



October 31, 2006

Mr. Steve Wright, Administrator
Bonneville Power Administration
P. O. Box 14428
Portland, OR 97293-4428

Subject: Cowlitz County PUD Comments on BPA's Regional Dialogue Proposal

Cowlitz County PUD appreciates this opportunity to provide comments on the Regional Dialogue Policy Proposal. The District would like to convey strong support for the general premise of allocating the output of the Federal system post – 2011. That said, we feel that the Public Power Council Proposal for Allocation of the output of the Federal system struck a balance between many contentious issues. We feel the PPC approach to resolving one of the issues, which BPA chose not to incorporate, is a critical element to “fair” Allocation of the output of the Federal system. This issue is the use of 2012 resources to determine the HWM's, as opposed to BPA's Proposal of 2010 resources. Recall that BPA chose to require utilities to apply resources shown in our current power contracts for the year 2010. As the following comments describe, we feel this is a mistake and urge BPA to reconsider using 2012 resources as the PPC Proposal suggested.

Following are our specific comments on the Proposal:

We agree with the PPC comments on the topic of Service to Publics;

For understandable reasons, the Policy Proposal does not address all of the details surrounding Service to Publics, and we expect that the Final Record of Decision (ROD) will not do so either. BPA should ensure, however, that it strikes an appropriate balance in the ROD by providing enough high-level policy decisions to give necessary guidance to the upcoming contract negotiations without locking itself into detailed implementation decisions that would preclude creative solutions during the negotiations.

Section III (B) (2)

“Decide Net Requirements Approach”

It is important that Net Requirements calculations use true critical water flows to determine both the HWM and the amount of Tier 1 power that can be purchased. True critical water for a Westside hydro resource should not automatically be based on the same year as the Columbia River critical water year of 1936 / 37. The net requirements process should recognize this and only require customers to declare actual firm resource capability, not the amount of generation that could have been produced during the 1936 / 37 water year. Cowlitz PUD's Westside resource has a 1976 / 77 critical water year, which is substantially less than the Regional critical water year. In fact, the 1936 / 37 water year ranks the 13th lowest water year on record for this Westside resource. Fair and reasonable resource declarations will be essential to the regional

acceptance and success of this Allocation construct. Use of 1936 / 37 water no longer makes sense for Westside resources, largely due to changes made in the 1997 Pacific Northwest Coordination Agreement (PNCA), which significantly modified the terms of Interchange Energy. We look forward to an open public process to establish a fair approach for calculating a Customer's Net Requirements as soon as possible.

Section III (B) (2)

“True-Up of Individual HWM’s with Actual FY 2010 Loads”

We agree that a true-up of loads used to calculate the HWM's in 2012 is appropriate, to the extent necessary. In addition, this true-up should take into account unusual events at specific large load consumers, such as temporary reductions as a result of unusual maintenance or temporary economic downturns that result in short-term reduction of specific large consumer loads. We also agree that weather normalizing actual loads based on long-term average weather (i.e.: 30 years, where available) is appropriate.

Section III (B) (2)

“Account for Conservation Achieved”

We feel the BPA Proposal did not go far enough to create adequate incentive for utilities to pursue BPA funded conservation. Rather than 50%, we believe that 75% of any BPA funded conservation between 2007 and 2010 should be added back into the calculation of HWM's. All conservation achieved during the same period that is utility funded should be added back into the HWM. This gives the appropriate incentive going forward to continue both utility funded conservation, as well as BPA funded conservation.

Some customers have been actively acquiring or developing resources in anticipation of Allocation. Many of these resources are renewable. It is important that BPA not penalize these customers for planning ahead and acquiring renewable resources. Power from any renewable resources that have been developed during the current contract period should not reduce the calculation of that customer's HWM. This includes resources acquired during the current contract period, prior to 2007.

Section III (B) (2)

“Use of FY 2010 Resource Amounts”

The Regional Dialogue Proposal's use of FY 2010 customer resource amounts, as they are identified in existing contracts, does not make sense to Cowlitz PUD. The PPC Proposal stated that 2012 resources amounts should be used to determine the HWM. This was proposed after many long discussions and compromises amongst the PPC members. By proposing to use FY 2010 resource amounts, BPA is in effect causing the resource decisions utilities made in the year 2000 to be in effect for approximately 26 years. BPA clearly told Cowlitz PUD in 2000 that we were making a 10-year commitment to resource performance. This statement applied not only to Cowlitz PUD's resources but also to the resources owned by Cowlitz PUD end-use consumers. The long term use of consumer-owned resources that were developed, financed and constructed by end-use consumers should not be determined based on the current use of those resources. Whether these consumer-owned resources are currently displacing load or being sold on the market, the disposition of these resources under the current contract should

not dictate future use during the upcoming contract period. This is why Cowlitz PUD strongly suggests BPA adopt the PPC Proposal to use 2012 resource amounts, which would allow the customers and consumer-owners to re-evaluate and refine resource operations and commitments, all within existing statutory requirements.

Cowlitz PUD observes that BPA did not make any significant mention of Contracted For, Committed To (CFCT) rights in the Regional Dialogue Proposal. This is a very important and noteworthy issue for Cowlitz PUD, as we have three industrial customers with historic CFCT rights. The PPC Proposal did not attempt to recognize the CFCT rights either, so it's not surprising that BPA didn't adequately address it. In order to achieve consensus on the PPC Proposal, Cowlitz PUD agreed to remain silent on this issue and instead sought out other compromises to balance the Proposal. A very significant compromise in this regard is the use of 2012 resources. Therefore, Cowlitz PUD strongly urges BPA to reconsider the BPA Proposal to use FY 2010 resources, and instead use FY 2012 resources as proposed by the PPC. If BPA chooses not to accept key portions of the PPC Proposal, such as this, it significantly affects Cowlitz PUD's ability to provide strong support to the Regional Dialogue.

We agree with the Proposal to adjust for hydro resources that are returned to a customer during the new contract period. These returned resources should appropriately reduce the customer's HWM that receives the returned resource, and in turn increase the HWM's of customers who lose use of that returned hydro.

Section III (B) (2)

“Augmentation Limits”

We agree it is appropriate to limit the amount of potential augmentation to prevent dilution of the value of Tier 1 power to a maximum of 300 aMW.

Section III (B) (3)

“Changes to Individual High Water Marks”

As the Regional Dialogue proposes, once a HWM is established for a customer, that HWM should be fixed for the term of the contract. Annexation, or similar action that only redistributes HWM between the two affected utilities is acceptable, to the extent it does not affect the rest of the customers' HWM's. Additionally, hydro resources that are returned to a customer should be adjusted for by decreasing the customer's HWM that receives the returned hydro, and in the same increment increasing the HWM for the customer that loses the output from the returned hydro. This too should have zero net affect on the HWM's of the rest of the customers.

Section III (B) (4)

“High Water Marks and Pooling”

Allocation will work to its full potential only if customers are able to work together to construct, or otherwise procure resources. A significant part of working together includes the ability to pool resources between utilities. We support pooling of HWM's along with pooling of other resources to enable customers to optimize their resource portfolios. BPA should reconsider allowing pooling of HWM's.

Section III (B) (6)

“Annual Net Requirements Calculations”

We agree that a simple, consistent and transparent approach to calculating Net Requirements is vital. In addition, there needs to be a fair, reasonable and expedited process to resolve any disputes between customers and BPA regarding Net Requirements calculations and load forecasts used to determine a Customer's Net Requirements and HWM's. Binding Arbitration would be one way to resolve these disputes in a fair manner.

Section III (B) (8)

“Treatment of Centralia”

While it may not be directly in our best interest, as a matter of equity, we continue to support the treatment of the Centralia resource described in the Regional Dialogue Proposal. We believe this was part of the compromise reached in the PPC Proposal and we continue to stand by the critical elements of that compromise.

Section III (B) (9)

“Rights to Remove Existing Resources”

It is essential that customers have the ability to remove existing resources from load service to the extent the customer experiences a load loss. We agree with BPA's Proposal in this respect.

Section III (B) (11)

“Customer Rights for Consumer Resources”

As noted in our comments regarding Section III (B) (2) above, Cowlitz supports the PPC Proposal to utilize 2012 resources or alternatively create a way in which customers' decisions as to the utilization of their resources in the current contract period essentially become 30-year decisions. We believe BPA's Proposal to use 2010 resources is strongly contrary to the understanding between BPA, Cowlitz and our customers at the time those decisions were made. We further believe, given the long term nature of these contracts, during which economic conditions and power markets will undoubtedly change, end use customers should have reasonable flexibility to alter the use of their resources during the term of the new contracts.

Section III (B) (14)

“Access to the Public Exchange”

We agree that the Residential Exchange is inconsistent with Allocation and customers must agree to settle any current or future Public Residential Exchange rights for the term of the contract.

The IOU exchange has long been a contentious and difficult issue in the Region. We support BPA's desire to put this contention behind us in order to have a more certain, stable future. That said, any resolution to this matter must be based on the fundamental principles that were

the underpinning of this section of the Regional Act. Stated simply, the Residential Exchange was intended to narrow the gap between the rates paid by public and IOU residential ratepayers. Twenty-five years later, the amount of increase in the PF rate, as compared to the IOU's average system costs have essentially achieved this goal without significant exchange benefits provided by public utility customers. In many areas of the region IOU residential rates are comparable to or even lower than rates of nearby public utilities. Furthermore it appears that household incomes in public utility service territories is lower than that of the IOUs as a whole, thereby creating a "reverse Robin Hood" effect of poorer households subsidizing more affluent households. Cowlitz PUD recognizes that any settlement of this issue is likely to be of an amount that is higher than we believe to be appropriate. That said, we believe it is wholly inappropriate to base exchange benefits on the basis of recent payments received by the IOUs. We strongly believe those payments are excessive and are contrary to both the letter and spirit of the law. We further believe that the Region's PUC's Proposal of somehow basing exchange benefits upon the proportionate share of residential customers is simply an attempt to rewrite the Act making up new provisions out of thin air, and cannot be supported.

Section III (B) (15)

"New Public Customers"

Supporting further development of Public Power is beneficial to the region as a whole. However, an unlimited open invitation to new Public Power loads at the Tier 1 price would place significant cost and resource risk onto the existing customers. We believe that the balance struck in the Regional Dialogue is appropriate and fair. Fifty aMW per year maximum, up to a total maximum during the contract period of 250 aMW is on par with historical needs and an appropriate limitation going forward.

Section III (C) (3)

"Load-Following Products"

BPA proposes to limit the amount of Slice product available to customers. At this point we cannot comment on whether we oppose this 25% limitation or not. Our support of BPA's Proposal is contingent upon whether or not BPA develops and offers a Partial Requirements or "load following" product that is palatable. Current "Load Following" products are not. They are far too restrictive to allow the levels of resource development, procurement and integration necessary in an Allocation scenario. If Slice is the only product BPA offers that effectively allows a customer to bring additional resources to load, we will oppose the limitation on Slice that BPA has proposed. However, if a Partial Requirements product is offered that is fair, reasonable and allows customers to efficiently bring additional resources, including intermittent renewable resources to load, we likely would not oppose the limitation suggested for the Slice product. The Partial Requirements products offered in this current contract period are not adequate.

Section III (D) (3)

"Tier 1 Rates for PF Power"

BPA proposes to include in Tier 1 rate calculations the "Acquisition costs for BPA's share of regional conservation targets". This cost should not be included in Tier 1 rates. This is an "incremental resource". Allocation is intended to put the customers "on the hook" for obtaining any incremental resource. Tier 2 rates are adequate incentive for customers to invest in conservation.

If potential RPS legislation in Washington passes, utilities in Washington will be required to purchase conservation. To require a Washington utility to purchase significant amounts of conservation in their service area, as well as pay, through their BPA Tier 1 rates, for other utilities' BPA funded conservation programs would be an inappropriate cost shift. Here again, costs related to BPA funded conservation should not be recovered in Tier 1 rates.

Section III (D) (5)

“Rates for Reshaping the FBS for Customer Use”

Any pricing or valuation of output of the Federal System for Priority Firm Tier 1 loads should be cost based, not market or opportunity-cost based. In addition, a fairly simple methodology should be adopted to do this which will produce relatively consistent, fair results that don't swing wildly from rate case to rate case. “Opportunity Cost” pricing is inappropriate for pricing Tier 1 products for Tier 1 loads. In addition, there needs to be strict, clear separation between Tier 1 and Tier 2 costs. All Tier 2 costs need to be excluded from Tier 1 rates.

Section III (E) (2)

“Irrigation Rate Mitigation”

This subsidy should be phased out completely. Just as we believe it is inappropriate for BPA as a matter of policy to subsidize the aluminum industry, we also believe it is inappropriate to subsidize a portion of the region's agricultural industry. While there may have been a rationale for the irrigation discount at the time this subsidy was established, that rationale, and that time has come to pass. Cowlitz PUD is the home of two pulp and paper industries that face an increasingly competitive market and do so without subsidy from BPA. These industries should not be asked to pay higher rates in order to subsidize others. We believe money spent on irrigation discount would be far better spent for the entire region on lowering the overall Tier 1 Priority Firm rate, thereby creating the best business environment as it relates to power costs, for all of our Region's industries.

Section III (E) (4)

“Transmission Considerations”

We agree with the PPC comments on transmission issues;

BPA's Proposal raises significant transmission issues, the most of which relate to queuing and having equitable access to Non-Federal Tier 2 resources. We suggest these issues be resolved rapidly but resolved outside of the formal regional dialogue process.

Section VII

“Service to DSI's”

Surplus power from the FCRPS is, for all intents and purposes, a thing of the past. So too should be the subsidies to the DSI's. It is not fair, nor equitable, to subsidize a failing aluminum industry on the backs of our customers, many of which are themselves businesses struggling to stay viable in a competitive international market. We can no longer claim to be supporting an

industry with a region wide presence, significant employment, and multiple facilities and facility owners. Continued subsidization of this industry is likely to be a subsidy to one company, whose commitment to this Region is suspect. The cost to the Region of subsidizing this industry is almost certainly greater than the benefit received.

Section VII

“Conservation”

We believe that Allocation will provide adequate incentive for customers to perform conservation on their own. That said, we understand how BPA may be reluctant to take that premise at face value. To placate any concerns that BPA may have that the Councils targets will not be met, we would suggest a phase-out approach, where within the first couple years, if customers demonstrate that they in fact are instituting sufficient conservation measures, BPA would completely step back from any Tier 1 funded conservation. At that point, any BPA conservation costs would be collected from Tier 2 rates (but only to the extent that customers request Tier 2 service from conservation resources). NEEA and related market transformation activities could reasonably be an exception. We believe it is reasonable for the costs of market transformation activities to be collected from Tier 1 rates. If customers do not demonstrate that they are stepping up to perform adequate conservation, BPA would continue for another short “interim” period to collect funds earmarked for conservation from Tier 1 rates. At the end of the “interim” period, BPA would again check to see if customers are performing adequate conservation. In this fashion, BPA would be assured that if there is not enough conservation being performed, it can still step in to provide funding on a temporary basis.

Section XI

“Long-Term Cost Control”

We would like to support the comments of Washington PUD Association (WPUDA) on the issue of long term cost control. WPUDA comments are the following;

WPUDA appreciates the Administrators recent efforts to create a more transparent and collaborative cost control process. WPUDA has examined the cost control mechanisms within the RD Proposal and agrees with BPA that the Regional Cost Review (RCR) would provide the most opportunity within the region for all stakeholders to participate and to make BPA's "decision making and cost information open and transparent with ample opportunity for input." Having said that, WPUDA is not convinced that the RD Proposal provides effective cost control mechanisms commensurate with customers making a 20-year contract commitment. Cost control is of utmost importance to BPA's customers. It is imperative that BPA and its customer's have reciprocal obligation and incentive to work cooperatively to control costs which ultimately show up in customer rates. Because rates are cost based, and this structure is to be set in place for 20 years, WPUDA believes the cost control process must provide for a real, durable and effective method by which customers can exert tangible input on BPA's costs. To the extent allowed by Federal law, this may require the Administrator to cede some of their inherent decision making discretion to the cost-control process. It is not clear that BPA has in fact gone as far as it is allowed in this regard. In this Proposal BPA is asking customers to settle certain issues and waive certain rights, which many customers are extremely reluctant to do. In return WPUDA asks the Administrator to revisit the RD cost control Proposal to assure that it does, to the extent allowed by law, provide customers with meaningful cost control mechanisms.

An important element of a creative and effective cost control environment is creating alignment of interests among various contracts / products. Currently the differences between how the Slice and other contracts treat true-up and CRAC mechanisms cause difficulties for both BPA and its customers. Those differences should not carry forward in the post 2011 contracts.

Absent an effective cost control mechanism, WPUDA would require a termination provision in the contract to minimize long-term risk of uncontrolled cost.

A very important element of effective cost control is preventing the leakage of Tier 2 costs into Tier 1 rates. While we understand that BPA has a statutory obligation to recover all costs, we also believe it is very important that all costs, benefits and risks of Tier 2 service be contained within Tier 2 rates and placed on customers opting for Tier 2 service.

Section XII

“Dispute Resolution”

We would also like to express our support of the comments of Washington PUD Association (WPUDA) on the issue of dispute resolution. WPUDA comments are the following:

WPUDA is not clear exactly what the proposed dispute resolution processes really are in the RD Proposal. For example, what is the remedy if a utility becomes involved in a dispute with BPA in the event BPA represents the dispute as a change in interpretation, rather than a change in underlying policy? We do understand that BPA cannot cede ultimate jurisdiction where they do not have the authority in law to do so, but we also understand that this is a settlement proposal and that BPA and the region should agree on a robust dispute resolution process that will serve us all equitably and fairly, one in which both parties have ceded some of their discretion to the process.

We do believe that all parties would be better served if those contract provisions that may lend themselves to solution through specific dispute resolution processes be so labeled in the contract. Certain provisions could be labeled as appropriate for arbitration, for instance, or submission to an administrative law judge or other independent third party. A more defined pathway to dispute resolution coupled with the issues identification process described below will provide more certainty for all parties.

One potentially viable dispute resolution alternative which has recently come to our attention is the proposed dispute resolution process in the Slice Settlement. (The following will need some review and cleanup prior to final language.)

As we understand it, there is first a 60 day facilitated discussion process in an attempt to identify and resolve the issues. The Administrator issues a draft report after the facilitation process addressing the resolved and unresolved issues, if any, and setting forth the Administrator's rationale and conclusions. Parties, if they disagree, are then given a time certain to initiate a non-binding arbitration process. Preference customers are allowed to intervene and participate in arbitrations, while others may if they can demonstrate standing. Parties cannot file a petition for judicial review until they have engaged in the arbitration process. If no party initiates the arbitration process, the Administrator issues a final decision based upon the draft report. If the arbitration process is undertaken, then within 15 calendar days of the arbitrators' decision, BPA issues a final written decision that (i) decides the disputed matter(s) and explains why BPA accepts or rejects the arbitrator's decision on each of the disputed matters, and (ii) makes final without change the disposition in the earlier draft report of the resolved matters. In the event the Administrator accepts the arbitrators' decision on a disputed matter, then any party to the

arbitration shall be bound by the Administrator's decision on that disputed matter and may seek no judicial review or any relief concerning the decision on that disputed matter, except that any party may seek review of the arbitration upon the grounds referred to in the Federal Arbitration Act, 9 U.S.C. §§ 1-16 (1988).

Conclusion

The Regional Dialogue ROD and its subsequent product development and contract negotiation is the most significant endeavor relating to the Region's power supply since the adoption of the Regional Act. Cowlitz PUD would like to thank and commend BPA for its willingness to initiate this process. We believe the Allocation of the Federal Base System, the commitment to preserve the cost based affordable tier one resource, and the associated clarity regarding the rights, responsibilities and options that exist for both BPA and the Region's utilities is the best way to assure the Region of an affordable and reliable power future. Just as importantly it enhances a cornerstone of public power; local control. Some utilities will rely on BPA for Tier 2 service; others will develop resources to meet their growing loads on their own or with others. The specifics of those decisions will vary among utilities based on community values, preferences and economics. This is as it should be. We would further like to express our appreciation for the extent BPA, in its draft, adopted PPC's Regional Dialogue Proposal. This is in the spirit of cooperation that served the Region well in the recently concluded power rate case and bodes well for the work that is yet to come as we move toward new long term contracts. In our comments we have attempted to continue in this spirit of cooperation. Comments submitted by PPC and WPUDA reflect a tremendous amount of effort in achieving compromise and consensus on a variety of difficult and sometimes contentious issues. Our support of certain positions in some cases is not in the narrow interest of Cowlitz PUD, but rather reflects our desire to encourage this spirit of collaboration. Your consideration of Cowlitz PUD's comments and your effort to forge a common vision on these issues is very much appreciated.

Sincerely,



Brian L. Skeahan
General Manager