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May 3, 2005

MEMORANDUM

TO: Council Members

FROM: Dick Watson

SUBJECT: Bonneville's Draft Closeout Report: BPA's Proposed Changes to Power Function Review Base Costs for conservation

Bonneville's Power Function Review was the process through which Bonneville laid out its initial assumptions regarding the various cost components going into the FY 2007-FY 2009 rate case. In its April 26 letter, the Council commented on those initial assumptions and raised concerns that Bonneville was not planning on sufficient funding to achieve Bonneville's share of the 5th plan's conservation targets.

Today, Bonneville released the Draft Closeout Report in which they document the changes they propose to make to their base costs. The section pertaining to conservation is attached. We have not yet analyzed the report in detail, but our initial reaction is that the bottom line is unchanged and that level of funding is unlikely to achieve Bonneville's share of the 5th plan's target.

Bonneville is taking comment on the Draft Closeout Report through May 20. Staff will provide a more detailed review of the proposed changes and a suggested response later in the week.

Draft Closeout Report: BPA's Proposed Changes to PFR Base Costs

CONSERVATION PROGRAM

	Average Expense	Average Capital
FY 2002-2006 Conservation Program (including rate credit)	\$66 M/yr	\$27 M/yr
FY 2007-2009 PFR Base Forecast	\$71 M/yr	\$32 M/yr
FY 2007-2009 Proposed PFR Forecast	\$70 M/yr	\$28 M/yr

The portfolio of energy efficiency programs BPA is proposing for the post-2006 period is very similar to what is currently available. BPA relied heavily on the Post-2006 Conservation Workgroup's recommendations in designing its proposed program approach. The key features of the proposed program are as follows:

1. a **rate credit program** (similar to the current C&RD with key changes, such as paying for only cost-effective measures, BPA incentives based on a % of what it costs to install measures and not value to the system, and requiring that measures be incremental, measurable, and verifiable with appropriate oversight and more frequent reporting);
2. a **bi-lateral contracts program** for our utility and federal agency customers (similar to the current ConAug program);
3. a **3rd party bi-lateral contracts program** for cost-efficient, region-wide approaches (similar to the VendingMi\$er program and includes BPA's support for the NEEA);
4. support of critical **infrastructure** elements, especially evaluations so we know if we are getting what we are paying for;
5. a separately funded **renewable resource option**; and
6. a proposed spending amount of **\$75 million/year** to capture BPA's 52 aMW/year share of the Northwest Power and Conservation Council's (Council) regional cost-effective conservation target at an overall cost of **\$1.4 million/aMW**.

Through the PFR process, several areas where decisions are yet to be made were identified as either potential savings or increases to the Conservation spending level from the PFR base. Each of these areas were discussed and taken into consideration when developing the proposed FY 2007-2009 Conservation forecast.

Possible Decreases Identified

1. **Proposal: Credit conservation done by utilities "on their own nickel" against BPA's target, reducing BPA's spending** - BPA's conservation target is based on cost effective conservation as defined in the Council's 5th Power Plan and reflects only loads BPA serves. Also, BPA serves only a fraction of some public utilities' loads. BPA agrees that if those utilities are effectively meeting some of BPA's target through their own non-BPA funded programs, then BPA should not separately forecast for the same conservation MWs. BPA does not believe that currently there is enough information on how much cost-effective conservation public utilities are accomplishing on their own to warrant

forecasting a reduction now. However, BPA will track this going forward and adjust its forecast accordingly. If this can be done before final studies are done for the FY 2007-2009 rate period, this adjustment will be made before the final rate decisions are made. **Draft Conclusion: Do not include this reduction in Initial Proposal, but possibly include it in final rate studies.**

2. Proposal: Reduce BPA target for “naturally occurring” conservation - BPA originally set the target at 40%, which is roughly the percent of the regional load BPA serves (7,782/20,472 aMW= 38% based on FY 2003 White Book information). This calculation is fully consistent with the methodology for setting conservation targets in this FY 2002-06 period, as agreed to between BPA and the Council. After consultation with the Council’s staff, BPA estimated which specific measures are likely to become standard practice in absence of any BPA/utility conservation programs. Based on this analysis, BPA estimated that roughly 7% of the Council's targets would be naturally occurring. Seven percent equates to roughly 4 aMW out of BPA's 56 aMW annual target. Based on the loads BPA serves, our share of the Council’s regional target over the FY 2007-2009 period is 168 aMW (40% of 420 aMW). This equates to an annual target of 56 aMW. We anticipate that the “naturally occurring” conservation will come in at about 7% or 4 aMW/year. This would give us a 52 aMW/year target and a 156 aMW target over the 2007-09 period. While there has been some comment that the Council has set too high a target for conservation, BPA believes it appropriate and achievable. The Council conducted an extensive public process as conservation potential was analyzed, and BPA and many others in the region participated in that process. Thus, BPA concludes the 52 aMW per year is the right target. **Draft Conclusion: Include \$4 million annual capital and \$1 M annual expense reductions in the rate case initial proposal.**

3. Proposal: Don’t require load decrement on rate credit - PFR participants commented that it will be harder for BPA to meet its MW targets for conservation within its spending level limit if it requires block and slice customers to reduce their load on BPA by the amount of conservation they accomplish under the conservation rate discount program. Consistent with the advice of its Post-2006 Conservation Workgroup, BPA has now proposed not to require load decrements from slice/block customers under the rate credit program, but continuing to require load decrements under the new bi-lateral contract program. **Draft Conclusion: Make the change recommended, but no reduction in costs.**

Possible Increases Identified

4. Proposal: Do not count IOU conservation BPA pays for toward BPA’s target, or count these MW’s but also add IOU residential conservation to BPA’s target - BPA proposes to count toward the 52 aMW annual target any cost effective conservation it helps ensure through its funding mechanisms, including the conservation achieved by IOUs under the rate credit program and the conservation accomplished by our Northwest Energy Efficiency Alliance (NEEA) funds. This decision is consistent with the current way we count delivered savings toward our share of the Council’s target in the rate period as agreed to by Council staff. Further, BPA invests in regional conservation that is currently counted toward BPA targets, e.g., NEEA market transformation. Counting

conservation funded by IOU rate credits is fully consistent with the methodology we use in this rate period, and should be extended to the FY 2007-2009 rate period. If BPA pays for it, BPA should count it toward our targets. **Draft Conclusion: Count IOU MW's and add to target, but no cost increase.**

5. Proposal: Increase spending to increase certainty of meeting conservation targets -

BPA acknowledges that the \$1.4 M/aMW target is a stretch. Based on recent conservation program performance and given the changes that have been made in the designs of the proposed program portfolio, BPA believes it has a reasonable chance to achieve its share of the Council's new conservation aMW targets with the proposed spending level. It is important to note that while BPA is targeting \$1.4 M/aMW, that figure is an average of different program spending levels. BPA has been successful at lowering the cost of savings through the Con Aug Program, and BPA will seek to continue to average program costs in the revised bilateral contracts at the current level (\$1.2 M/aMW). Similarly, the NEEA has a demonstrated track record of \$1 M/aMW. This leaves the budgets for local initiatives higher (\$1.7 M/aMW). Thus, the success to date with driving down program costs and continuing to adapt new marketing strategies leads BPA to believe these forecasted targets are achievable. Just as important, BPA believes that setting and meeting aggressive costs containment goals is important both to keep rates down and to maintain support for steady conservation funding, since higher costs per MW make conservation spending levels less sustainable during periods of even greater financial stress. BPA will assess progress towards our aMW conservation goal and proposes to adjust for underperformance against the target in the next rate period. **Draft Conclusion: Keep funding at current forecast.**

6. Proposal: Increase spending level for administrative costs - BPA is proposing to pay up to 10% of administration costs under the new rate credit and bilateral contracts program. The Conservation Workgroup recommended 20% of administrative costs be included. The current C&RD credit allows credit of 20% for administration cost to support infrastructure building. For ongoing conservation programs, however, administration should be lower. A number of utilities and end users that are partners in capturing the regional conservation have told BPA they don't need a full 20% administration for on-going programs. BPA has included a number of activities and tools that should reduce utility administration costs (e.g., standard program design templates and marketing materials, mechanism for utility sharing, etc.). However, BPA received numerous written comments on this topic shortly before issuing this report and will consider them during the comment period. **Draft Conclusion: Keep funding at current forecast.**

7. Proposal: Increase spending level for conservation infrastructure - The Conservation Workgroup recommended a 2% infrastructure spending level (i.e., \$1.6 M/year). BPA has proposed instead conservation spending levels for FY 2007-2009 that includes \$1 M/year for the infrastructure spending that should be sufficient to cover these activities. The 2% infrastructure support forecast was not based upon detailed analysis and budgeting. More detailed analysis developed by BPA leads the Agency to conclude the necessary infrastructure support can be accomplished at the \$1 M/year level. The \$1 M/year is a component of the \$75 M/year proposed conservation acquisition program level. **Draft Conclusion: Keep funding at current forecast.**

Table 1: Proposed Conservation Program Annual aMW Targets and Spending Levels

<u>Program</u>	<u>aMW</u>	<u>Forecast</u>	<u>Cost/aMW</u>
Rate Credit (at 0.5 mills = \$42M*/year with IOUs and Pre-Subers included)	21	\$36M	\$1.7M
Utility & Fed. Agency Bi-Lateral Contracts	15	\$21M	\$1.4M
3 rd Party Bi-lateral Contracts	6	\$7M	\$1.2M
Market Transformation (via NEEA)	10	\$10M	\$1.0M
Infrastructure Support and Evaluation	---	\$1M	---
Total	52	\$75M	\$1.4M

* - assumes \$6M/year of the \$42M/conservation rate credit will be spent on renewables .

In total, BPA proposes to reduce the base PFR spending levels (both capital and expense) for achieving the Council's cost-effective conservation target by \$5 M/year to \$75 M/year (includes the conservation rate credit), which is a portion of the overall Conservation forecast of capital and expense spending. The proposed spending level is an actual increase of \$5 M/year over the average annual spending level in the current rate period.

Table 2: PBL Total Proposed Conservation Forecast FY 2007-2009

<u>Program</u>	<u>Proposed Forecast</u>	<u>Annual MW Target Spending</u>
Generation Conservation Expenses	\$34.0 M	
EE Development (Reimbursable)	\$12.9 M	
Energy Web/Non-Wires Solutions	\$1.0 M	
Technology Leadership	\$1.3 M	
Legacy (Contract closeout after FY 2000)	\$2.8 M	
Low-Income Weatherization	\$5.0 M	
Market Transformation	\$10.0 M	YES
Infrastructure Support and Evaluation	\$1.0 M	YES
Conservation Rate Credit	\$36.0 M	YES
Expense Total	\$70.0 M	
Generation Conservation Capital Total	\$28.0 M	
Utility & Fed Agency Bi-Lateral Contracts	\$21.0 M	YES
3 rd Party Bi-lateral Contracts	\$7.0 M	YES

BPA Proposals Proposed PFR Base FY 2007-2009

(Reductions)/Increases

Reduce Conservation Expense Spending Level (\$1 M/year)

Reduce Conservation Capital Spending Level (\$4 M/year)

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