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TACOMA PUBLIC UTILITIES

October 31, 2006

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

Re: Tacoma Power's Comments on Bonneville Power Administration's Long-Term
Regional Dialogue Policy Proposal of July 13, 2006

Dear Mr. Wright:

Tacoma Power appreciates the opportunity to provide comments concerning the Bonneville Power Administration's (BPA) Long-Term Regional Dialogue Policy Proposal of July 13, 2006. Tacoma Power's comments extend to many of the issues described within the Policy Proposal; while Tacoma Power acknowledges the work completed thus far, we all must recognize the large task lying before the region. A commitment on behalf of BPA and others to strive for completion will be needed to bring closure in a timely manner to the many open-ended questions that the Policy Proposal produces.

The following summarizes the issues that are most important to Tacoma Power in the development of new power sales contracts and associated rate methodologies:

- High Water Mark Determinations:
 - Consistent with the Public Power Council's April 10, 2006 letter, Tacoma Power supports using FY 2010 actual customer retail loads and a reasonable estimate of FY 2012 customer resources for determining contractual High Water Marks (HWMs). Resources that are not available at the start of the contract period should not be included in the determination of HWMs and Net Requirements determinations.
 - The methodology used to determine HWMs should recognize utility funded conservation investments made between 2002 and 2012 and therefore not create any disincentives for conservation investments between now and 2012.
 - The methodology should incorporate transparent and objective protocols to the greatest extent possible for any appropriate adjustments to loads and resources affecting HWMs.

- Treatment of Centralia: Tacoma Power properly removed the Centralia resource in accordance with the terms of its 1981 Power Purchase Contract with BPA. The Centralia

resource will not have been available to serve Tacoma Power's loads for over twelve years by 2012 when the new contacts become effective. An essential compromise within the public power community on this issue has been reached, which supports the permanent removal of the Centralia resource from the resource exhibits of all of the previous public power purchasers of Centralia. BPA has the discretion and legal standing to endorse this consensus.

- **Product Development:** The products developed for the new contacts must be both viable and durable for the entire contract period. Additionally, the products developed must meet the needs of customers within the region.
- **Treatment of Conservation:** Conservation acquisition in the post-2011 period should generally become the responsibility of utilities individually. Only costs associated with a defined budget for market transformation program should be funded within Tier 1. Any costs associated with utility requested conservation acquisition programs should be restricted to Tier 2.
- **Dispute Resolution Protocols:** As endorsed by PPC, dispute resolution protocols should ensure neutral, timely, and objective decisions to the greatest extent possible within BPA's statutory framework.
- **Cost Control:** BPA, as the caretaker of valuable regional assets has a fundamental responsibility to ensure the costs of preserving the long-term viability those assets are appropriate and reasonable. Therefore, BPA must establish a reliable practice to control costs and should do so with significant input from its contractual customers. In that light and given the prospect of tiered rates, BPA also must be vigilant in ensuring that Tier 2 costs do not migrate into the Tier 1 rate pool.
- **Waiver of Customer Rights:** Customers should not be requested to effectively "waive" any statutory rights through the signing of a contract as a condition of exercising their statutory right to purchase power from BPA until a complete and comprehensive agreement on the new contracts has been reached.
- **Transfer Service:** Tacoma Power supports BPA's proposal to place a cap and limit upon future transfer service, and feels that the limits proposed are both fair and equitable compared to historical and projected transfer service costs. Consistent with our previous comments on this issue, we do not support the current practice of allocating transfer services costs to power. These costs are transmission costs and should be allocated, priced and billed as such.
- **Transmission Considerations:** Transmission service for preference customers' loads must be reasonably available, or customer development of new resources will be thwarted.

- Benefits to customers of IOU's: Tacoma Power supports the idea that a conclusion and settlement can be reached between BPA, IOU's and Public's on the issue of benefits among IOU Residential Exchange Customers.
- Resource Adequacy: Tacoma Power supports the establishment of resource adequacy standards for the region through the Regional Resource Adequacy Forum, but does not support having these standards as a provision in BPA power sales contracts.

One of the main principles in shifting to an allocation realm based on tiered rates is to encourage resource development by customers. BPA's current proposal falls short of this ideology because of the introduction of many unnecessary uncertainties. The uncertainties increase the risk and reduce the willingness and probability that Tier 1 preference customers will be able to make long-term resource decisions. Tacoma Power supports the continued evolution of the current proposal so that unnecessary uncertainties such as the creation of durable and flexible long-term contracts, how loads and resources are accounted toward a utilities HWM and Net Requirements calculations, BPA's role in regards to conservation and renewables acquisition or facilitation and other items specifically addressed below can be limited or eliminated completely before the signing of the Regional Dialogue Contracts.

The Regional Dialogue Proposal must be composed of a robust and durable solution for the region's Load Serving Entities. The contracts must be able to endure many unforeseen possibilities throughout the contract period. Additionally, the proposal must be successful in the case that Tier 2 becomes less expensive than Tier 1 or in the case that Tier 1 resources fail or must be derated by some amount. The contracts must provide for reliable dispute resolution and reasonable cost control during the entire term of the contract. At the same time, the contracts must also provide sufficient flexibility for customers to react to changes in the cost of Tier 1 power and possible significant changes in wholesale power markets. It is imperative to note that the components of the proposal are a complete packet and must all work together to produce a durable and successful package of contracts, rates, and policies. While significant progress has been made over the last few months it is apparent that a considerable amount of work still lies before BPA, its customers, and the region before new contracts can be executed in 2008.

Tacoma Power supports the comments provided by the Public Power Council in many areas addressed in BPA's Long-Term Regional Dialogue Policy Proposal. However, Tacoma Power also provides here additional clarifications and differentiations from comments submitted by the Public Power Council in certain areas within BPA's Long-Term Regional Dialogue Policy Proposal.

Schedule

The proposed schedule leading up to the signing of the contracts (identified on page 5 of the BPA's proposal) and the schedule for activities once the contracts are signed are two areas of concern to Tacoma Power. As previously mentioned, one of the most important purposes of the long-term Regional Dialogue contracts is to promote resource development by customers and create a stable but flexible contract and rate structure for federal power sold to all of the

preference customers within the Northwest. In order to accomplish the many tasks before the region, Tacoma Power supports BPA staying with the current schedule for a Record of Decision (ROD) on the Policy Proposal by January 2007. Delaying the ROD until February or March of 2007, if absolutely necessary, should not interfere with continued preliminary work on the tiered rates methodology, revisions to the 5(b)/9(c) policy, new product definitions, and the fundamental provisions in standardized contracts; these must be finished before bilateral contract negotiations can be completed. BPA must acknowledge the difficulty associated with asking customers to sign contracts before many of these important processes have been completed, and thus the need for such processes to come to conclusion before contract execution. This will undoubtedly require a significant commitment by both customers and BPA during 2007, in order to allow bilateral negotiations to begin in early 2008.

Additionally, once the contracts have been signed, a schedule must be determined for the actual implementation of tiered rates and the biennial recalculation of expected Tier 1 rights for each rate case, including net requirements determinations. Both the contracts and the rate methodology should, with a high level of certainty, lay out the schedule for actions taken in advance of and during each rate case. Without this biennial implementation schedule, resource and power purchase decisions by customers will not be feasible, again thwarting the objectives of the Policy Proposal.

High Water Marks

BPA proposes a multi-step process for establishing High Water Marks (HWMs), using a new net requirements methodology, 2010 actual loads and resources, potential augmentation, and a conservation adjustment (§III.B.2., pp. 13-15). In general, Tacoma Power agrees with this approach, including the transparency aspect with the exception of designating resources as of 2010. The process for establishing HWMs should meet the following objectives:

1. In order to minimize disputes, the process for determining initial HWMs should be as transparent as possible. This implicates methodologies, data sources, confidentiality (especially of end-user information), and consistency in application across utilities. Any exceptions should follow a standardized procedure that all can review.
2. The establishment of initial HWMs should reflect as accurately as possible the loads and resources of individual utilities at that point in time. Actual 2010 loads will be known in early 2011. Also in 2011, reasonable estimates can be made of 2012 non-federal resources available to meet utility loads in the new contract period, especially if the methodology for making such estimates is established before 2011. In effect, both determinations can be made at the same time. There may be little reason to expect dramatic changes in loads from 2010 to 2012, but the utilities' resources used to calculate HWMs should not be tied to decisions made (or required) under existing contracts. BPA required current contracts to rely on 1998-99 FREs, which was unreasonable at the time, and there is no reason to require decisions made under current contracts to have spill-over effects into new contracts.

3. Incentives to continue conservation programs between now and the implementation of the new contracts must be preserved and enhanced in accordance with the April 10, 2006 PPC letter.

In addition, Tacoma Power recommends that BPA make the following modifications to the HWM approach, in the interest of assuring greater transparency and regional acceptability of the calculations and resulting HWMs.

First, the new net requirements policy should include a detailed methodology for doing weather-normalization of 2010 actual loads. The weather-normalization process should rely to the greatest extent possible on publicly-available information and a methodology that is applied consistently across all of BPA's customers. The starting point for such a process should be actual retail loads in fiscal (contract) year 2010. Either these actual retail loads should be made public on a utility-specific basis, or the actual retail loads should be turned over to a third party who will certify that the loads going into the HWM calculations match actual amounts.

Second, the new net requirements policy should identify a limited list of "significant one-time force majeure events" that will be used to modify actual 2010 loads and 2012 resources, such as the forced outage of a generator or a strike that closes a manufacturing plant during 2010, or uncontrollable regulatory proceeding outcomes. The obligation to document such "significant one-time force majeure events" should fall on the utility claiming such an event. To the extent possible within the Administrator's statutory obligations, disputes over the existence, qualification, and impact of force majeure events on individual HWMs should be reviewed by a neutral entity, which would yield a non-binding recommendation to the Administrator within 60 days (or some similarly fixed amount of time) of submission of the claim. The recommendation should be made public, and the Administrator should explain any deviation from the non-binding recommendation in the final decisions on HWMs that will go into new power sales contracts.

However, utilities should not be required to have resources specified within their new contracts that will not be available to serve load starting in FY 2012. Tacoma Power supports the use of 2010 loads and reasonably projected 2012 resources as an overall compromise to get the region to adequate allocations. Tacoma Power does not agree that using 2012 projected resources introduces a significant amount of uncertainty into the allocation process. First, as noted above, there is uncertainty about actual 2010 loads until some time in early 2011. From the perspective of 2007, this uncertainty is likely to be greater than the uncertainty about resource capability forecasted in 2011 for 2012, simply because of the gap in time between the date of the estimate and the year for which the estimate is being made. For example, BPA proposes to forecast total PF loads in 2007 for 2010. A 1.5 percent load growth assumption for three years implies about 4.6 percent load growth over three years. If PF loads are about 7,000 aMW, this implies over 320 aMW of load growth. However, actual 2010 loads will most likely not reflect exactly 320 aMW of load growth since 2007. The uncertainty around this amount of load growth is greater, in Tacoma Power's estimation, than the uncertainty about resource capabilities between 2010 and 2012. If customers can plan for the uncertainty surrounding over 300 aMW of projected load growth, they should be able to manage around the uncertainty associated with specific resource changes from 2011 to 2012. Finally, as Tacoma Power has noted elsewhere, customers

should not be penalized in future contracts for decisions that BPA made regarding resource declarations in current contracts. This applies to both customer- and consumer-owned resources.

BPA has recently posited the possibility of two approaches to determining HWMs: the "annual" and "monthly" options. Although Tacoma Power understands that the "official proposal" at this point is the "annual" option, we propose that the details of transforming each utility's annual HWM into monthly and diurnal Tier 1 rights be developed carefully. It is noteworthy that as a part of the product development exercise for the current subscription contracts, the products in the product catalog were defined well enough for a purchaser to understand how its annual net requirement number could be transformed into more useful granular data for modeling assessment purposes. Although at this point in the Regional Dialogue process the "annual" HWM approach appears preferable, a more detailed understanding of critical details of diurnal and monthly derivations is required before final decisions concerning Tier 1 rights can be made.

One potential shortcoming in BPA's proposal is the lack of a HWM for capacity, which is combined with (and may in fact drive) the proposal that load-following and peak demand services be priced "at market" or "at opportunity cost". This creates the incongruous result that Tier 1 purchases are "on the margin" for load following customers during each rate period. Because of the potential for rate design details to change over time, this will make planning and implementing conservation and demand-side management (DSM) programs more difficult at utilities that purchase load-following service from BPA. In essence, these utilities will have to redesign their conservation and DSM programs every rate period, which could be as often as every two years. Tacoma Power understands the difficulties associated with establishing a "monthly capacity HWM", but urges BPA to rethink this issue. One option may be setting HWMs for capacity in Tier 1. In theory, the monthly peaking capacity of the Tier 1 resource pool could be forecasted, much as the monthly energy capability of the Tier 1 resource pool will be forecasted in each rate case. The HWMs (in percentage terms) could then be applied to the forecasted monthly Tier 1 peaking capacity, to establish monthly Tier 1 capacity rights, which should be priced based on an approach to separating energy and capacity services established in the tiered rates methodology. Peak loads greater than Tier 1 capacity rights should be priced at market or opportunity cost, to provide the right price signals for conservation and DSM during each rate period. However, customers' contract rights to Tier 1 service should not be compromised by biennial changes in rate design. Other options would focus on pricing Tier 1 rights much as the Slice product is priced today. Tacoma Power recognizes that many details of these options have not been worked out, but suggests again that care be taken in the development of the HWM determination methodology.

BPA requests comments in particular on §III.B.2 (p. 14) related to "unused" HWM amounts. BPA needs to define what they propose to do with the "headroom" that results from difference between HWM Tier 1 and the net requirements that BPA will serve during a particular year. Tacoma Power assumes that BPA will sell that power into the market or to Tier 2 customers. Tacoma Power proposes that when or if this scenario occurs, a share of the net revenues of the resold power be credited back to the Tier 1 pool.

Finally, Tacoma Power strongly urges BPA to establish in new contracts that HWMs are percentage shares of Tier 1 resource capabilities, and not average MW amounts. Although the aMW amounts should be calculated using the approach outlined in §III.B.2 (as modified by the above suggestions), these individual aMW amounts should then be translated into percentages for inclusion in new long-term contracts. This should make the calculation of each utility's Tier 1 rights during the contract period more transparent.

Tiered Rates Methodology

In §III.D.2., BPA describes the need for a tiered rates methodology. This methodology would be developed through a series of public workshops, followed by a §7(i) process under the Northwest Power Act, with the result filed at FERC for long-term approval. Although Tacoma Power recommends that the details of the methodology should be developed through the public workshops and tested in the §7(i) process, certain principles can and should be established at this point.

Tier 1 costs and Tier 2 costs should be strictly separated to the maximum extent possible, and the costs of different Tier 2 products should also be strictly separated to the maximum extent possible. Although this will require several decisions regarding rate design, product design, contract provisions, and BPA's accounting systems, the entire structure of tiered rates and power allocations depends critically on the assurance that customers who choose not to buy "X" will not be required to pay for "X", unless BPA's overall ability to meet its statutory obligations is threatened. Because of the various systems that must be designed or redesigned, BPA should begin immediately working toward the goal of cost separation within the PS.

BPA should not rely on arguments that joint costs cannot be separately assigned to individual products, and that fixed costs (such as certain overheads) would be incurred in any event and so should all be assigned to Tier 1. State regulatory commissions require that labor costs at IOUs be separately tracked between regulated and unregulated business lines, to ensure that the "captive" customers of the utility are not assigned costs that should be recovered from unregulated activities. BPA can and should adopt the same approach, because its Tier 2 product offerings will be "competing" in some sense against alternative means of meeting power requirements. If BPA does not adopt this approach, Tier 1 customers will automatically and by definition be subsidizing Tier 2 products, which will then appear more attractive than is reasonable or appropriate, compared with alternatives.

In addition to cost separation, BPA must implement risk separation. Again, Tier 1 risks should not be borne by Tier 2 customers, or vice versa, and the risks of individual Tier 2 products should be incorporated into the prices of those products separately. If these risks are appropriately identified and the costs of managing such risks appropriately assigned, then the potential for Tier 2 costs to migrate to Tier 1 *in extremis* should be minimized. For example, customers buying resource-specific Tier 2 products should bear the forced outage risks of those resources: market purchases to fill behind a resource that is forced off-line must be borne solely by those customers who have chosen to buy the resource-specific Tier 2 product. Other methods

are possible for risk separation and risk coverage, such as insurance services; all of these should be required elements of product design and contract development for Tier 2 products.

BPA has already established that product development costs must be borne by customers of certain products, specifically Slice. Prior to the offer of the Slice product, BPA required potential Slice purchasers to contract separately for Slice development costs, and since the Slice product has been implemented, actual Slice purchasers have paid separately for Slice implementation costs. These principles should be extended to all Tier 2 products. Specifically, development and implementation costs for Tier 2 products must be borne by those customers who agree up front that they are sufficiently interested to support the development of the individual products and/or agree that they are willing to bear the full cost of actually implementing the product. This up-front agreement must be established in the bilateral contract negotiations scheduled for 2008, because BPA will likely incur costs from that point on in preparing to meet Tier 2 loads after 2011. Again, without such assurances, Tier 1 customers will be subsidizing the development and implementation of Tier 2 products. Furthermore, customers who wish to avoid such developmental costs before 2011 (which is a legitimate position) should be required to purchase a standard, market-based Tier 2 product for each rate period until such time that they are willing to share in the costs of developing other Tier 2 products. It is understandable that customers might be unwilling or unable to pay up front for certain product offerings to be developed, but there should be consequences for such actions that ensure that other customers do not subsidize the ultimate product design and offering.

BPA staff have indicated in tiered rates workshops that the costs that BPA expects to incur to meet capacity or reliability requirements for loads in the Transmission Service (TS) control area will be isolated and recovered only from those customers in the TS control area for which BPA has agreed to accept the responsibilities under still-developing FERC, NERC and WECC regulations and policies. For example, BPA may have an obligation to ensure that certain capacity margins are met for loads in the TS control area. Such capacity margins may be met by peaking resources, DSM programs, or other means, but in any event the customers who choose to remain in the TS control area should be responsible for the recovery of the costs of such capacity margins. Tacoma Power operates its own control area and will be individually and separately responsible for meeting FERC, NERC, and WECC reliability criteria, and it would be unreasonable in the extreme to ask Tacoma Power ratepayers to, in addition, pay for capacity resources that are required to meet reliability criteria in any other load area, including TS's. BPA should establish, as a principle in the Regional Dialogue ROD, that the tiered rates methodology will assign incremental reliability costs to those who cause BPA to incur such costs.

Once the tiered rates methodology is developed and finalized via a §7(i) process, it must be memorialized in manners that provide reasonable assurance that the methodology will remain stable over time. This means (1) that the methodology must be submitted to FERC for approval for a period no less than the duration of the new contracts, (2) that the methodology once approved by FERC must be included in the new contracts, and (3) that there be neutral, third party interpretations of the rate methodology in the event of disputes, even if the final decisions on implementation of the methodology are made in §7(i) processes by the Administrator. The

third element applies especially to the allocations of costs between Tier 1 and Tier 2 products, and among Tier 2 products. The tiered rates methodology should include principles that a neutral third-party entity would be used in the event of disputes, in order to develop a recommendation to the Administrator.

BPA should recognize that it makes no sense to send "price signals" when customers are not able to respond to them. This means that the prices set for Tier 1 service should ensure cost recovery but should not incorporate "price signals". Tier 1 purchases are expected to be based on take-or-pay contracts, which are incompatible with the very concept of price signals and demand responses to such signals. Price signals should be reserved for Tier 2 products, including purchases of capacity (peak load) above Tier 1 capacity rights. One approach that meets this goal is to price Tier 1 as a percentage of the total Tier 1 revenue requirement, as Slice is priced today. This would remove the uncertainty about demand and energy charges for Tier 1 from future rate cases, and provide a level of certainty about Tier 1 pricing that will allow other decisions to be made by all parties.

Tacoma Power understands that BPA proposes using a single after-the-fact "true-up" rate adjustment mechanism to cover differences between expected and actual Tier 1 costs and revenues (p. 39). The main reasons for this approach would be to align the interests of preference customers purchasing different types of Tier 1 products (especially Slice and non-Slice), and to ensure that the costs of Tier 1 are actually covered by BPA's revenues. In general, Tacoma Power supports this approach, especially if it is implemented in conjunction with a "Slice-like" approach to pricing Tier 1 power. However, other mechanisms for the recovery of actual costs may support these two overall objectives, and BPA should not prejudge this issue in the Record of Decision on the Regional Dialogue. Rather, the details of ensuring cost recovery for all types of power products purchased from BPA should be developed in the tiered rates methodology.

Product Definition

While it is understandably early in the development of the products that will be offered to customers under the Regional Dialogue Contracts, a number of significant questions and uncertainties must be worked out during 2007. BPA must be committed to working with customers to create products that will be both compelling and durable for the duration of the contract period. While some customers may expect that their circumstances will remain the same throughout the contract period, many critical facts will undoubtedly change, and customers must be able to change from the initially selected products, with sufficient notice, during the entire contract period. Tacoma Power expects that notice for product changes would address both the notice period before a product change could go into effect and the minimum duration of any new product selection.

Of significant importance, the unit cost of shaping services should not vary among different products. For example, a Full Service Customer should not be expected to pay more or less, on a unit basis, for a given amount of shaping services than what a partial requirements customer would pay for that same amount of shaping services. This principle applies to both load-

following services and the service of “reshaping” the output of the Tier 1 resource pool to meet a flat or shaped block delivery obligation. In this way customers that need more (or less) shaping services would pay more (or less) in total based only on the amount needed or used. Likewise each of the products should be composed of both energy and capacity.

Tacoma Power supports beginning with the products currently available in today's product catalog as the starting place for developing the product catalog for the Regional Dialogue Contracts and offers the following comments in regard to specific products.

Load Following: Partial Requirements

The partial requirements product should be defined such that it is a useful alternative for customers with limited generating resources or those adding new resources, i.e., for instance, as an alternative to purchasing the Slice Product.

Block

Tacoma Power would like to see a Shaped Block product with modifications offered for the Regional Dialogue Contracts. The Shaped Block product should retain the current characteristics and also provide some additional shaping capabilities including the following: (i) a customer's block contract amount should be based on customer loads and resources, (ii) heavy load hour shaping should be a calculation based upon customer sustainable peaking capacity and peak loads, (iii) customers should have daily light load hour shaping, including Sundays, (iv) customers should have shaping ability during both heavy and light load hours across the month, and (v) BPA should recognize block heavy and light load contract definitions consistent with NERC holidays. Tacoma Power recognizes there may be pricing implications of such services but they would create a more balanced and useable shaped block product.

Slice

Tacoma Power would like to support comments provided by WPAG and joint comments of the Slice Purchasers with regard to the treatment of the Slice product in the ROD. Although Tacoma Power is not currently a purchaser of the Slice power product, Tacoma Power is interested in ensuring that the Slice product remains a viable product option in the post-2011 period. Tacoma Power has therefore reviewed the proposed “Alternative 2” carefully, as well as the proposal to limit the sales of the Slice product to 25 percent of the Tier 1 system. In general, Tacoma Power has concluded that the elimination of certain capacity rights in a new offer of the Slice product are not reasonable or necessary, and that the proposed overall limit on Slice sales is too low.

It is unfortunate that significant misunderstandings and disagreements led to the litigation regarding the Slice contract during the last few years. However, that litigation has now been settled, and BPA should use the settlement as the basis for moving forward with a new offer of the Slice product. There was apparently no need in the settlement to change the definition of the product, and thus there is no need to reduce capacity rights of Slice purchasers in the future. BPA has not demonstrated, to Tacoma Power's knowledge, that any specific capacity right, with

the possible exception of load regulating capacity, has, is currently, or will cause difficulties in the delivery of the Slice product. BPA has also not demonstrated that reductions in capacity rights for Slice purchasers will yield comparable flexibility to Slice purchasers and PS as the marketer of the remaining Tier 1 capability. BPA has also not justified the proposal that "off-the-top" obligations should be expanded over time to integrate new resources. Slice purchasers know that they are accepting the inherent uncertainties of the Slice system capability, but BPA should not be able to diminish that capability for its own marketing purposes. To do so would put the Power Services at a competitive advantage in resource integration services, which is contrary to the fundamental principles of both the Regional Dialogue proposal and of the development of markets for these services. BPA should not create advantages for the PS in the market for resource integration. BPA should not remove capacity rights from the Slice product and replace them with revenue credits.

Removal of the Centralia Project from Declared Resources

Consistent with the previous submission of comments from the Public Power Council on August 7, 2006, Centralia participants should not be required to declare Centralia in the 2010 (or, preferably, 2012) determination of net requirements and HWMs. There is no need for a public process; the current situation is a result of BPA's decision in 2000 to force utilities to live with their 1998-99 Firm Resource Exhibits, which was unreasonable at the time and remains such. Additionally Tacoma Power would like to support the document prepared and submitted to BPA on September 26, 2006 on behalf of Snohomish, Tacoma Power, Seattle, and Grays Harbor in relation to the Centralia resource.

As a minority shareholder of Centralia, Tacoma Power has not retained ownership of the Centralia resource since May 2000... Tacoma Power has fulfilled the contractual requirements necessary to remove Centralia from our Exhibit C. It would be inequitable for BPA to reduce the amount of Tier 1 resource available to Tacoma Power, and the other public utilities that were shareholders of Centralia, by assuming that this generating project is still available to serve these utilities' retail loads.

Treatment of Priest Rapids Project Power

Tacoma Power supports the comments (1) through (4) and (6) and (7) submitted by Grant County PUD on October 17, 2006 as part of the overall package of the Regional Dialogue Policy Proposal.

Fall Back Proposal

BPA has proposed in §XIV a "Fallback Proposal" in the absence of regional consensus on the package proposed on July 13. Although Tacoma Power understands the purpose of such a fallback proposal, it is not clear what circumstances would trigger the fallback, and what the details of the fallback would look like. Furthermore, there are no logical connections among the various elements of the fallback proposal. Tacoma Power recommends that BPA rethink the fallback proposal and revise it significantly.

It is not clear what "regional consensus" within the context of the fall back proposal means. BPA has not proposed a metric by which regional consensus could be measured. It is entirely possible that one or two regional entities (public utility, private utility, DSI, or governmental body) could hold out and defend a specific position, thus thwarting "regional consensus" and forcing the fallback proposal. Given the many compromises that have been struck within public power on "service to publics", there is no need to hold those elements of the proposal hostage to "regional concensus" on other issues. As an example, Tacoma Power believes that the treatment of the Centralia resource, as unanimously endorsed by the PPC membership, should be followed consistent with our comments above.

New Publics

In general Tacoma Power does not support augmenting the existing FBS for new publics once the contracts have been signed. It is not BPA's responsibility to plan and provide power for customers whose existence is not yet known at the time of signing the Regional Dialogue contracts.

Resource Removal

Customers should not be obligated to declare resources in the new contract period except where (i) a customer is purchasing under the Partial Requirements contract provisions, or (ii) the customer is either shifting from a Full Requirements to a Partial Requirements or from Partial Requirements to Full Requirements service. In addition, (iii) a Block or Block/Slice customer may wish to shift to Full or Partial Requirements service during the term of the contract. Provided that sufficient notice is given to BPA, this shift in service should be permitted, but BPA can reasonably require that such a customer comply with the resource declaration requirements of Partial or Full Requirements service, both at the time of the shift in service, and subsequently for the remainder of the contract.

Block and Slice/Block customers have limited their purchases from BPA to well-defined products that limit BPA's obligation to serve. The flip side of this is that these customers have taken on the obligation to meet the remainder of their retail loads without reliance on BPA. Accordingly, there is no reason for Block and Slice/Block customers to have to declare or undeclare non-federal resources during the entire term of the contract (with the exceptions noted immediately above associated with a change in type of service or Partial Requirements service). BPA's obligation to serve will not be affected by customers' individual choices regarding the use of non-federal resources and power supplies, either owned by the customers or purchased from third parties. There is no economic consequence to BPA, or other BPA customers, of changes in the non-federal resource decisions of Block and Slice/Block customers, and so there is no need to justify resource declaration or undeclaration requirements. Tacoma Power supports BPA's proposal to offer a limited resource removal right for load loss a customer may experience within a specific rate period.

Take-or-Pay Requirements

BPA proposes that purchases of both Tier 1 and Tier 2 power would be on a take-or-pay basis (§III.B.12). Tacoma Power generally agrees with this proposal, because it will help ensure both repayment of BPA's debts to the U.S. Treasury and the lack of cross-subsidies between Tier 1 and Tier 2 products.

However, if a customer is required to sign a take-or-pay contract with BPA, BPA has a reciprocal obligation to keep the costs of power under that contract under control. This is a natural, standard, and reasonable *quid pro quo* in any commercial arrangement. (See also Tacoma Power's comments on Cost Control.)

Conservation

Tacoma Power supports the Public Power Council comments that conservation between FY02 and FY10 be included in the determination of the HWMs. Additionally, Tacoma Power supports that utilities should receive credit for directly funded conservation.

As a fundamental part of the approach to allocation, utilities will be individually responsible for making commitments relative to conservation. Each utility will be responsible for managing load growth and in many circumstances one of the most effective and economical ways of doing so is through acts of conservation. If specific utilities determine the need for assistance in pursuing conservation Tacoma Power would support BPA offering conservation programs to individual utilities who would be directly responsible for costs and benefits relating to that service. Programs like Con-Aug should be offered to customers as a Tier 2 service of which the requesting customers desiring the product would be responsible for the costs and benefits incurred by that product.

Tacoma Power acknowledges that this is different from past practices and because markets are not completely perfect a modest amount of transformation costs included in Tier 1 could benefit everyone. Tier 1 customers could support a limited cost directly related to market transformation going forward in the new contract period. Elimination of CRC and Con Aug from Tier 1 would also avoid future arguments about the beneficiaries versus the payers of the costs of these programs.

Renewable Resources

Tacoma Power does not support Tier 1 customers paying for the acquisition of Tier 2 renewable resources. Customers electing to purchase renewable resources from BPA to serve Tier 2 loads should pay for these resources. That is part of the cost of Tier 2. Research, development and integration are all costs customers that do not purchase BPA's Tier 2 resources face having to pay, and BPA should not subsidize Tier 2 by having Tier 1 customers pay for the associated acquisition costs of obtaining suitable Tier 2 resources. A possible alternative is having Tier 2 customers pay short-term market rates while BPA and individual customers determine the best alternatives for the customer's Tier 2 loads.

Tacoma Power in general supports BPA's proposal that public power customers share with BPA their renewable resource acquisition plans for the next 5-10 years prior to each rate case, but this requirement should be rolled into the Resource Adequacy reporting requirements. Additionally the information reported should only be used as a means for reporting and not for any other purposes or decisions.

Transfer Service

The Direct Assignment Guidelines appear to be fair and clear but could be strengthened by requiring customers to submit up-front payment of construction costs.

Tacoma Power agrees that BPA's proposals would be positive steps to advance the quality of service, especially the proposals that BPA (i) formalize communications between parties, and (ii) take a proactive stance in working with third-party transmission providers. On a region-wide basis, any action to increase communication and coordination is helpful. Tacoma Power also agrees that BPA's ability is limited in the area of forcing transfer service providers to provide levels of service quality to GTA customers that equal the level provided to the transferring utility's native load customers. Tacoma Power recommends BPA focus on increasing communication and coordination, and resist the urgings of some parties to try to force specific planning standards on third-party transfer service providers.

Tacoma Power prefers that BPA hold the transfer contract(s) rather than the utility benefiting from transfer service. In situations such as Tacoma Power's territory with multiple small GTA customers, BPA and the transmission provider gain efficiency through BPA dealing with the transmission provider directly. In situations with one isolated GTA customer of moderate size, BPA may gain efficiency by allowing the customer to hold the contract. Tacoma Power agrees that BPA needs to carefully define the reimbursement process in cases where the customer holds the contract. Additionally, Tacoma Power encourages BPA to actively pursue situations in which it may be more cost effective to directly connect individual customers to BPA instead of relying on transfer service as a means of receiving power.

Transfer service should only be used to meet "requirements loads" as defined in statute; however, the costs of transmitting power products beyond Tier 1 obligations should be the responsibility of the individual transfer customers. Where all Tier 1 customers are responsible to share in the costs associated with transfer service, only transfer service associated with serving Tier 1 should be included in the Tier 1 costs. Ultimately transfer service costs should be included in the Transmission Services revenue requirement and not the Power Services rates, because they are costs associated with transmission. Tacoma Power encourages BPA to make a determination for the FY2010-2011 rate period for both Power and Transmission rates as to where the transfer service costs should lie.

Tacoma Power is in agreement with BPA that the complexity of the day-to-day implementation of transmission services has significantly evolved over the past 10 years. As many BPA customers in the region resolve to actively pursue various means of relieving congestion and seeking other long-term transmission solutions, those customers should be responsible for

making their own transmission arrangements in the new contract period and not rely on BPA to do so for them. Tacoma Power is responsible for procuring the necessary additional transmission capacity required to meet loads above our Net Requirements; in many situations that may require the purchase of additional transmission and/or additional staffing. While Tacoma Power recognizes BPA's need for additional staffing for transfer service, that additional cost should be the responsibility of the transfer customers receiving the benefit of such staffing and not the responsibility of all Tier 1 customers.

In the final analysis, Tacoma Power supports BPA's decision to cap the costs for the transfer of non-federal power to load to 30 MW or \$800,000 a year (whichever is less). Tacoma Power also supports BPA's decision not to pay for the transmission losses associated with the wheeling of non-federal power. In certain circumstances the losses associated with the transmission can be significant and it should not be the responsibility of all Tier 1 customers.

Cost Control

BPA has reviewed three options for long-term cost control in the Policy Proposal: a regional cost review (RCR) process, the cost management group (CMG), and inclusion of costs in BPA's rate proceedings. For a variety of reasons, BPA has proposed the RCR process. Tacoma Power respectfully submits that the informality of the RCR process is insufficient, and that BPA's costs should also be subject to review in regular power and transmission rate cases.

Tacoma Power does not see a significant value in the creation of the CMG at this time, largely because of the reasons that BPA cites (p. 77). However, relying on the RCR alone is not sufficient. The reasons offered by BPA for not including cost review in rate cases rely on several unreasonable assumptions: (1) that there would be no RCR in advance of the rate case; (2) that including costs would make the rate cases lengthier; (3) that rate cases reduce public visibility; (4) that access to information in rate cases is limited to "parties"; (5) that collaboration on cost review would be lost; (6) that manager-level representation would be lost; and (7) that this change would increase the potential for litigation and FERC review of BPA's cost levels. These are addressed in turn:

1. The formal 7(i) process could easily be preceded by an RCR process.
2. Rate case schedules are established by the hearing officer. All parties to rate cases face the need to allocate scarce resources, and are unlikely to spend significant quantities of time on small cost issues. Triage of issues during a rate case is a constant need.
3. If a rate case is preceded by an RCR process, public visibility would not be reduced. Furthermore, BPA's rate cases are open to the public.
4. Entities sufficiently interested in BPA's costs and rates should become parties to the rate case. There is no evidence that parties have been unreasonably excluded from participation in the past, and so there is no reason to be concerned about such access in the future.
5. Again, if the RCR process precedes the rate case, opportunities for collaboration would not be lost. In fact, if the consequence for "failure" of the RCR process is that costs

would be reviewed in a rate case, with an initial decision by a neutral third party, there may be an incentive to compromise in the RCR process.

6. BPA's customers and other regional interests must decide how to allocate the scarce time of the relevant managers. Tacoma Power expects to continue making management available for these processes, because of the significance of BPA's costs and rates in Tacoma Power's overall cost structure.
7. Tacoma Power is not proposing a change in FERC's authority to review BPA's rates, which must be adequate to cover BPA's costs. Given this limited authority, Tacoma Power sees no increase in the potential for litigation over BPA's costs, compared with what exists today.

Cost control pertaining to the Regional Dialogue Contracts is of the utmost importance when signing a contract that will be effective for approximately twenty years. Thus, Tacoma Power has concluded that BPA should adopt the Regional Cost Review, which would be a less formal process, but should also not preclude cost issues from being raised in formal 7(i) processes. Customers would have to be careful to manage their resources during rate cases and limit arguments to cost elements with significant impact and potentially questionable value or justification. The hearing officer should also be empowered to render an initial decision on cost levels, which would be reviewed by the Administrator, who would in turn be free to accept, reject, or modify the initial decision. The Final Record of Decision in a 7(i) process would explain the Administrator's decision to accept, reject, or modify the hearing officer's decision.

Dispute Resolution

BPA has proposed a three-part approach to dispute resolution in the Policy Proposal (§XII). This approach can be summarized as follows (pp. 79-80):

1. Certain rate case issues would be decided by the hearing officer, whose decisions would be binding on the Administrator with two exceptions: cost recovery and compliance with a court order.
2. Certain contract issues, defined narrowly and based on facts, would be resolved by a neutral third party.
3. Other issues would be decided by the Administrator; in some cases, these issues would be decided based on neutral sources of information.

This three-part approach demonstrates considerable thought and attention to both the interests of BPA's customers and BPA's statutory obligations. Tacoma Power applauds BPA for opening the door to a greater degree of third-party involvement in dispute resolution than has been the case in the past, while operating within existing statutory constraints. Tacoma Power further agrees that a "one size fits all" approach is not the best way to proceed on this difficult but critical component of the new power sales contracts.

Before commenting on specific elements of BPA's proposal, Tacoma Power must emphasize the importance of this issue. Investment decisions will be made, by BPA, by its customers, and by retail consumers, during the course of the new power sales contract that must be able to rely on the terms and conditions of the wholesale power contract. In this regard, the contract must have

commercial reliability that approximates as much as possible standard methods of doing business. Tacoma Power recognizes that BPA has statutory requirements and obligations, but wishes to emphasize up front that the success of the new contracts is critically dependent on their commercial foundations. Customers are being asked to make take-or-pay commitments for both Tier 1 purchases and, possibly, Tier 2 purchases from BPA. Customers will be making choices on the margin between (a) federal Tier 2 products and (b) non-federal resources and services that will probably be offered by a variety of potential counterparties. Tacoma Power is strongly interested in purchases of Tier 1 power from BPA, and may be interested in Tier 2 products, depending on their commercial viability.

No contract can be expected to be complete or perfect, especially one expected to support power deliveries for almost two decades. It is almost a certainty that circumstances will arise that require interpretation of the contracts; in addition, BPA must set its rates to recover its costs. However, uncertainty about the future combined with statutory obligations cannot and should not be used to justify unilateral decision-making in all dimensions of the arrangement, including contract interpretation and rate setting.

Tacoma Power agrees that the overall construct (both the contracts and the tiered rates methodology) should be immutable over time, with narrowly defined exceptions for court orders, cost recovery, and subsequently enacted legislation. Tacoma Power does not agree, however, that this barrier should be established "in the rate" (see p. 83); rather, any barriers to and conditions precedent to change should be established in the contracts, subject to the understanding that the parties can agree to amend the contracts. Tacoma Power also agrees with the proposal that the hearing officer should be empowered to determine whether a proposed change is contractually prohibited, subject to a subsequent review by the Administrator that would focus on the question of whether the change is required to comply with a court order or to ensure cost recovery.

Regarding eligibility and the allocation of Tier 1 rights, Tacoma Power recommends that the outcome of the initial determination of HWMs be included in the customer's contract and expressed as a percentage of Tier 1 resource capabilities. However, the determination of the contractual HWMs should not be made in a rate case, but in a separate formal decision-making process. This process should, as BPA proposes in §III.B.2., be conducted in a public manner in accord with the methodology established in the Regional Dialogue ROD, which should reduce or at least minimize the potential for disputes and misunderstandings. The result of this HWM determination process would be a percentage for each preference customer, to be stated in the customer's contract, which would be applied to the capability of the Tier 1 resource pool in each rate case, or each rate period of the new contracts. Individual rate cases, and perhaps other processes, would determine the forecasted capability of the Tier 1 resource pool for each rate period. The rights to purchase (non-Slice) Tier 1 power for each rate period would then be set in diurnally differentiated monthly energy and, perhaps, capacity amounts for each rate period, based on the determination of the size of the Tier 1 resource pool and net requirements determinations.

In addition, the results of the upcoming 5(b)/9(c) policy review should also be incorporated into the contracts as an exhibit, so that the customers can rely on the policy for decisions regarding future resources. BPA has proposed that the tiered rates methodology would not be subject to "change" absent a new 7(i) process, and the same guarantee should be applied to the 5(b)/9(c) policy.

At this point in the process, Tacoma Power understands that BPA's Policy Proposal is only the beginning of a dialogue on this subject (among others). Considerable work is necessary to flesh out the elements of the three-part approach proposed by BPA and turn concepts and agreements in principle into actual contract language. Tacoma Power looks forward to working with BPA to develop specific contract language acceptable to all parties.

One important consideration that is not apparent in the Policy Proposal is the potential need for accelerated dispute resolution processes in order to accommodate commercial needs of both parties. The Policy Proposal articulates a three-part approach, one of which is tied to the 7(i) process. Other disputes might be referred to a neutral third party, whereas a third category would be reserved for the Administrator, but perhaps constrained by neutral sources of information. Tacoma Power has experienced lengthy delays in the resolution of disputes with some non-federal counterparties, and is interested in expedited dispute resolution wherever possible. Thus, one of the "design criteria" for dispute resolution should be the identification of opportunities for quick decision-making. For example, certain issues will have to be resolved before a rate case even starts (e.g., the size of the Tier 1 pool), which should put a natural time limit on any related dispute resolution process.

Tacoma Power supports the proposal that disputes of a "factual" nature, e.g., involving load and resource calculations, should be referred to a neutral third party to the greatest extent possible. Again, the neutral party should be given a reasonable but limited amount of time to render a decision, which should be binding on both parties except for clearly defined exceptions.

Regarding "cost migration", Tacoma Power is concerned about the possibility of Tier 2 costs "migrating" into Tier 1, which could happen for a variety of reasons. Each of these reasons (and any others identified in the near future) should be addressed in the tiered rates methodology and resolved in a manner that provides commercial reliability to purchasers of both Tier 1 and Tier 2 products. For example, there may be a disagreement about the allocation of joint costs between Tier 1 and Tier 2, or among Tier 2 products. This is a common problem facing regulatory agencies at the state level, who must address the recovery of costs from "regulated" and "unregulated" activities of investor-owned utilities. BPA should adopt a "direction of effort" approach to this problem, as opposed to a "but for" test. That is, internal cost-tracking systems should be established that support reasonable allocations of joint costs. The "but for" test assumes that all joint costs are fixed costs, would be incurred by BPA even if Tier 2 products were not offered, and thus should be recovered through Tier 1 rates. The allocation of joint costs is not simply an academic exercise: it directly affects the prices that BPA will ultimately charge for Tier 2 products, and the risks that BPA will assume in offering such products. Unless these costs and risks are properly allocated to Tier 2 products, BPA may assume too much risk relative to the prices being charged for such products, and thus may increase the likelihood that costs will

“migrate” to Tier 1. Given the overall goals of the Regional Dialogue process, this would be the wrong outcome.

Any changes that will affect the size of the FBS and the amount of power provided to customers under the regional dialogue contracts should be open to discussion and public review.

Transmission Issues

In order to ensure a smooth transition from the current contracts, transmission considerations must be measured. There should not be any discrimination among NT, PTP, federal, non-federal, Tier 1 and Tier 2 customers in access to transmission for Load Serving Entities. Load Serving Entities within the Northwest serving Northwest loads should be given preferential access to transmission in contrast to entities using Northwest transmission for the purpose of wheeling through or exporting power. A plan should be developed that describes how BPA intends to handle customers transitioning into the new power purchase contracts with BPA Power Services.

Waiver of Rights

BPA proposes three types of “waivers” in the Policy Proposal regarding preference customers.

- First, preference customers would be required to “forego” requests for billing credits for new resources (p. 19).
- Second, preference customers would be required to “settle” their residential exchange rights (p. 20).
- Third, preference customers would have to “agree not to challenge” the tiered rates methodology, once established (p. 29).

The first two waivers of rights are essential components of the tiered rates construct, and appear reasonable in order to avoid the costs of new resources being melded into BPA's Tier 1 rate structure. (However, if preference customers are going to waive the rights to residential exchange benefits and billing credits, then funding to the IOU residential ratepayers must be adjusted downward over time to reflect the fact that the Tier 1 rate will not be rising as fast as it otherwise would.)

The third “agreement not to challenge” is very broadly worded in the Policy Proposal. It is not clear whether BPA intends this “agreement” to cover only the Record of Decision on the tiered rates methodology, or to cover implementation of that methodology over the term of the contract. If the former, then no contractual provision regarding the right to challenge is necessary if the tiered rates methodology is completed before the contracts are offered, which is essential. Once the ROD on the tiered rates methodology is issued, interested parties will have a statutorily

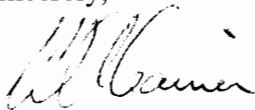
defined amount of time to challenge that ROD in the Ninth Circuit. Once that window of opportunity closes, BPA will not have to worry about future challenges to the methodology itself. However, it is likely that issues will arise in the implementation of the methodology during the term of the contract, and customers should not be required to waive any right to challenge BPA's approach to those issues. Indeed, the section on dispute resolution in the Policy Proposal appears to contemplate such challenges. Thus, the language on p. 29 is overly broad. BPA could decide to complete the §7(i) process 90 days before offering the new power sales contracts, and thus could avoid any contractual language requiring customers to agree not to challenge the methodology. In general, customers should not be requested to effectively "waive" any statutory rights through the signing of a contract as a condition of exercising their statutory right to purchase power from BPA until a complete and comprehensive agreement on the new contracts has been reached.

Resource Adequacy

Tacoma Power supports the concept of establishing energy and capacity standards for the region through the Regional Resource Adequacy Forum. As a stakeholder participant in both the policy and technical Forums, we appreciate the diligent effort that the Northwest Power and Conservation Council, BPA and other participants have put into the process. Although we recognize that there is still work to be done, we are confident that this effort will be successful – that this process will yield an effective well vetted consensus driven policy and framework for resource adequacy. We agree with Bonneville's position that mandatory resource adequacy standard compliance should not be a provision in power sales contracts. Further, we suggest that Bonneville should not revisit this position if the work of the Resource Adequacy Forum is not complete prior to the publication date of the Long-Term Regional Dialogue Policy and ROD. To date, the Resource Adequacy Forum has achieved significant consensus on an energy standard and is getting close in this regard on a capacity standard. Establishment of adequacy standards for the region is a complex and time consuming effort. It would not be in the best interest to rush this effort or to establish standards that are not adequately analyzed and vetted.

Thank you again for the opportunity to provide comments on this important policy proposal. Should you have any questions regarding these comments please contact me at (253) 502-8203.

Sincerely,



William Gaines
Superintendent/COO