October 18, 2002

Mr. Stephen J. Wright
Administrator and Chief Executive Officer
Bonneville Power Administration
P.O. Box 12999
Portland, OR 97212

RE: BPA's Power Supply Role after 2006

Dear Mr. Wright:

This letter is in response to the Northwest Power Planning Council and the Bonneville Power Administration (BPA) request for comments regarding how BPA will market power and distribute the benefits of the Federal Columbia River Power System (FCRPS) in the Pacific Northwest after 2006. As a long-term stakeholder in BPA, and with roughly half of our load served by BPA, we are keenly interested in realizing a positive and equitable outcome to the regional dialog now underway. Our comments herein are categorized in three main areas: The Joint Customer Proposal; Clarification of Subscription Benefits; and Preservation and Allocation of Benefits within the Subscription Period.

I. Joint Customer Proposal

The majority of Tacoma Power's efforts regarding Post-2006 service have been directed toward collective development of the Joint Customer Proposal. In early 2002, Tacoma Power commenced participation in the Joint Customer Proposal discussions. Our support for the process to formulate a proposal was rooted in the fundamental objectives of equitable allocation of the Federal system and equal exposure of all customers to the risks and benefits of changes to the costs of the Federal system. As the process progressed, we began to realize that the process was not driven by principles, but rather by an overwhelming desire of certain customer groups to obtain, at the expense of other customers, a long-term deal that was better than their current contracts.

Contrary to comments made by Proposal participants, the final Joint Customer Proposal did not accomplish its objectives, nor does it have the full support of public power. Tacoma Power supports the Proposal's principles and objectives, but we do not support the Proposal in its current form.

We found the proposal fundamentally violated the equitable benefits and risks principles, with certain customers gaining benefits over and above their current contracts, while other customers, such as Tacoma lost benefits over current contracts. Throughout the development process, Tacoma Power's intent was to ensure that the benefits we received under the Joint Customer Proposal were, at a minimum, consistent with the losses or gains of other parties. The following is a description of issues we felt were inequities in the current proposal.

Our key concerns with the Proposal are as follows:

<u>Allocation of the FBS</u>
The current allocation in the Joint Customer Proposal does not equitably allocate the FBS system. In light of the varying degrees planning certainties inherent in Subscription contracts, and that all customers should share an equitable degree of planning certainty under the new contracts, we believe allocation under the Joint Customer Proposal should be as follows:

- Allocation based on CY 2007 Net Requirement for Full Requirements Customers
- Allocation based on the greater of CY 2007 Net Requirement, or CY 2002 Net Requirement for Block and Slice Customers
- Surplus Firm FBS would be allocated to all customers

<u>Access to Surplus Firm FBS</u>

To the extent there is Surplus Firm FBS after net requirements are determined, the principles of equal benefits and equal risks require that such surplus be shared amongst all BPA preference customers, and not allocated to particular customer groups. While we understand the Full Requirement Customers' desire for "headroom" in the 2006-2011 period, we do not believe that special allocations of FBS for the purposes of ensuring "headroom" is appropriate in light of the equitability principles upon which the Proposal was founded. Hence, to the extent Surplus Firm FBS is available, surplus based products should be offered to all customers and not reserved solely for the special use of Full Requirements customers. In addition, any Surplus Firm available should be used to provide FBS based shaping at the cost of the FBS for the duration of the contract.

<u>IOU Benefits</u>

It is our belief that the Investor-owned Utility Financial Benefit arrangement in the Joint Customer Proposal creates benefits for the IOUs that are far too generous. In particular, we believe that the overall benefit level of 3300 aMW is too large. BPA's determination of 2200 aMW as a basis for IOU residential and small farm load benefits is reasonable and should not be adjusted upward unless net requirement determinations are conducted by BPA to ensure that amounts above 2200 aMW are consistent with their obligation to serve and within applicable statues. Furthermore, preference customers under the Proposal are at great economic risk because the financial benefits to the IOUs are only bounded in the first five years. Absent the ceiling, or similar protections arising from Section 7(b)(2) of the Northwest Power Act, sufficient safeguards do not exist in the Proposal to ensure that the customers of preference utilities will not suffer any adverse economic consequences as a result of the Proposal. Given the changes in the Proposal, we are concerned about the legality of replacing the rate ceiling mechanism in the Northwest Power Act with the proposed arrangement.

The magnitude of benefits should be based on the Investor Owned Utility's Average System Cost (ASC) rather than the embedded cost of a Combined Cycle Combustion Turbine. With the prohibition against the resale of requirements based power, the true benefits conveyed from the Federal System to the utility, for the purposes of low and stable rates, is the difference between that utility's ASC, and the lower cost of the Federal Base System. The move toward CCCT marginal cost or market price overstates the benefits due to utilities, shifts significant benefits from preference customers to IOU, and subjects preference customers to potential risks associated with commodity volatilities. This is clearly a violation of the intent of the Northwest Power Act and cost risk safeguards built into the construction of the REP and should not be part of any future IOU arrangement.

<u>GTA and LDD Costs</u>

Allocation and payment for the General Transfer Agreements is still an open issue within the region, and nothing stated, implied, nor inferred in the Joint Customer Proposal should be construed as settlement of these issues. This issue should be left to a rate case, or other similar venue for resolution.

II. Clarification of Subscription Benefits

<u>Contract Year 2007-2011 Period</u>

As part of its BPA Post-2006 process, BPA must completely address how it intends to continue service to customers that choose to remain on their Subscription contracts for the term of such contracts. BPA must provide certainty to customers who remain with their Subscription contracts with respect to the rates, terms and conditions of service. Customers must retain all rights available under the Subscription contracts for the term of these contracts, and should not be harmed by continuing service. BPA must fully honor all terms, conditions, and rate provisions contained in the contracts, and all supporting Subscription documents pertaining to such provisions. For example, for customers who purchased the SUMY Block Product, contract provisions and rate case documents state that the block power purchased in the second five years of the contract would be at the FBS-based lowest-cost PF for all MWh's purchased. If this benefit of lowest-cost PF were reduced or diluted in any way, such customers should be provided full financial restitution for economic harms suffered as a result of changes in BPA policy affecting such customer. To the extent there is a different rate for net requirement no greater than the CY 2007, similar restitution must be provided if net requirement determinations in CY 2012 and beyond result in a financial harm to the utility.

BPA must provide these customers adequate notice of the rates to be paid under Subscription contracts at the same time conversion contracts are offered. Customers cannot make prudent decisions regarding BPA service without knowledge of the rates, terms and conditions are under which each option of service will be offered.

Contract Year 2012-2022 Period

Prior to the expiration of full-term Subscription contracts in 2011, such customers should receive a replacement requirements contract to serve their net requirements, and should pay the same rate as customers who had chosen in CY 2007 to convert to new 20-year contracts. BPA has a continuing obligation to serve the Section 5(b) net requirements of all Customers who choose to remain on their Subscription contracts. Service to these customers should be at the same rate as customers who chose to convert to new contracts. Such rates should be based on BPA's un-augmented costs, at the lowest-cost PF, and should be entirely consistent with the equitable benefits and risks principles of the Joint Customer Proposal.

III. Preservation and Allocation of Benefits within the Subscription Period

General Cost Control

Over the course of less than two years, BPA's internal costs have increased dramatically. Although internal costs were just recently forecasted in the rate case in 2000, and in the cost review in 1998, BPA has not adhered to these levels, but rather continued to operate in a deficit spending mode. Quite simply, we believe BPA lacks the internal fiscal discipline necessary to operate to a budget, and favors the convenience and immediacy of CRAC adjustments to cost cutting.

To remedy this problem, customers must take control and obtain meaningful and enforceable participation in the process of setting BPA's expenditures and rates. We propose a task force be constructed, composed of representatives from each customer segment, to set BPA forecasted budget levels and monitor BPA spending. In the event BPA internal costs are above budgeted amounts, such over-runs would not be recoverable through CRAC, but rather through deferment of capital projects, additional reductions in internal programs, or reductions to the Treasury Payment Probability. The task force, in concert with BPA, would decide the appropriate means to eliminate the over-run.

Equitable Benefits for CY 2007-2011 vs. CY 2002-2006

In 1998, BPA released its Power Subscription Strategy; a strategy premised on the fundamental objectives of equitable distribution of the benefits of the Federal Columbia River Power System, and equitable sharing of the corresponding risks associated with such benefits. For the period of time that the Subscription Contracts remain in effect, and serve as the instrument of the Power Subscription Strategy, BPA has an overarching duty to the citizens of the Northwest to ardently pursue and accomplish the objectives of equitable distribution of benefits and risks of the Federal Power System, consistent with the Northwest Power Act.

To clarify, over this 10-year period, the benefits and risks of the Federal System should be shared equitable between all customers of BPA. We propose that at the end of the current five-year rate period, BPA evaluate the total rate period benefits received under each class of contract (Slice, Block, IOU Settlement, Full Requirements), and seek in the following five-year rate period to adjust the benefits flowing to each class of contract to ensure that over the total 10-year period, all customers, via their respective contracts, receive equitable benefits.

As an example, if it was found at the end of the current rate period, consistent with the Act, that one class of Subscription contract, the IOUs Residential Exchange Settlement Contracts, received a disproportionate share of the federal system benefits, in the first five years of the contract period, their benefits in the second rate period would be proportionately adjusted downward by the amount necessary to ensure that their overall 10 year benefits were no greater, and no less than any customer's benefits, consistent with the Northwest Power Act.

IV. Conclusion

Tacoma Power expended a great deal of time and resources in the negotiation of its current BPA Subscription Contract. Over the term of the contract, it is our hope that the contract will prove to be a prudent and cost-effective power supply choice. However, due to the present and projected magnitude of BPA's CRACs, and the resultant relationship of BPA and the market, any potential positive benefits will most likely only materialize in later years of the contact, when BPA is projected to be below market. In the first year of the contract we have suffered great financial harm – harm that is disproportionately above that suffered by other customers of BPA. Recovery for Tacoma Power can occur only if BPA employs prudent and immediate cost controls, and adheres to the fundamental cost and benefit objectives developed in the Subscription Strategy, and Tacoma ultimately receives benefits to offset the near-term harm that has already occurred.

Conversion to a new contract in CY 2007 could hamper this recovery. While it is feasible that Tacoma could again see positive benefits from any BPA contract, it is only under the following conditions that such recovery under contract conversion may be realized:

- Any adjustment to Tacoma Power's BPA requirements quantity of cost-based FBS cannot fall below Tacoma Power's 2002 contracted requirements quantity
- Financial restitution must be made to compensate Tacoma Power for damages resulted from purchase of the Stepped-up Multi Year Block Product and conversion to the new contract

In closing, our request of BPA is simple. Employ without exception, the principles born in the Power Subscription Strategy and the Joint Customer Proposal. Spread equitably the benefits and risks of the Federal System to all customers during the 10 year Subscription term. Ensure that beyond the 10-year term, sufficient and robust contractual mechanisms exist to guarantee the continued equitable allocation of benefits and risks well into the future.

Since submittal of the Joint Customer Proposal to BPA, the Proposal has continued to evolve. Adequate comment period must be give by BPA to address these and subsequent changes to the Proposal. Tacoma Power reserves the right to formally comment on the final version of the Proposal prior to its acceptance and final consideration by BPA. We look forward to continuing this process. I thank you for the opportunity to comment and look forward to your response.

Sincerely,

Steven J. Klein
Superintendent