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November 14, 2006

MEMORANDUM

TO: Power Committee Members

FROM: Wally Gibson, Manager, System Analysis and Generation
John Fazio, Senior System Analyst

SUBJECT: Resource adequacy implementation paper comments

The Council received only one set of comments on this issue paper. Those comments were provided by the Northwest Energy Coalition, which participated actively on both the Adequacy Forum's technical and steering committees. In summary, the Coalition believes that the implementation plan is too weak and will not ensure that the region will maintain an adequate power supply. The Coalition made three recommendations:

1. Include an analysis of the costs associated with a resource adequacy standard.
2. Re-title the paper "A Reporting and Early Warning Mechanism" and send it back to the Forum with instructions to put together a stronger implementation plan.
3. Insist that BPA be the backstop and acquire resources, if necessary, should its customers fail to meet the adequacy standard.

The concerns presented in the Coalition's comments were discussed at length during the Resource Adequacy Forum's Steering committee meetings. An assessment of the costs of maintaining an adequacy standard are important and will be made but do not need to be included in the implementation plan. The voluntary nature of the plan does leave concern as to whether utilities will take actions when and if called for, however, it was the best the committee could do given the concern of its members to avoid "regulatory" language. With regard to the Coalition's third recommendation, Bonneville is currently examining its status with respect to the proposed regional standard. Whether it should be the backstop is unclear and needs further assessment.

The full text of the Coalition's comments is provided in the Council packet under the agenda item entitled "Decision on adoption of resource adequacy implementation paper." A presentation that summarizes the implementation plan is provided as an attachment to this memo.

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Comments of the NW Energy Coalition
Northwest Power and Conservation Council's Proposed
Resource Adequacy Implementation Plan
(document # 2006-17)
October 16, 2006

The NW Energy Coalition ("Coalition") has participated extensively in the Resource Adequacy Forum. We support the metric and targets that the Council recently adopted from the Forum's recommendation. These comments, however, are directed at the Forum's recommended implementation plan ("Plan") with which we have reservations that were not adequately addressed by the Forum. We focus on the Plan's recommendations regarding the Bonneville Power Administration, because it is our understanding that the Council's recommendations will be incorporated, to a great extent, into BPA's Regional Dialogue decisions. (We also have one relatively minor problem with the Plan's proposed "red-yellow-green light" warning system that we believe is confusing that we address in this footnote.¹)

The Coalition's main concern is that the implementation plan continues to rely on a weak voluntary mechanism. Congress and the North American Electric Reliability Council are moving toward a more mandatory approach that includes penalties.² The significant costs associated with meeting the standards must be appropriately recognized in this process. It is these costs and potentially perverse market signals that could drive utility behavior to under-build under a purely voluntary standard. However, we believe *the costs of failing to meet the standards will be even greater* and cause more harm to ratepayers and the Northwest economy, as we saw in 2000-01 energy crisis.

Recommendation #1. A discussion of the real costs of maintaining this standard—and failing to meet this standard—should be added to the document, preferably with some numerical analysis and estimates.

¹ Perhaps we're just dense, but the red-green-yellow mechanism seems to imply that there are two lights: one for the economic standard and one for the physical standard. The Forum talked about only one light. It would turn yellow when the region failed the economic standard (but still met the physical standard) either three or five years out, and would only turn red when the region failed the physical standard 3 years out.

² A very recent article in the New York Times entitled, "Power-Grid Report Suggests Some Dark Days Ahead," by Matthew Wald illustrates that NERC is having second thoughts about voluntary standards:

WASHINGTON, Oct. 15, 2006 - Companies are not building power plants and power lines fast enough to meet growing demand, according to a group recently assigned by the federal government to assure proper operation of the power grid.

The group, the North American Electric Reliability Council, in its annual report, to be released Monday, said the amount of power that could be generated or transmitted would drop below the target levels meant to ensure reliability on peak days in Texas, New England, the Mid-Atlantic area and the Midwest during the next two to three years.

The council was established in 1965 after a blackout across the Northeast, and has since set **voluntary standards** for the industry. (emphasis added)

However more important than a discussion of these costs are the *implications for implementation* of these costs. It is one (easy) thing to say utilities will voluntarily meet these standards, but it is another to be in the board rooms when someone has to authorize the money to be spent--and continually spent year after year in the face of what appears to be long-term low price market availability of power from the market (caused by the standard). There could be intense pressure, especially from some ratepayers, to rely more on the market.

An important element of this problem is that each utility is acting independently of the many other utilities in the region. This will be even more the case after 2011 under BPA's Regional Dialogue proposal. Any one utility that decides to rely upon the market more heavily will reap an immediate advantage. This is a recipe for a "Tragedy of the Commons" (and eventually, inevitable boom-and-bust commodity market-) behavior. Consumers will pay the price for inadequate power supplies that will most likely be greater than wise utility investments in reserve capacity. Strong rules and penalties, on the other hand, will level the playing field and allow each utility to take the appropriate actions necessary to meet the standards.

The Coalition is concerned that the difficulty of this whole effort has been vastly underestimated and underrepresented. That over-optimism has allowed the Forum to be satisfied with a very weak implementation plan. We hope the Council will not wear similar rose-colored glasses during this review.

Recommendation #2. The Council should re-title this paper a "Reporting and Early Warning Mechanism." Implementation should be sent back to the Forum with instructions to put together a stronger implementation plan.

The Coalition is strongly opposed to the paper's inadequate recommendations regarding Bonneville, since its recommendations will strongly influence BPA's Regional Dialogue outcomes. BPA will be transferring its load growth obligation to its utilities, so its Regional Dialogue contracts will be the only means to enforce an adequacy standard. The recommendations in this paper call for a very passive relationship, in essence counting on the optimistic view that utilities will voluntarily act unlike competitive actors. It instead assumes they will put aside their individual interests in order to spend a lot of money to work in the public interest. It is good to be hopeful, but we would want a strong backup plan in place if that optimism turns out to unwarranted. This proposal does not provide much of a backup plan. It is mostly a communication and dialogue plan. The presumption being that once the region is aware of a problem it will take action as a whole unit. This approach has not really worked on the transmission side with specific lines needed but not enough players willing to step up and make the investment. All parties seem to look to each other to make the investment.

Recommendation #3 Bonneville should evaluate in aggregate whether it and its utilities are meeting the adequacy standard. If not, BPA should be the backstop and acquire

resources to meet the standard. Costs of the backstop acquisition would be allocated to the utilities that are short.

The Coalition has made this recommendation since the beginning of this process, and we still believe it is a simple solution for the utilities buying from the federal system. In essence BPA's utilities (and its own Tier 2 business) would have to demonstrate that they had sufficient resources. If not, BPA would acquire them on their behalf. Since this arrangement would have to be incorporated into BPA's post-2011 contracts, that will be negotiated in the coming months, the region cannot wait and see if a purely voluntary approach will work. The backstop must be included in those contracts, but only triggered if the voluntary approach is proving inadequate.

NW Energy Coalition appreciates this opportunity to comment and will remain involved in the Forum. We believe the progress the Forum has achieved is notable, but the implementation plan is completely inadequate without stronger assurances that, if voluntary compliance turns out to be insufficient, the region, especially BPA, has the ability to remedy the lack of resources.



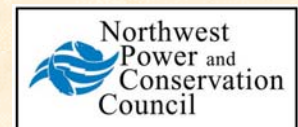
PNW Resource Adequacy Implementation Plan

Power Committee
November 14, 2006
Couer D'Alene, Idaho

Outline

- The Implementation Plan
 1. Acquiring resource and load data
 2. Assessing the status of the power supply
 3. Comparing the status to the adequacy standard
 4. Taking appropriate actions, if necessary
- Expectations about Bonneville contracts
- Outcomes in actual operations

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Implementation Plan

Step 1 – Acquiring Data

- Consistent with existing utility reporting
- PNUCC will continue to collect data
- Outstanding issues
 - Standardize counting conventions for resources
 - Standardize counting conventions for conservation
 - Standardize counting for planned resources
 - Refine definitions for capacity reporting
 - Some confidentiality issues yet to be resolved

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Implementation Plan

Step 2 – Assessing the Status

- PNUCC will assess the power supply status from a “bottom-up” approach – aggregating data received from individual utilities
- The Council will assess the power supply status from a “top-down” approach – using its own regional load assessment and resource data
- Differences in the assessed status will prompt a review of the data and in cases where differences are warranted, an explanation of the results

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Implementation Plan

Step 3 – Comparison to Standards

- The status of the power supply 3 and 5 years into the future will be compared to the “physical” energy and capacity standard adopted by the Council.
- The Council will also compare the power supply status to its “economic” standard defined in the Fifth Power Plan.
- The Forum may choose to develop its own “economic” standard at some future time.

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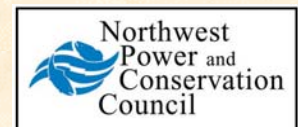


Implementation Plan

Step 4 – Taking Actions

- No action if physical and economic standards are met.
- **“Yellow light”** warning, if the economic standard is not met in either the 3rd or 5th year or if the physical standard is not met in the 5th year.
- **“Red light”** warning, if the physical standard is not met in the 3rd year.
- A “red light” warning triggers
 - A process to validate the data
 - A heavily publicized report
 - Instigation of public meetings to consider possible actions

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Implementation Plan

Other pieces

- Expectations about Bonneville contracts
 - Load and resource reporting requirements
 - Affirmation by customers that they understand their adequacy obligations and that there will be no Bonneville backup service
 - Three-year notice for taking further Bonneville service
- Outcomes in actual operations
 - Dependent on actual water conditions
 - Utilities that are short in actual operations face high prices and any environmental mitigation responsibilities