

## **SLICE ISSUES PAPER**

### **BPA Positions**

#### **I. Issue: Post-2006 Inventory Augmentation Costs**

#### **II. Questions:**

What should the Slice participant's responsibilities be for future inventory augmentation in subsequent rate periods?

#### **III. Background:**

- A. The Slice product is a minimum 10-year product.
- B. Slice participants' financial risks, for the true-up and power losses (hydro creep), is not capped as it is for the Cost Recovery Adjustment Clause (CRAC).
- C. Slice shares will not increase as inventory is augmented to meet Subscription requirements.
- D. Slice participants will be able to increase firm block purchases to meet their load growth in future Subscriptions. Slice participants will pay the "then applicable PF rate" for the increases in their block purchases.
- E. As the Slice product was originally proposed, the cost of Slice would have included only costs for resource additions necessary to meet the pre-2002 Subscription load.
- F. When BPA composed the first Slice product description, in February 1999, BPA and interested parties concluded that Slice participants must bear "reasonably equitable" responsibility for inventory augmentation costs as other 10-year contract signers.
- G. Slice participants have commented that this aspect of the Slice product significantly affects the risk associated with Slice and is a strong disincentive to signing 10-year contracts.
- H. Consequently, Slice participants have made a case that given the 10-year minimum term for Slice, the Slice participants' responsibilities for post-2006 "inventory solution" costs should be clearly defined in the Slice contract. They have suggested that the amount of system augmentation should be defined not to exceed a pre-determined amount in MWs, the net cost of which will not be limited. The proposed cap is the 2002 power rate case inventory augmentation plus 400 aMW for additional service to IOU residential and small farm load, plus a limited amount of new public agency loads.
- I. Attachment 1 identifies all of BPA's public (written) references to the Inventory Solution for additional background.

#### **IV. Review of methodology for “Net Cost” of the Inventory Solution:**

- A. The “net cost” approach that BPA proposed in its 2002 initial rate proposal sets the Slice participants’ share of the financial obligation of the inventory solution based on:
  - 1. the size of the system augmentation (in MWs), and
  - 2. the “net” price of the system augmentation (price of system augmentation less the PF rate the associated system augmentation is disposed at).
- B. The net cost approach allows the Slice participants to participate in the inventory solution without the need to adjust the power deliveries to the Slice participants.
- C. The net cost approach does not include augmentation used to replace Federal Base System (FBS) capability that is lost due to changes in FBS operations (such as implementation of new fish measures). This loss is already incorporated into the Slice product since the Slice participants would receive less Slice power (given that they would get a share of the actual generation produced).
- D. For this discussion, the Inventory Solution is the amount of system augmentation that is needed to meet the sum of the loads for the following categories:
  - 1. Pre-existing Federal load commitments
  - 2. Public load
  - 3. IOU load (Residential Exchange)
  - 4. DSI load

#### **V. Review of Proposal and Associated Process:**

- A. Slice participants have proposed that their participation in future inventory solutions be based on the same “Net Cost” methodology, except that the amount of system augmentation (see IV.A.1 above) should not exceed a pre-defined amount of system augmentation. This would not necessarily limit the Slice participants’ cost exposure (say if the cost of purchases were to increase) but it would define what augmentation they would or would not participate in.
- B. Over the course of the next few months, BPA will examine this issue. BPA has yet to determine what process it will use to decide this issue but we would like some input from our customers.
- C. BPA is considering using the Slice participants’ proposal with the following clarifications:
  - 1. Pre-existing Federal load commitments identified in the 2002 power rate case.
  - 2. Public load as identified in each power rate case (no limit).
  - 3. IOU load (Residential Exchange) up to 2200 MWs.
  - 4. DSI load up to 1440 MWs

#### **VI. Considerations:**

- A. Does this represent a fair sharing of risks, consistent with the intent of the Slice product and the risks borne directly by Slice participants?
- B. If policy changed regarding who may subscribe to BPA power, does this appropriately treat Slice participants with respect to paying for any additional inventory augmentation? Does this represent a potential cost shift to other customers?
- C. The Slice product does not include provisions to cover a participant's load growth, so Slice will not contribute to the need to augment inventory.
- D. Slice provides other risk benefits to BPA and the region that other requirements products do not provide (no cap to financial adjustments, hydro creep and market price risks taken on directly by the Slice participant).
- E. The Slice product purchased by participants does not receive any portion of the augmented power associated with the inventory solution.
- F. Unlike other requirements products, Slice has a minimum term of 10 years. Slice participants do not have the option of signing up for 5 years if they are uncomfortable with the uncertainty of future inventory augmentation.

## Attachment 1

### **BACKGROUND REFERENCES**

In order to avoid a shifting of costs to non-Slice purchasers, BPA stated that the Slice purchasers would be required to pay the cost of power purchases that were needed on a planning basis to meet all load service requests made under the Subscription process, the "regional solution" (inventory solution). Power Subscription Strategy, Administrator's Record of Decision, December 1998, p. 103.

Purchasers of Slice shares will pay their proportionate share of the net costs of relieving the expected FCRPS inventory constraint (inventory solution), whether that solution is power purchases, cash payments or another solution. Power Subscription Strategy, December 1998, p. 14.

BPA stated that only customers who make commitments greater than five years will get a contractual guarantee of BPA's lowest cost-based rate beyond FY2006. BPA suggested a possible approach for "providing benefits to those customers that make a longer-term commitment." One way to approach this was for this lowest cost-based rate to bear the costs associated with loss of system capability but, in the future, would be protected from costs associated with serving additional load placed on BPA after the Subscription window closes. Power Subscription Strategy, December 1998, p. 15.

Slice participants are responsible for paying their percentage share of PBL line item revenue requirements including the "net costs of relieving the expected FCRPS inventory constraint resulting from Subscription, including resource acquisitions and short term purchases, if necessary, but not including future inventory constraints such as those from load growth." BPA Power Products Catalog, December 1998, p. 23, and BPA Power Products Catalog, September 1999, p. 40.

The Detailed Product Description for Slice specified a method for including the net cost of the inventory solution for the 2002-2006 rate period. In subsequent rate periods, BPA stated that it will set the Slice Revenue Requirements with regards to the net cost of any "Inventory Solution" in a manner that is reasonably equitable to the treatment of such costs in rates for other 10 year (or longer) Subscription requirements contracts. Detailed Product Description, February 1999, p. 10.

BPA stated that its decisions with respect to the Slice participants' responsibility for inventory solution costs for the pre- and post-2006 periods are fair and equitable in relation to customers who sign other long-term Subscription contracts. BPA stated that it will not determine what the inventory solution costs for the post-2006 period will be prior to the rate case for that period, and while BPA will provide contractual guarantee to lowest cost-based rates for those committing to purchase for longer than five years, BPA has not guaranteed a rate for the post-2006 period. "Slice of the System" Product Team Report, August 1999, p. 21.

The net costs associated with the Inventory Solution will become an obligation of the Slice participant. Because Slice participants will pay estimated, rather than actual costs associated with the Inventory Solution, a cost shift may result. BPA will examine the potential for and the extent of a cost shift among customers in the 2002 power rate case. BPA stated that there is no way to determine what, if any, Inventory Solution will be necessary for subsequent rate periods. Slice participants will be treated in the same manner as other Subscription contracts extending beyond the FY2002-2006 rate period. 2002 Initial Power Rate Proposal, Wholesale Power Rate Development Study, WP-02-E-BPA-05, August 1999, pp. 156-157.

BPA will examine whether excluding the net costs of the inventory solution from the true-up process for the Slice product creates a cost shift. 2002 Initial Power Rate Proposal Direct Testimony of Mesa et al., WP-02-E-BPA-32, p. 12, lines 16-18, p. 13, lines 16-17.

BPA defined and described the inventory solution costs that the Slice participants would be required to pay. BPA also explained what it means by the “net cost” of the inventory solution and that it would be included in the Slice Revenue Requirement. 2002 Initial Power Rate Proposal Direct Testimony of Mesa et al., WP-02-E-BPA-32, p. 12-14.

BPA stated that the net cost of the inventory solution for the second five years (or more) of the Slice contract would be estimated in the applicable rates process for that period. 2002 Initial Power Rate Proposal Direct Testimony of Mesa et al., WP-02-E-BPA-32, p. 15.

BPA explained that it needed to consider including the net cost of the inventory solution in its true-up process for the Slice product because there was an increase in the size of the inventory solution, since the initial design of Slice. This increased the potential for a cost shift among customers if the net cost of the inventory solution was not included in the true-up process. 2002 Initial Power Rate Proposal Direct Testimony of Mesa et al., WP-02-E-BPA-32, p. 15.