Loveland Area Projects
and
Pick-Sloan Eastern Division

Drought Adder Discussion

July 2014

Overview of Component Costs

→ **Drought**

- Includes costs associated with the current drought period, using balloon-payment methodology
  - Future non-timing power purchases related to drought
  - Historical drought debt
  - Interest on drought debt (both historical and on-going)

↗ **O&M**

- Annual O&M
- Investments - Additions and Replacements

→ **Capital**

- Annual Interest on Investment
- Inflation

↘ **Interest**

- Normal Timing Purchases
- Transmission Costs

Western AREA POWER ADMINISTRATION

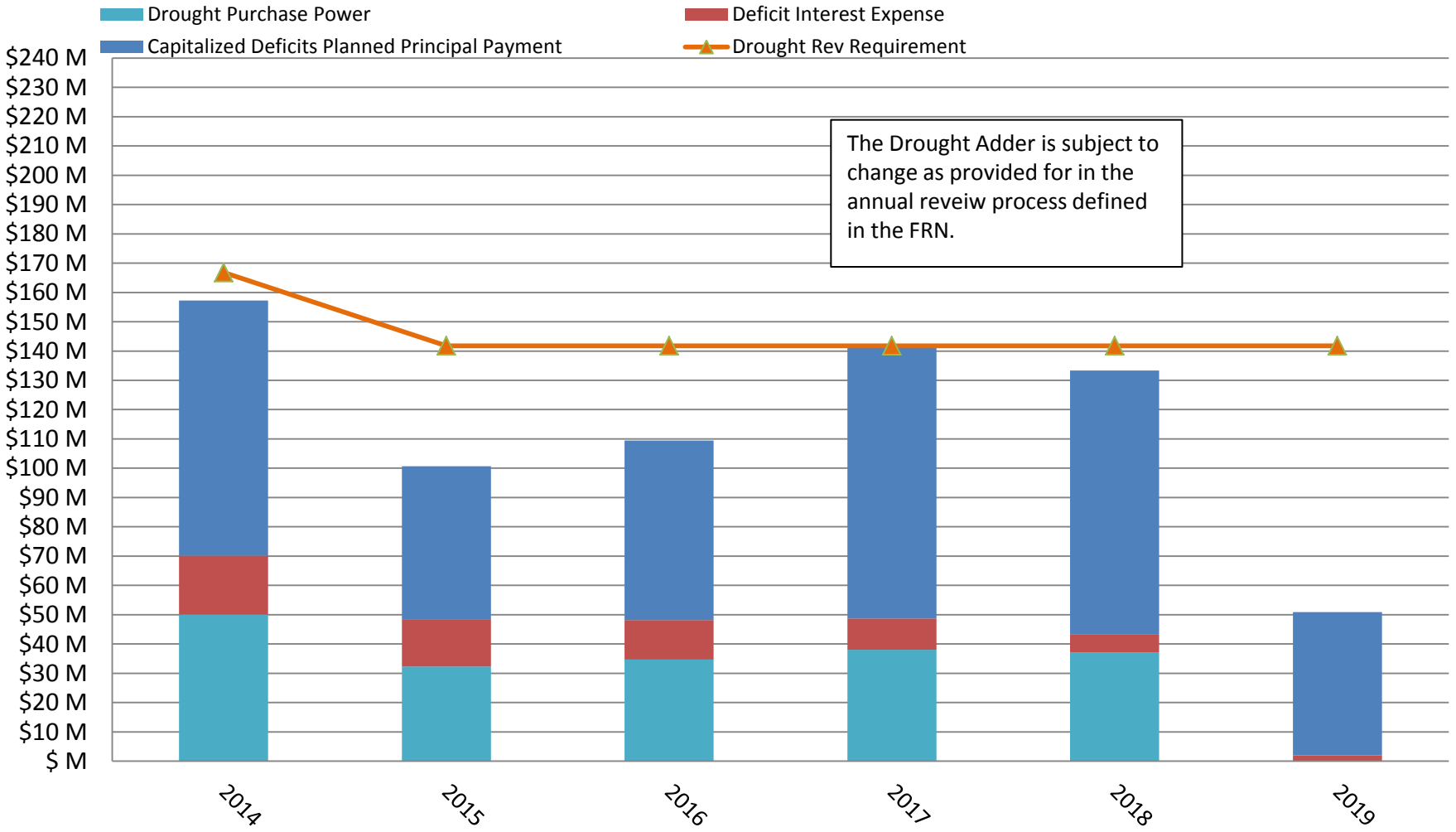
Why the Drought/Base changes for Pick-Sloan PRS

- Drought Adder is going down
  - Deficit taken was $843M vs. projected $945M
  - Deficits being paid differently than projected
    - FY 15 Rate Set PRS shows $432M unpaid as of FY 13
    - FY 10 Rate Set PRS showed $665M unpaid as of FY 13
  - Deficit projected to be totally repaid in 2019 vs. 2018
  - Projected Total Deficit Interest is now $340M vs. $384M
  - Projected Drought component is now 11.83 mills vs. 16.67 mills

- Base increasing
  - New 5-year cost evaluation period
    - New Investments/Replacements
    - New Operations and Maintenance Expenses
    - Inflationary costs

Western AREA POWER ADMINISTRATION

2015 Rate Setting Study for Pick-Sloan (ED & WD)
Planned Drought Adder Repayment by Category



Pick-Sloan
Drought Repayment

- In the FY 13/rate setting PRS, the Drought Adder component is being reduced, starting in FY 15, to $142M (11.83 mills) in order to recover all the costs assigned to the Drought Adder (deficit repayment, interest, PP) by the time the last payment on the deficit is due (2019).
- The $142M is needed in order to meet the pinch point of the drought costs in FY 2017. This causes some "over collection" of drought costs in FYs 15-16, which are used to pay down deficit and lower the FY 17 pinch.
- It's clear that after 2018 the Drought Adder could be decreased for 2019 and 2020.

Western AREA POWER ADMINISTRATION

Question

- So why does the Pick-Sloan Drought Adder Recover $878M Over the next 6 years (FYs 14-19) when the total unpaid deficit is $432M after 2013?

Answer

- As shown in slide 4, the Drought Adder not only covers deficits, but also interest on the deficits (both the historic interest associated with the first few years deficits were taken before we implemented the Drought Adder and the on-going interest) and future non-timing energy purchases.

Historical Interest

- When the Drought Adder was first implemented, the decision was made to include the historical interest associated with the deficits.
  - Roughly $282M remains in the rate after 2013.
  - Each year a portion is prorated out.
  - We are half way through the process of phasing this impact to zero.

Drought Adder Purchase Power

- 5 years of future non-timing purchases are still being included in the Pick-Sloan drought adder.
  - When the Drought Adder was first implemented
    - LAP internally defined the non-timing purchases as any purchases above the defined timing purchases of 167.2 GWh during the period of a defined drought (when LAP generation at plant, less CBT pumping, is less than 1,950 GWh for 2 consecutive years).
      - P-S WD defined the timing purchases (162 GWh) as the difference between historical actual purchases and the actual generation shortfall, plus the 66 GWh shortfall in the marketing plan and the purchases required for EI, losses, water release timing, CROD schedule timing, etc.
      - Fry-Ark is a pumped-storage project so it's operation is relatively unaffected by hydrologic conditions and much more dependent on unit availability, so its timing purchases were defined as 10% of the project's generation (5.2 GWh).
    - Pick-Sloan ED defined the non-timing purchases as **any** purchases above the defined timing purchases of 600 GWh.

Drought Adder Purchase Power Cont.

- Since LAP was, by internal definition, out of drought status in 2011, RMR stopped allocating GWh to the drought adders in the 2011 PRSs.
- Pick-Sloan ED continues to include purchases over the 600 GWh in the drought adder as per the original implementation criteria.
  - Discussion needs to take place with customers before changes can be made to the definition in order to remove the GWh from the future projections.
    - What criteria should be used to determine when Pick-Sloan ED is in and out of drought status, how/when to implement it, etc?
  - Don't want this change in assumptions to prohibit us from being able to include projections in the drought adder in the future.

FY 2013 Projection of Pick-Sloan PRS Composite Rate