

CUSTOMER COMMENTS ON COUNCIL'S DRAFT RECOMMENDATIONS REGARDING BPA'S FUTURE ROLE

INTRODUCTION

These comments are submitted on behalf of BPA's customers in response to the draft recommendations released by the Council on April 8, 2004.¹ The customers appreciate the time and effort that the Council has put into the topic of BPA's future role, and look forward to continuing to work with the Council to successfully implement a long-term change to the manner in which BPA fulfills its regional power supply obligations.

1. The Focus of the Recommendations

In its comments, the Council has focused primarily on the long-term role of BPA as a power supplier. This is the correct focus for the Council. Given the Council's statutory responsibility for the Power Plan, the long-term issues regarding BPA's power supply role are the appropriate area for the Council to provide guidance. And it is on the long-term issues that the Council can provide the most assistance to the region.

2. Rule Making to Alter BPA's Power Supply Role

The draft recommendations suggest that BPA's role be changed by a rulemaking under the Administrative Procedures Act (APA). The proposed rule would stipulate that: 1) BPA will allocate and sell power from the existing system using one rate; 2) load obligations beyond the existing system requiring additional resources will only be provided through bilateral contracts with the customer receiving the service; and 3) such additional resources will only be sold at the incremental costs of such resources. The proposed rule would be adopted in 2004, and would have the binding force of law over BPA's activities in the next rate case and in any contract negotiations. The suggested benefits of this approach are increased difficulty in modifying the policy once adopted, making it more durable, and changing BPA's role without the need for legislation. The Council is to be commended for bringing imagination to this difficult topic. However, for the reasons below, the proposed rulemaking approach will not deliver the benefits ascribed to it.

Implementing a long-term change in BPA's power supply role through a rulemaking asks regional customers to make twenty, thirty or forty year resource decisions on a policy that can be altered, or discarded, in a matter of months. The suggested rulemaking approach would offer no more durability than the status quo, i.e., a § 553 proceeding under the APA, which provides for publication of a proposed rule in the

¹ Due to the short comment period and the number of individual customers involved, these comments have not been reviewed and/or approved by governing bodies of most of the customers. As a consequence, these comments should be treated as staff level comments that are not binding on any board, governing body or utility. In addition to supporting these comments, some customers and customer groups will submit separate comments in response to the draft recommendations.

Federal Register, an opportunity to comment, and publication of the rule prior to its adoption, with no limitation on the ability of BPA to revoke or modify it. A policy, however adopted, will not provide a permanent and durable allocation upon which utilities can rely, and is not a suitable substitute for approaches that will provide durability, which include long-term, enforceable contracts and, if determined to be necessary and appropriate, federal legislation.

There are a number of other reasons why the proposed approach should be reconsidered. First, the proposed rule would make final, binding decisions on rate issues. Pursuant to §7(i) of the Pacific Northwest Electric Power Planning and Conservation Act, the Administrator is required to decide rate issues on the record developed in an evidentiary process conducted in accordance with §7(i).

Second, if the rule making is completed by the suggested deadline of 2004, it would have the force of law during the next BPA rate case. As a consequence, it would likely require that BPA implement tiered rates in that rate case. This is in conflict with the Council's recommendation that tiered rates need not be implemented in the near term.

And third, adopting now a binding policy with the force of law would lock in an allocation of the Federal power system before the nature of the allocation is known, and before customers know whether the issues of cost control, cost segregation and contract enforceability have been successfully resolved. This is putting the cart in front of the horse. Customers must be convinced that these issues have been successfully resolved before a binding commitment to allocation is made. Because without successful resolution of these issues, there would be little or no willingness among preference customers to sign a long-term take or pay contract with BPA.

Under current circumstances, the best approach would be for BPA to adopt through its normal process a policy stating a policy objective as follows:

BPA's role in providing power beyond the capability of the Federal power system should be limited to providing power to those who request it, and in a manner that assigns the costs and risks of such service solely to those who receive it.

This should be coupled with an aggressive schedule for resolving the long-term allocation, such as that proposed by the customers with their April 11, 2004 comments to the Council.

3. Offering New Long-Term Contracts as Soon as Practicable

The draft recommendations endorse offering new, long-term contracts as soon as practicable, and well before the 2011. This is a sound recommendation. An early contract offer is vital to timely resource planning by BPA's customers. However, as discussed below, the draft Recommendations do not adequately address issues of cost

separation and contract enforceability, and the overarching issue of cost control, that must be resolved if there is to be an allocation.

a. Cost Segregation, Contract Enforceability and Cost Control

Cost segregation, contract enforceability and cost control are the issues that are at the heart of a long-term allocation. An allocation is only worthwhile if it can successfully segregate costs in a manner that ensures that only those who impose incremental costs on BPA pay those incremental costs. And successfully segregating incremental costs has no value to customers if it is not memorialized in contract provisions the customer can enforce, even when it is in BPA's interest to do otherwise. A long-term take or pay contract will only be executed by customers if they have assurance that the costs they pay for the power will be controlled over the term of the contract. Hence, the resolution of the issues of cost segregation, contract enforceability and cost control are prerequisites to successfully implementing an allocation of the Federal power system.

The draft recommendations mention binding arbitration and placing revenue requirement issues in the rate case as solutions to the BPA cost control issue, and do not discuss cost segregation and contract enforceability. The suggestions contained in the draft recommendations only scratch the surface of this area. At a minimum, all three of these issues should be identified in the recommendations as areas where considerably more work must be done to resolve these matters.

4. Allocation of the Federal Power System

The Council continues to support a long-term allocation of the existing Federal power system. This fundamental change in BPA's power supply role is worthwhile, and if properly implemented, will benefit all electric consumers in the region. This continued support is warranted.

In this portion of the draft recommendations, it is suggested that an allocation be based on historic net requirements from a multi-year period and be divided into heavy and light load hour periods by month. This recommendation should be reconsidered for a number of reasons. First, the question of how each utility's allocation should be determined is a highly complex area that will involve consideration of current contract provisions, statutory requirements, and administrative practicability. This is not a policy area, but one of substantial complication and detail that can, and should, be left to the customers to resolve.

Second, the question of whether an allocation methodology is acceptable to the customers subject to it will be a matter of judgment. An allocation methodology will only be implemented if it is judged by the customers to be fair and equitable. In this regard, it presents the same issues of equity and judgment as does the issue of the benefits for the residential and small farm customer. In that instance, the Council wisely took the view that this was an area where the customers would have to judge whether the agreement achieved an equitable result. It is recommended that the Council take the

same approach regarding the allocation methodology to be used to allocate the Federal power system. Council recommendations on the details of an allocation methodology should be avoided.

a. Adjusting Allocations for Retail Load Loss

For an allocation to provide the foundation for resource planning and acquisition, it cannot be subject to reduction due to variations in the retail load. A better approach would be to use other mechanisms to address load loss in a manner that do not require reduction of a customer's allocation. An example of such mechanisms is the approach contained in the current Slice contract, which permits the customer to take certain actions to maintain its net requirement when load loss occurs. The point is that an allocation cannot be subject to reduction due to load loss if it is going to provide the customer with a solid foundation for long-term resource planning and acquisition activities.

b. Replacing Federal Power System Losses

The draft recommendation suggesting that customers be given an option of having BPA replace reductions in Federal system resources is a sound one. Giving customers the option of having BPA replace their proportionate share and charging those customers the costs of those replacement resources particularly in an allocated system, is a good approach and is supported by the customers. In such circumstances, the customers would also have the option of not having BPA replace the Federal system reduction, and replace the resource on their own.

5. Tiered Rates Are Not Recommended for Now

The Council makes the following statement regarding tiered rates in the draft recommendations:

If Bonneville's role is defined through rulemaking as described above and if new contracts can be negotiated and offered well before the end of the current contracts, the Council would not press for tiered rates under the current contracts. However, if there is not significant progress toward establishing Bonneville's role in rule and developing new contracts effecting that role, the Council would reconsider implementation options such as tiered rates.

This is a sound approach, and reserving the ability to revisit it will serve as an appropriate motivator to keep the region focused on solutions to the long-term allocation issues. Expressly reserving the right to revisit BPA tiered rates is particularly important in light of the significant issues being raised about BPA's ability to adopt a durable policy to fundamentally revised role (see discussion in Item 2 above).

6. Conservation and Renewables

The implementation of an allocation of the Federal power system through long-term, enforceable contracts will shift to customers the responsibility of incremental resources, and give them a stronger signal to acquire cost effective conservation and renewables. Combined with increased resource planning at the state and local level, this should result in greater utility emphasis on conservation and renewable resources.

There is substantial continuing value in regional assessment of cost effective conservation potential, centralized assessment of emerging conservation and resource technologies (both Council roles), and coordinated acquisition (e.g., through codes, standards, or jointly sponsored programs). BPA's role in direct acquisition of conservation and renewable resources should change. The extent of that change will depend on the specific nature of the allocation approach. For example, an allocation approach may leave BPA responsible for limited bilateral acquisition and load shaping activities that could involve continued direct, though smaller, BPA investments in energy conservation. The customers look forward to participating in discussions to flesh out alternative approaches to ensure that allocation is done in a manner consistent with the statutory priority given to conservation and renewables.

7. Resource Adequacy

The Council recognizes the issue of resource adequacy will need to be addressed in the context of a fully allocated Federal power system, and the customers agree that the Council should play an active role in this matter.

The draft recommendations suggest that resource adequacy standards might be the way to resolve this issue. This is not the best way to address resource adequacy. In the first instance, neither the Council nor BPA has the authority, under existing law, to require the construction of resources by any customer. Further, making BPA the resource policemen for the region would conflict with state regulatory and planning processes already in place, and preempt local control of resource decisions. Simply stated, the command and control regulatory model is not the best way to address this issue.

An approach that is more consistent with an allocated Federal system would be to treat failure to plan adequate resources as a matter of pricing and incremental cost assignment. So long as BPA has in place tariffs and contract provisions that ensure that those who lean on BPA pay the full costs of the resources BPA has acquired to supply to them, the market price of power will ensure that utilities take seriously the need to plan adequate resources.