain on the original Slice Creditworthiness Agreement.

Suggested Motions

There are no motions at this time. Staff will return with a resolution at the October 6, 2009 Board meeting at which time the Board will take action.