

COMMENT SHEET
CVP COST ALLOCATION MEETING OF JUNE 29, 2012

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Comments:

NCPA provides the following comments on the material presented at the June 29, 2012 meeting:

1. Flood Control: NCPA is supportive of the use of the "rule curve" methodology presented at the meeting regarding the sizing of the single purpose alternatives (SPA), the facilities to be analyzed, and using the cost curve model to re-price the SPA. The same re-pricing cost estimate methodology needs to be used for each SPA and multipurpose without one project purpose analysis to ensure consistency and an equitable comparison amongst all project purposes.

2. Navigation: The Central Valley Project authorization act stated that the primary purposes of the project are river regulation, improvement of navigation, and flood control. If navigation benefits are no longer being provided by the project, then we agree that future costs should not be assigned to that purpose. The purpose of this cost allocation is to align the current and future benefits of the project with the costs of the project.

3. Recreation: The CVP provides significant recreation benefits even though the Solicitor's office of the Department of Interior has concluded that recreation is not an expressly authorized purpose of the CVP. NCPA believes Reclamation's cost allocation process needs to recognize the value of these benefits and assign CVP multipurpose joint costs to recreation commensurate with those benefits. Allocating costs to recreation should follow the same concept Reclamation proposes for navigation; allocate costs to beneficiaries based on the projected benefits to be received.

If legislative action or some other vehicle is needed to recognize recreation as a project beneficiary, then that course of action should be pursued. NCPA understands that, pursuant to the McGovern amendment, any cost allocation changing the method and manner in which joint project costs are reassigned requires Congressional approval. Reclamation should include recreation in the cost allocation as a CVP project purpose and disclose to the appropriate

Congressional committees that costs are allocated to recreation in accordance with the benefits received. Since recreation benefits are obviously provided by the CVP, an appropriate share of the costs should be allocated to that beneficiary.

4. Power: Under the methodology section in Reclamation's CVP Cost Allocation Study Draft Assumptions and Approach, the Separable Costs Remaining Benefits (SCRB) allocation method must use the most economic SPA that generates the same benefits as the multipurpose project. Reclamation has proposed using hydropower facilities as the power SPA, but that proposal does not meet the SCRB criteria of being the most economic alternative. Gas fired thermal plants will be substantially lower in cost than building large hydropower units and should be used to determine the SPA.

Reclamation proposes to utilize the PLEXOS model to determine power benefits by estimating the cost of power "avoided" by the generation of the CVP system. That approach determines the marginal cost of the Western Interconnection for a specific capacity and energy quantity, not the benefits derived from CVP generation. CVP generation is base load "must take" power, not the marginal last units to be placed on the system to meet load.

The proposed modeling does not take into account the hourly variability of the CVP product. Customers are only allowed to schedule the CVP resource two days in advance and have to pay Western to firm that scheduled energy because generation changes on an hourly basis, sometimes dramatically. During flood control operations the generation can fluctuate from more than 1500 megawatts to a few megawatts on very short notice. Even in normal operations water releases change constantly to meet river regulation, water quality, temperature, and other requirements, changing the quantity of generation. In addition there are days, weeks and sometimes months when CVP generation is not even sufficient to meet project use load. Preference power customers are required to pay for energy purchased from the market to support the project use load, while receiving no energy or capacity from the CVP.

The PLEXOS model also proposed using a mix of thermal and renewable resources. The CVP, because it is large hydro, is not considered a renewable resource and any use of renewable resources distorts the value of the benefits provided by the CVP. Similarly, power customers do not receive carbon cap and trade allocations for CVP generation and thus do not receive any carbon emission benefits from the CVP product.

Customers develop a portfolio of resources to meet their forecasted load several months in advance of the actual delivery date. The CVP resource is always different from the amount forecasted. When the available CVP energy exceeds the forecasted energy customers sell other contract energy to the market to balance their resources with customer demand. If the generation is short of the

forecasted amount they purchase additional energy from the market. The value of those purchases or sales is based on the California Independent System Operator (CAISO) market hourly price.

Most customers schedule energy from the CVP based upon the hourly price of the CAISO energy market and the associated transmission congestion prices. Western sells ancillary services to its customers based upon the CAISO market price and receives the market price for selling excess CVP generation to the CAISO. The CAISO market price determines the benefit value the power customers receive for CVP generation.

The power SPA should be developed using a thermal gas plant and the power benefit evaluation should be based on a forecast of CAISO energy values. Modeling the “avoided cost” measured on a regional scale does not yield a result that corresponds to the power benefit provided by CVP hydro generation.

Another critical determinant in the cost allocation is the amount of power that will be generated from the CVP system in the future. The proposed Delta Flow Criteria of seventy-five percent of unimpaired flows reduces CVP generation by approximately thirty percent. In addition, the recent decision by Reclamation to release additional water down the Trinity River above that required in the Record of Decision reduces generation and water deliveries. Forecasted generation and water deliveries determine project benefits and the forecasts need to account for future operational changes.

5. Water Quality: The costs for providing water quality standards above the standards of SWRCB Water Rights Decision 1485 shall be non-reimbursable. Reclamation interprets the language to say there are no additional costs incurred to meet water quality conditions above D-1485; therefore no costs will be allocated to water quality. That argument could be made for any project purpose, since it can be argued that multipurpose costs are incurred for dam operation with no additional costs for any project purpose.

A cost allocation is based on the benefits received by project purposes, not additional costs that may be incurred or avoided. Clearly water quality receives benefits from the current operation of Folsom, Shasta and Trinity Dams in addition to New Melones and those benefits need to be used in the cost allocation to determine water quality’s appropriate share of CVP costs. Thus, both CVP capital and O&M costs should be allocated to water quality to recognize the benefits provided.

6. Fish and Wildlife: While construction of the CVP affected fish and wildlife, the reality is substantial development would have occurred in the Central Valley even without its construction. The Central Valley has great climate and abundant streams, which attracts people to the area. Even in areas untouched by the CVP significant population growth occurred. Fish and wildlife encroachment would

have occurred with or without the CVP and CVP customers have made contributions to improve fish and wildlife habitat.

CVP users have contributed significantly more dollars per capita than any other Central Valley resident to restore the fish and wildlife in Northern California. Almost \$1.5 billion has been spent on Central Valley Project Improvement Act (CVPIA) projects and another \$1 billion or more spent in CVP expenditures on fish and wildlife activities.

Reclamation proposes to release water down the Trinity River this year far in excess of the natural unimpaired flows; this is another clear example of fish and wildlife enhancement provided by the CVP. The cost allocation needs to recognize the fish and wildlife improvements that have been provided by the CVP and allocate costs to fish and wildlife accordingly.

7. Period of Analysis: Reclamation has stated that they will evaluate benefits for 50 years into the future but if the benefits do not exceed the SPA then historical benefits will be evaluated back to 1980. The purpose of updating the cost allocation is to align the project costs with the benefits resulting from the future operation of the project. Costs have already been allocated based on the past benefits developed by the project.

CVP power costs have to be recovered by future energy deliveries and the project power benefits need to be aligned with those projected deliveries. Using historical benefits means that customers have to pay twice for those benefits – once in the historical deliveries they received and again in the future deliveries. Placing additional costs on power for benefits already repaid will probably make the CVP power uneconomic. Power benefits should correspond to the future operation of the project, not the historical operation that no longer exists.

A clear example of why using historical benefits does not work is navigation. Reclamation states there are no future benefits attributable to that project purpose. Yet if historical benefits were used, costs would be allocated to navigation in the current cost allocation study. If navigation was a reimbursable function, how would Reclamation collect revenue from a beneficiary that no longer exists? If future benefits are less than the projected costs of the project, that revelation should not be swept under the rug by including old benefits from CVP operations that no longer exist. Instead the financial viability of the CVP should be clearly stated and cost allocation alternatives developed to deal with the circumstance that current project operations have reduced benefits below costs.

8. Finally, the Central Valley Project Improvement Act (CVPIA) contributions from power and water need to be treated as specific costs in the cost allocation process. These contributions are mandated requirements for receiving CVP

power and water and need to be subtracted from the justifiable expenditure in determining the remaining justifiable expenditure.