

## GTH UPDATE Energy

### BPA PROPOSES TO SHARE THE PAIN OF OVER-GENERATION

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On February 7, 2012, the Bonneville Power Administration ("BPA") issued a proposed "Over-Supply Management Protocol" to address over-generation events like those that caused BPA to force curtailments of wind generation in each of the last two years.

In a major departure from prior policy, BPA will now pay wind generators to curtail production if necessary to maintain compliance with Total Dissolved Gas ("TDG") standards at federal hydroelectric dams. The costs of such curtailments will be split 50-50 between BPA's power customers and wind generators operating in BPA's control area. Comments on the BPA proposal will be accepted through February 21, 2012.

#### THE OVER-ABUNDANCE PROBLEM: WIND GENERATION COLLIDES WITH FISHERIES CONSERVATION

In past years, non-hydro generators in the Pacific Northwest generally shut down in the spring, when high flows on the Columbia River system resulted in cheap and plentiful electric power from the federal hydro system. Shutting down thermal generators to perform maintenance in the spring made sense because BPA could provide replacement power below the marginal cost of production for those generators. Such shut-downs also kept the regional power system in balance.

With the rise of wind power in the Pacific Northwest, however, this picture changed. Not only is wind generation non-dispatchable – that is, wind generation is produced when the wind blows, not when it is required to meet loads – but wind generators also lose significant revenues if they do not produce. Specifically, the federal Production Tax Credit, which has been a key economic driver of Northwest wind expansion, is paid only if power is produced. In addition, power purchase agreements for wind generation commonly provide that the generator is paid only if power is produced, and, in some cases, the generator may be subject to significant penalties if power production targets are not met. Hence, unlike thermal generators, curtailment of wind production produces significant costs for generators even if BPA provides free replacement power.

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This problem came to a head in the spring of 2010 and again in 2011 when BPA ordered significant curtailments of wind generation in its control area during periods of high water in the Columbia Basin. BPA's only other option – to run water over dam spillways rather than through turbines – could not be exercised because spilling water over dams would increase Total Dissolved Gases (“TDG”) in the water, causing the federal dams to violate TDG limits established under the Clean Water Act. Exceeding total dissolved gas limits threatens to harm fisheries, including endangered salmon and steelhead runs, through gas bubble trauma, the equivalent of “the bends” in human divers.

### **BPA’s “ENVIRONMENTAL REDISPATCH” POLICY SPAWNS LITIGATION**

Prior to the spring run-off period in 2011, BPA announced an “Environmental Re-dispatch Policy,” which provided that, if conditions warranted, BPA would provide free power to non-federal generators and would order them to curtail production if necessary for federal hydroelectric dams to stay within TDG limits. But, BPA concluded, it would not pay “negative prices” – that is, it would not pay generators to curtail production -- and it would not pay wind generators damages if they lost revenues from Production Tax Credits or contractual commitments due to curtailments ordered by BPA.

In July 2011, a group of wind generators challenged BPA's Environmental Re-dispatch Policy in a complaint filed at the Federal Energy Regulatory Commission (“FERC”). On December 7, 2011, FERC issued an order concluding that BPA's Environmental Re-dispatch Policy violated FERC's open access policies and improperly discriminated against wind generation in violation of Section 211A of the Federal Power Act. This marked the first time FERC had exercised its power under Section 211A.

FERC's decision also proved extremely controversial. For example, on January 24, 2012, nineteen members of the Pacific Northwest Congressional delegation sent a letter to Energy Secretary Chu suggesting that FERC had overstepped its authority in issuing the December 7 order and should have deferred to ongoing efforts in the region to address the over-generation problem.

### **BPA’s “OVER-SUPPLY MANAGEMENT PROTOCOL” PROPOSAL**

On February 7, 2012, BPA responded to FERC's December 7 order by proposing a new “Over-supply Management Protocol,” which will replace its Environmental Re-dispatch Policy. Under the Over-supply Management Protocol, BPA proposes to pay regional wind generators to curtail production if necessary to avoid TDG violations at federal dams. The costs of such payments will be recovered from BPA's power supply customers (generally, public power agencies) and wind generators operating in BPA's balancing authority, split on a 50-50 basis.

Specifically, the Over-supply Management Protocol would:

- Pay wind generators to curtail production if other options, such as curtailing the region's thermal generation and modifying operations of the federal hydro system, have been exhausted.
- Payments will be based on a "cost curve." That is, BPA will identify the generators available for curtailment on a least-cost to highest-cost basis, and will order curtailments starting with the cheapest generator and stopping when sufficient curtailment has been achieved.
- To assemble the cost curve, generators in BPA's control area will be required to submit their per-MWh costs of generation upfront, subject to audit, adjustment, and penalties if the costs are overstated. The BPA policy provides a formula so that generators can identify their costs under various scenarios, such as selling unbundled Renewable Energy Credits ("RECs") under contract, selling RECs on the market, or selling a bundled product, and also provides guidance as to how the costs of lost PTCs and other incentives are to be factored into the cost claim.
- The costs of any curtailments ordered by BPA will be split 50-50 between users of the Federal Base System (predominantly public power utilities) and wind generation customers located within BPA's control area. BPA will not pay negative prices to wind generators outside its control area based on the fear that generators could use publicly-available information on river flows to withhold power from BPA at strategic moments, forcing BPA to pay extreme prices to obtain sufficient curtailments.
- Existing generators will be required to participate in the curtailment pool, but future generators will have the option of either, participating in the curtailment pool and paying their fair share of the curtailment costs, or else not participating in curtailments and not being subject to the cost allocation.
- For this year, BPA will pay the costs of any necessary curtailments from its Transmission Business Line reserves. For future years, BPA will set rates using the process specified in Section 7(i) of the Northwest Power Act (the usual mechanism for setting rates), to reflect the 50/50 cost split.
- Of particular significance, the proposed policy indicates BPA intends to file an Open Access Transmission Tariff ("OATT") that complies with FERC requirements by the end of March. BPA has not had a FERC-conforming OATT for several years, a source of considerable controversy in the region.

#### **NEXT STEPS AND DEADLINES**

- BPA will take comments on the Oversupply Management

Protocol proposal through February 21, including a workshop on the proposal on February 14 (certain to be a Valentine's Day treat!).

- BPA will then file the proposal, including its response to comments, with FERC on March 6, the deadline specified in FERC's December 7 order.
- For years 2013 through 2015, BPA will carry out a Section 7(i) rate proceeding so that the 50-50 cost split contained in its proposal can be reflected in its power and transmission rates. For 2012, BPA proposes to fund any curtailments from its existing Transmission reserves, but those costs will be recovered from future ratepayers as identified in the Section 7(i) process.
- Petitions for rehearing of FERC's December 7 order have been filed by many Pacific Northwest parties and remain pending at FERC. It is unclear what effect the BPA proposal will have on FERC's ultimate disposition of these rehearing petitions.
- There is also a lawsuit in the Ninth Circuit challenging BPA's Environmental Re-dispatch decision. It is also unclear what effect the BPA proposal will ultimately have on the Ninth Circuit litigation.

## DOCUMENTS

Documents concerning BPA's Oversupply Management Protocol are [available here](#).

The attorneys at Gordon Thomas Honeywell have extensive experience in all areas of the energy and utility industries, including regulatory matters, project development, renewable energy, power purchase agreements, REC purchase agreements, transmission, taxation, municipal law, cooperative law, public records requests and general operations.

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