



C11-20

BC HYDRO F2020-F2021 REVENUE REQUIREMENTS EXHIBIT C11-20

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August 2, 2019

Mr. Patrick Wruck
 Commission Secretary and Manager
 Regulatory Support
 British Columbia Utilities Commission
 Suite 410, 900 Howe Street
 Vancouver, BC V6Z 2N3

Dear Mr. Wruck:

RE: British Columbia Utilities Commission (BCUC or Commission)
British Columbia Hydro and Power Authority (BC Hydro) and Powerex Corp
(Powerex) 2019 Letter Agreement Application

BC Hydro writes to file with the Commission a letter agreement between Powerex and BC Hydro that provides for the forward sale and delivery of wholesale electricity by Powerex to BC Hydro (**2019 Letter Agreement**). The 2019 Letter Agreement is an "energy supply contract" (**ESC**) within the meaning of that expression in the *Utilities Commission Act (UCA)*. The agreement was executed on June 6, 2019, and is filed within 60 days of that date pursuant to the Commission's Rules for Energy Supply Contracts for Electricity. The 2019 Letter Agreement is attached as Appendix 1 (a redacted copy in the public filing; an un-redacted copy in the confidential filing).

BC Hydro seeks a determination from the Commission that the 2019 Letter Agreement is in the public interest, and an order accepting it as filed under section 71 of the UCA. A draft order to that effect is attached at Appendix 2.

Recent amendments to the UCA have the effect that the UCA is no longer applicable to Powerex.¹ Nevertheless, the statutory obligation remains on BC Hydro to file ESCs, regardless of the statutory exemption applicable to Powerex. Accordingly, this application should be understood as one made solely by BC Hydro, despite the wording of section 71(1) of the UCA which requires both parties to an ESC to file it with the Commission.

¹ New section 1(2) of the UCA came into force on May 16, 2019, by virtue of section 10 of the *Energy Statutes Amendment Act, 2019*, chapter 24, SBC 2019.

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Relationship with 2018 Letter Agreement

On December 6, 2018, BC Hydro filed with the Commission an agreement between it and Powerex that provided for the forward sale and delivery of wholesale electricity by Powerex to BC Hydro (**2018 Letter Agreement**). The record of the proceeding regarding the 2018 Letter Agreement was made public on May 23, 2019,² and the 2018 Letter Agreement has been the subject, in part, of Information Requests in BC Hydro's Fiscal 2020 to Fiscal 2021 Revenue Requirements Application (**F20-F21 RRA**).³ The 2018 Letter Agreement was accepted for filing pursuant to section 71 of the UCA by Order E-15-19.⁴

The 2019 Letter Agreement is quite similar in form and substance to the 2018 Letter Agreement. Both are enabling agreements that allow BC Hydro to acquire forward physical wholesale electricity to manage potential electricity shortages in the operational time horizon.⁵ However, there are some important differences between the two agreements. In light of intervenor and Commission awareness of the 2018 Letter Agreement, and to avoid misunderstanding, BC Hydro notes the differences between the two at the outset of this application as follows:

- The 2018 Letter Agreement was a short term arrangement in effect for only seven months (December 1, 2018, to June 30, 2019); the 2019 Letter Agreement is a longer term arrangement in effect until terminated by either party. That is, the 2019 Letter Agreement does not have a fixed term or expiry date;
- The 2018 Letter Agreement was entered into to respond to an impending electricity supply issue that arose; the 2019 Letter Agreement was entered into proactively to ensure appropriate measures are in place should similar supply issues arise from time to time and generally to allow BC Hydro to manage the type of risks that led to the 2018 Letter Agreement in a timely way (any purchases that BC Hydro has made under the 2019 Letter Agreement will be disclosed as discussed below in the section titled "Reporting". BC Hydro will also be providing an updated forecast cost of energy confidentially to the BCUC in the F20-F21 RRA Evidentiary Update to be filed on August 22, 2019 and provided publicly on October 18, 2019). A more fulsome discussion of the rationale for the 2019 Letter Agreement is provided below; and

² Available at <https://www.bchydro.com/content/dam/BCHydro/customer-portal/documents/corporate/regulatory-planning-documents/regulatory-filings/fep/00-2019-05-23-bchydro-bcuc-wm.pdf>.

³ See for example BC Hydro responses to BCUC IRs 1.21.xxx - 1.24.xxx, part of Exhibit B-5 in the F20-F21 RRA proceeding.

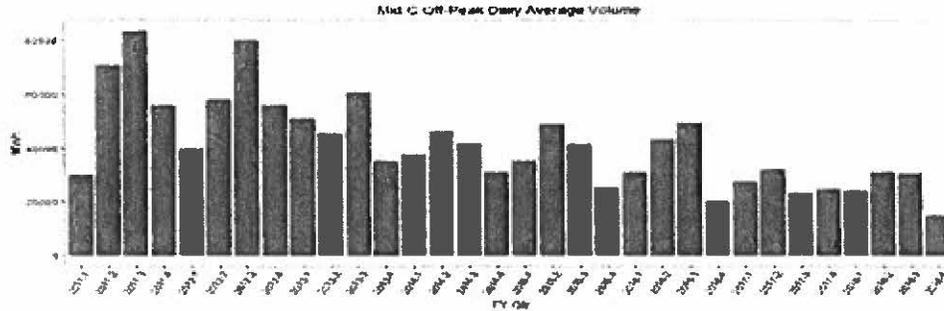
⁴ At <https://www.ordersdecisions.bcuc.com/bcuc/orders/en/item/418174/index.do?q=e-15-19>.

⁵ In response to BCUC IR 1.15.3 of the F20-F21 RRA (Exhibit B-5) BC Hydro explained the difference between the planning view and the operational view of BC Hydro's resource needs: "*In summary, the planning view reflects the capability of resources based on BC Hydro's planning criteria while the operational view shows the forecasted operation of these same resources given market and system conditions.*" The difference between the two views is the reason BC Hydro can be in surplus from a planning perspective and concurrently in deficit from an operating perspective.

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Figure 10.2: Mid-C Liquidity (Day-Ahead Off-Peak)



In summary, the impending physical supply issue in 2018/2019 was largely caused by low system inflows and the Enbridge pipeline explosion in October 2018.¹¹ The 2018 Letter Agreement was a response to those conditions and also accounted for the declining liquidity in Pacific Northwest wholesale day-ahead markets by providing for more certainty of supply through the forward physical purchases.

On a go-forward basis BC Hydro observes that, since the beginning of the current fiscal year, it has continued to have low system inflows, and has no basis to believe that the long-term decline in day-ahead market liquidity will quickly reverse itself. There are numerous other events that could result in similar supply shortfalls that threatened BC Hydro last winter, which may not reliably be addressed through purchases from Powerex on a day-ahead basis under the 2003 TPA. In these circumstances, BC Hydro believes it is prudent and in the interests of its ratepayers to have in place an additional mechanism that will allow it to respond to system conditions and reliably manage potential electricity shortages in a timely and cost-effective way. The 2019 Letter Agreement serves this objective.

Finally, it is apparent that an alternative solution to the on-going operational supply issues arising from the liquidity decline in day-ahead markets would be a revised Transfer Pricing Agreement. BC Hydro and Powerex are considering updating the 2003 TPA, including considering how the 2003 TPA might usefully be revised to accommodate forward transactions. That consideration is underway, but is not a trivial exercise because of the central role that the 2003 TPA plays in the BC Hydro-Powerex relationship. Nevertheless, and to the extent that Powerex and BC Hydro do update the 2003 TPA for that purpose, the 2019 Letter Agreement can be considered a bridging mechanism.

¹¹ Later a particularly cold winter and resulting increased heating loads exacerbated the situation.



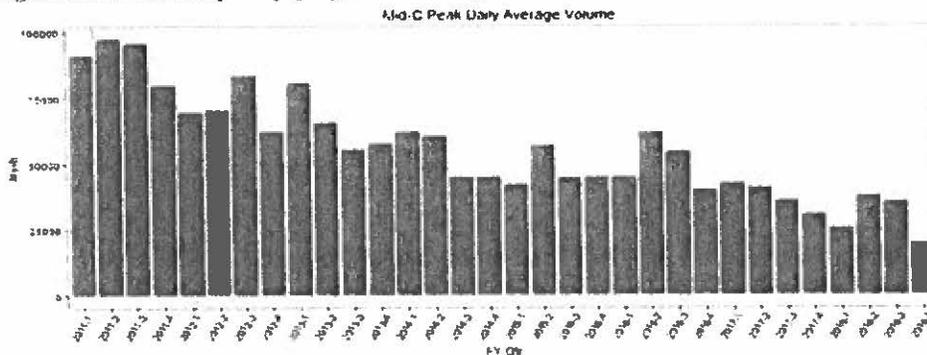
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Since 2003 BC Hydro and Powerex have purchased and sold wholesale electricity exclusively through the Transfer Pricing Agreement (2003 TPA).⁸ The 2003 TPA has proved to be a reasonably robust and relatively flexible mechanism to facilitate BC Hydro purchases of imported wholesale electricity from Powerex, and sales to Powerex for export. However, purchases and sales under the 2003 TPA are effected on a day-ahead, pre-schedule basis, and are mechanistically allocated to the account of Powerex (via the Trade Account) or BC Hydro. The 2003 TPA has worked well in the context of a consistently liquid wholesale day-ahead market for electricity in the Pacific Northwest. As such, the 2003 TPA did not provide, and did not need to provide, any mechanism for forward physical sales or purchases between BC Hydro and Powerex.⁹

Over the past decade there has been a steady decline in the volume of wholesale electricity traded on a day-ahead basis in the Pacific Northwest; that was one of the factors that prompted the 2018 Letter Agreement as a solution to the impending electricity supply issue BC Hydro faced in winter of 2018/2019, rather than attempting to rely on day-ahead purchases under the 2003 TPA. In response to BCUC IR 1.8.1.1 in the proceeding regarding that agreement, BC Hydro filed graphs showing declines in liquidity for both on-peak and off-peak hours at the Mid-Columbia wholesale electricity trading hub. Those graphs are reproduced here.¹⁰

10. Market Liquidity

Figure 10.1: Mid-C Liquidity (Day-Ahead Peak)



⁸ Subject to the 2018 Letter Agreement and now the 2019 Letter Agreement.
⁹ The 2003 TPA does provide for forward financial hedges, but not forward physical deliveries.
¹⁰ Source: Bonneville Power Administration, Southern Intertie Data Report, January 28, 2019, p. 27, at <https://www.bpa.gov/Finance/RateCases/BP-20/Models/Southern%20Intertie%20Data%20Report%20FY2018.pdf>.