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REBUTTAL TESTIMONY OF

ALLEN L. BURNS AND JOHN L. ELIZALDE

Witnesses for Bonneville Power Administration

SUBJECT: Rebuttal Testimony for Power Rates Design Policy

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4

5 **SUBJECT: REBUTTAL TESTIMONY FOR POWER RATES DESIGN POLICY**

6 **Section 1. Introduction and Purpose of Testimony**

7 *Q. Please state your names and qualifications.*

8 A. My name is Allen L. Burns. My qualifications are contained in WP-02-Q-BPA-08.

9 A. My name is John L. Elizalde. My qualifications are contained in WP-02-Q-BPA-19.

10 *Q. Have you previously filed testimony in this proceeding?*

11 A. Yes. We previously sponsored direct testimony on Bonneville Power Administration's
12 (BPA) Power Rate Design Policy. Burns and Elizalde, WP-02-E-BPA-08.

13 *Q. What is the purpose of your rebuttal testimony?*

14 A. The purpose of this testimony is to respond to the direct testimony filed by parties on
15 BPA's power rate design policy.

16 *Q. How is your testimony organized?*

17 A. This testimony is organized in four sections. Section 1 outlines the purposes of our
18 testimony. Section 2 responds to arguments regarding Power Rate Design Policy made
19 by: (1) public agency parties; (2) investor-owned utilities (IOU) parties; (3) direct
20 service industry (DSI) parties; and (4) stakeholder/constituent parties. Section 3 responds
21 to issues raised about the scope of this rate case. Finally, Section 4 addresses some
22 remaining issues on the Residential Exchange Settlement.

23 **Section 2. Power Rate Design Policy**

24 ***Public Agency Parties***

25 *Q. Western Public Agencies Group (WPAG) argues that BPA's competitive position is not a*
26 *major issue in the rate case; but rather, BPA is confronted with its more traditional*

1 *problem of having more demand than supply. Cross, et al., WP-02-E-WA-01, at 5.*

2 *Please respond.*

3 A. We conclude from WPAG's testimony that they are suggesting we do not need to worry
4 about our competitive position. Our testimony in WP-02-BPA-08, at 3-4, discussed
5 changing market conditions and the increase in demand for power marketed by BPA.
6 Although not termed a "major issue," BPA must continue to concern itself with the
7 market and constantly assess and undertake actions that ensure that BPA remains
8 competitive. The market is cyclical and volatile. If BPA allows its costs and rates to
9 increase and then market prices fall as they did in 1996, BPA could again find itself in a
10 position similar to its position in 1996.

11 Q. *WPAG argues that BPA's Initial Rate Proposal does not correctly implement the Power*
12 *Subscription Strategy Record of Decision (Subscription ROD) because BPA has now*
13 *committed to substantially greater sales of power to both the DSIs and the IOUs than was*
14 *contemplated in the Subscription ROD due to extreme political pressure placed on BPA*
15 *by some DSIs, the state public utility commissions (PUC), and certain IOUs. Cross,*
16 *et al., WP-02-E-WA-01, at 6. Do you agree?*

17 A. We do not agree with WPAG's characterization. BPA is attempting to implement the
18 basic goals of the Subscription Strategy. As described in our testimony (WP-02-BPA-08,
19 at 7, lines 18 and 19), BPA's proposed rates are designed to implement the four goals of
20 the Subscription Strategy. The proposed rates promote the spread of the benefits of the
21 Federal Columbia River Power System (FCRPS) while avoiding increases in average
22 Priority Firm (PF) rates (*see Keep, et al., WP-02-E-BPA-17*). Our original testimony
23 states that we are putting rates into effect that will allow BPA to meet the net firm load
24 requirements of its preference customers, offer a combination of power and financial
25 benefits to regional IOUs for the benefit of their residential and small farm consumers,
26 and serve a significant portion of the DSI load at competitive rates.

1 As we testified in WP-02-BPA-08, at 11, BPA is considering increasing the
2 amount of power available to the IOUs from 1,800 average megawatt (aMW) to
3 1,900 aMW. The decision of whether to increase to 1,900 aMW will be made in a
4 separate process and would modify the 1998 Subscription ROD. This increase is not an
5 issue in this rate case; however, what is an issue in this rate case is how the costs of this
6 action are or would be reflected in rates. In regard to the DSIs, the Subscription ROD
7 committed no specific amount of service to the DSIs. This is consistent with BPA's
8 Federal Register Notice, *see* Department of Energy, BPA, 2002 Proposed Wholesale
9 Power Rate Adjustment, Public Hearing and Opportunities for Public Review and
10 Comment, 64 Fed. Reg. 44318 at 44322 (1999), which stated that sales to the DSIs are an
11 open issue in this rate case. We indicated in our original testimony (Burns and Elizalde,
12 WP-02-E-BPA-08, at 8) that the DSI proposal differs from the proposal in the
13 Subscription ROD. However, it still meets the four basic goals of the Strategy. For
14 further discussion *see* Berwager, *et al.*, WP-02-E-BPA-38. Putting aside the political
15 pressure to increase the amounts of power and/or benefits that BPA will provide to either
16 the IOUs or the DSIs, we believe BPA's Initial Proposal is correctly implementing the
17 goals of the Subscription Strategy.

18 *Q. WPAG argues that it appears that BPA is increasing the price and constraining the*
19 *supply of Federal power available to preference customers to ensure that there is an*
20 *adequate supply of Federal power to meet the power supply demands of the IOU and DSI*
21 *customers. Cross, et al., WP-02-E-WA-01, at 6. Likewise, Springfield Utility Board*
22 *(SUB) contends that such sales were not included in the Subscription ROD and that*
23 *neither the DSIs nor the IOUs have rights to such power sales. As a result, SUB argues*
24 *that its rights to the lowest cost based priority firm power have been eroded. Nelson,*
25 *WP-02-E-SP-01, at 2. Please respond.*
26

1 A. We do not agree with WPAG or SUB's characterizations. BPA will meet the net firm
2 load requirements of its preference customers. This section 7(i) rate proceeding will
3 establish the rates that will apply to power sales under Subscription contracts. The actual
4 amount of power that BPA is obligated to sell to preference customers is determined by
5 contract. In its Initial Proposal, BPA proposed to meet the needs of its preference
6 customers while avoiding increases in the average PF rate. As stated in the Subscription
7 ROD, the lowest cost-based PF rate is available to preference customers that sign
8 contracts in the Subscription window for firm power to meet their regional firm power
9 loads. In making the PF rate available to its preference customers, BPA is under no
10 obligation to restrict service to IOUs for service to their residential customers and DSIs in
11 order to further lower the PF rate. BPA notes that there are no constraints on the supply
12 of Federal power available to preference customers.

13 Consistent with meeting the needs of its preference customers, BPA expects to
14 provide some service to IOUs and DSIs. This service will be consistent with the stated
15 goals of BPA's Power Subscription Strategy to: (1) spread the benefits of the FCRPS as
16 broadly as possible, with special attention given to the residential and rural customers of
17 the region; and (2) avoid rate increases through a creative and businesslike response to
18 markets and additional aggressive cost reduction. In regard to the DSIs, the Subscription
19 Strategy committed no specific amount of service to the DSIs and our current proposal to
20 now offer the DSIs a specific amount of power is a logical implementation step. For
21 more information on the DSI proposal, *see* Berwager, *et al.*, WP-02-E-BPA-38.

22 Q. *SUB argues that BPA's recently released newly revised draft policy proposal regarding*
23 *Subscription power sales to customers and customers' sales of firm resources is eroding*
24 *SUB's rights to the lowest cost-based priority firm power under BPA's rate case*
25 *proposal. Nelson, WP-02-E-SP-01, at 2. Please respond.*
26

1 A. SUB is referring to a separate and independent policy proposal by BPA on the
2 determination of customers' net requirements under 5(b) and 9(c) of the Northwest Power
3 Act that is not within the scope of this rate proceeding. SUB, and any other interested
4 parties, had an opportunity to submit comments on BPA's revised draft policy proposal to
5 BPA as provided in BPA's Federal Register Notice, 64 Fed. Reg. 58039 (October 28,
6 1999).

7 Q. WPAG argues that BPA may be considering establishing different or longer Subscription
8 periods for certain customer classes, such as tribal utilities, and that BPA should not
9 create any such exceptions, which would be unduly discriminatory. *Cross, et al.,*
10 *WP-02-E-WA-01, at 12. Please respond.*

11 A. BPA's decision regarding the Subscription period is not an issue in this rate case. Please
12 see the Subscription ROD and BPA's letter to Customers and Interested Parties,
13 Enclosure 2 "Summary of Product Catalog Change," attached to *Keep, et al.,*
14 *WP-02-E-BPA-43.*

15 Q. *The Public Power Council (PPC) argues that BPA kept its "rate pledge" of avoiding rate*
16 *increases by shifting money from the Power Business Line (PBL) to the Transmission*
17 *Business Line (TBL), whereas PPC contends the PF-02 rate is really about 9 percent*
18 *higher than PF-96. Leone and Robinson, WP-02-E-PP-01, at 8; Opatrny et al.,*
19 *WP-02-E-PP-02, at 6. PPC calculates that \$84 million in costs are migrating from PBL*
20 *to TBL. Id. Please respond.*

21 A. PPC appears to misunderstand BPA's "rate pledge" as expressed in the Subscription
22 ROD. One of the Subscription Strategy's goals is to provide rate stability and to avoid
23 rate increases in the PF rate. This goal has become known as the "rate pledge." The
24 Subscription ROD, however, specifically stated that rates would be decided in the Rate
25 Case: "The Subscription Strategy does not establish any rates or rate designs. The
26 establishment of rates and use of rate design can be determined only in a formal hearing

1 under section 7(i) of the Northwest Power Act.” See, e.g., Power Subscription Strategy
2 ROD at 115.

3 The Subscription Strategy goal of no PF rate increase was never intended by BPA
4 to cover items functionalized to transmission, including costs associated with ancillary
5 services. BPA has been functionalizing costs and revenues to generation and
6 transmission for years. These practices have been aired and tested in prior rate
7 proceedings and reviewed by the Federal Energy Regulatory Commission (FERC). The
8 few changes BPA is proposing are in response to FERC policies related to the unbundling
9 of transmission and ancillary services from power rates. As in previous rate cases, BPA
10 continues to functionalize costs in a manner consistent with jurisdictional utilities.
11 See DeWolf, *et al.*, WP-02-E-BPA-13 and WP-02-E-BPA-39. See also DeClerck, *et al.*,
12 WP-02-E-BPA-26 and WP-02-E-BPA-51. BPA has not moved costs from power to
13 transmission to achieve the rate goal, and PPC has provided no evidence or support for its
14 contention.

15 *Q. PPC argues that BPA’s proposal for the IOUs to settle the Residential Exchange is not*
16 *consistent with BPA’s Power Subscription Strategy policy that the power BPA provides*
17 *the IOUs be charged a “PF-equivalent” rate. BPA has suggested a number of “targeted*
18 *adjustment charges (TAC)” and other mechanisms that expose a significant portion of*
19 *preference requirements load to additional charges tied to market prices. PPC believes*
20 *that these market charges should be eliminated; however, should such charges be*
21 *retained, BPA should charge the IOUs a rate equivalent to the average rate that*
22 *preference customers actually pay for requirements service, not the lowest available PF*
23 *rate. O’Meara, et al., WP-02-E-PP-07, at 2. As an example, PPC states that BPA’s*
24 *proposal to increase the IOUs’ Subscription amount from 1,800 megawatt (MW) to*
25 *1,900 MW is a cost increase that will not incur a targeted adjustment charge.*
26 *Opatrny et al., WP-02-E-PP-02, at 12. Please respond.*

1 A. One of the goals in BPA's Subscription Strategy is the spreading of Federal benefits.
2 Along with that, the Subscription ROD also noted BPA's expectation that the rates for
3 both public agency customers (PF preference) and the residential and small farm load of
4 IOUs (Residential Load (RL) or PF Exchange Subscription) would be approximately
5 equal, subject to review and establishment in BPA's rate case. The amount of power
6 offered to the IOUs under the settlement, however, is fixed at either 1,800 aMW or
7 1,900 aMW. IOUs would not be able to purchase any additional power after the
8 Subscription window closes at the RL or PF Exchange Subscription rates.

9 Any additional requirements load placed on BPA by the IOUs beyond the
10 Residential Exchange Settlement amounts during the Subscription window will be at the
11 NR rate. BPA has reconsidered its previous proposal to not apply a TAC to the NR rate.
12 BPA now proposes to establish a TAC for the NR rate. Please see the testimony of
13 Arrington, *et al.*, WP-02-E-BPA-49. This change will help ensure equivalent treatment
14 for both IOU and public agency loads not forecast to be served during the 2002–2006 rate
15 period.

16 BPA has not changed its proposal to consider increasing the IOUs' Subscription
17 amount from 1,800 aMW to 1,900 aMW. We stated in our testimony in WP-02-BPA-08
18 at 12, lines 2 to 6, that BPA will not increase the IOU settlement amount from
19 1,800 aMW to 1,900 aMW unless we can do so without negatively affecting BPA's
20 ability to meet our rate pledge (as defined in Keep, *et al.*, WP-02-E-BPA-17), Treasury
21 Payment Probability (TPP) goal, the DSI proposal, or BPA's fish and wildlife
22 commitments.

23 In addition, similar treatment exists between the public customers and the IOUs
24 because the Cost Recovery Adjustment Clause (CRAC) will also apply to the RL and PF
25 Exchange Subscription rates. *See* DeWolf, *et al.*, WP-02-E-BPA-39.
26

1 Q. PPC, Northwest Requirements Utilities (NRU), and SUB argue that BPA's proposed
2 reserve level of \$1.26 billion is too high. Leone and Robinson, WP-02-E-PP-01, at 1;
3 Nelson, WP-02-E-SP-01, at 2; Saven, WP-02-E-NI-01, at 8. The reserve level should not
4 exceed \$850 million. Leone and Robinson, WP-02-E-PP-01, at 5; *Id.* Please respond.

5 A. The \$1.26 billion estimate is a high-end estimate of the expected value of a broad range
6 of potential reserve levels by the end of Fiscal Year 2006. This estimate assumes that
7 reserves will not be reduced because of distributions under the Dividend Distribution
8 Clause (DDC). This reserve level is not a plan or a target *per se*, but part of a range of
9 outcomes from a package of risk mitigation tools that have been designed to achieve
10 BPA's TPP policy standard. We acknowledge the concerns expressed by PPC, SUB, and
11 NRU in building reserves, and now propose to reduce the threshold for considering
12 dividend distributions under the DDC from \$1.2 billion to \$950 million. *See* DeWolf,
13 *et al.*, WP-02-E-BPA-39.

14 ***Northwest Investor-Owned Utility Parties (Northwest IOUs)***

15 Q. The Northwest IOUs argue that BPA should functionalize costs between power and
16 transmission in the same manner as is required of public utilities by FERC.
17 *Eakin et al.*, WP-02-E-AC/GE/IP/MP/PL/PS-01, at 3-4. Please respond.

18 A. Concerns by parties regarding the functionalization of costs between transmission and
19 power should be addressed with specifics. *See* the testimony of DeWolf, *et al.*,
20 WP-02-E-BPA-39.

21 BPA is subject to FERC review and approval of BPA's wholesale power and
22 transmission rates. BPA counsel has advised that the standard for FERC approval is
23 whether: (1) rates are sufficient to assure repayment of the Federal investment in the
24 FCRPS over a reasonable number of years after first meeting BPA's other costs; (2) rates
25 are based on BPA's total system costs; and (3) transmission rates equitably allocate the
26

1 cost of the Federal Transmission System between Federal and non-Federal power using
2 the system. This standard is established by statute, rather than by BPA policy.

3 *Q. The Northwest IOUs are concerned over the finality of FERC's approval of BPA's power*
4 *rates prior to full functionalization of costs to transmission. There could be*
5 *misfunctionalized costs. The Northwest IOUs recommend that BPA remove the cap on*
6 *the CRAC in order to collect any costs from power customers that are wrongly*
7 *functionalized to transmission. If the cap is not removed, then power sales contracts*
8 *should contain a specific provision permitting a rate adjustment if necessary to collect*
9 *any costs functionalized to transmission that FERC determines are not transmission*
10 *costs. Eakin et al., WP-02-E-AC/GE/IP/MP/PL/PS-01 at 15. Please respond.*

11 *A.* The proposed CRAC design is not being changed to accommodate the potential for
12 changes in the functionalization of costs due to the transmission rate proceeding and
13 review by FERC. BPA has, however, reviewed its risk analysis in Non-Operating Risk
14 Model (NORM) for the possibility that these uncertainties are not captured adequately.
15 *See Lovell, et al., WP-02-E-BPA-40.* The basic design of risk mitigation tools in BPA's
16 Initial Proposal is adequate to accommodate the potential for any change in
17 functionalization that occurs after wholesale power rates are set.

18 *Q. The Northwest IOUs do not support BPA's proposed staggered contract terms. They*
19 *argue that staggered contract terms for "much of BPA's power sales" threaten BPA's*
20 *and the region's ability to arrive at a consensus about BPA's future role and increases*
21 *BPA's financial risk. Eakin, et al., WP-02-E-AC/GE/IP/MP/PL/PS-01, at 15-16. Please*
22 *respond.*

23 *A.* BPA's decision regarding staggered contract terms was decided in the Subscription
24 Strategy and is not an issue in this rate case. The rate issue is whether, given staggered
25 contract terms, BPA's revenues will be able to recover its costs. Since BPA is setting
26 power rates for the five-year rate period, rates for contracts with terms longer than

1 five years will be determined in a future section 7(i) proceeding. Staggered contract
2 terms assure BPA of expected revenues, thereby reducing financial risk.

3 *Q. The Northwest IOUs argue that BPA should plan on expected financial reserves by 2006*
4 *of \$500 million, which is within the range of planned BPA financial reserves in recent*
5 *history. Any unexpected cost underrecovery should be collected through an uncapped*
6 *CRAC. Eakin et al., WP-02-E-AC/GE/IP/MP/PL/PS-01, at 15-16. Please respond.*

7 *A. BPA calculates financial reserves as part of the risk mitigation process. It is not a target*
8 *or an input as implied by the question. As stated previously, BPA is proposing*
9 *adjustments to the DDC threshold level, which address the concern of a high expected*
10 *value of reserves. See DeWolf, et al., WP-02-E-BPA-39.*

11 With regard to the suggestion of an uncapped CRAC, BPA believes that an
12 uncapped CRAC is not consistent with BPA's goal of rate stability. We also believe that
13 an uncapped CRAC does not foster good business relationships between BPA and its
14 power customers. See Lovell, et al., WP-02-E-BPA-40.

15 ***Industrial Customers of Northwest Utilities (ICNU)***

16 *Q. ICNU proposes that BPA establish a "Ratemaking Separation" process where BPA*
17 *would establish revenues and revenue requirements for the generation and transmission*
18 *lines separately, and then each business line would develop their rates later. Wolverton,*
19 *WP-02-E-IN-01, at 16. How do you respond to this request?*

20 *A. While BPA does not disagree with the concept of "ratemaking separation" as proposed*
21 *by ICNU, we do not feel a separate process is necessary. See DeWolf, et al.,*
22 *WP-02-E-BPA-39.*

23 ***High Load Factor Group***

24 *Q. The High Load Factor Group (HLFG) argues that the proposed caps on the Demand*
25 *Charge and Load Variance charge be eliminated. HLFG argues that both caps distort*
26 *the market price signals and lead to economically inefficient solutions for society*

1 *regarding electrical capacity usage. Koehler et al., WP-02-E-HL-01, at 9. In particular,*
2 *the HLFG argues that the cap on the Load Variance charge shifts approximately*
3 *\$20 million annually to energy charges. Id. at 11. Please respond.*

4 A. We believe it is necessary to keep the price caps as proposed. This is based on the need
5 to balance the competing goals of pricing products to reflect costs versus concern over
6 the degree of rate impact in spreading the benefits of the FCRPS. BPA is mindful that its
7 rates, taken in total, must recover BPA's costs, taken in total. While we are moving
8 toward a rate design for power products that appropriately sends price signals at the
9 margin, BPA believes that there would be unreasonable rate impacts for some customers
10 if BPA designed rates to fully reflect market price signals. BPA believes these proposed
11 rates balance the above competing goals of rate stability and product pricing to reflect
12 cost.

13 ***Direct Service Industry Parties (DSIs)***

14 Q. *The DSIs argue that an excessive floor rate or typical margin frustrates BPA's*
15 *Subscription Strategy policy that its regional customers should all be served at equivalent*
16 *rates. The DSIs make recommendations regarding the section 7(c) typical margin and*
17 *floor rate and regarding BPA's rate design step used to calculate Northwest Power Act*
18 *rates. Wilcox and Waddington, WP-02-E-DS-02, at 9. Please respond.*

19 A. BPA believes that, as presently calculated, the floor rate does not frustrate the
20 Subscription Strategy and is not excessive. See Ebberts, WP-02-E-BPA-47 for BPA's
21 testimony regarding the floor rate. Furthermore, the Subscription Strategy ROD clearly
22 states that rates must be developed and established in accordance with the rate directives
23 in section 7 of the Northwest Power Act.

24 ***Stakeholder/Constituent Parties***

25 Q. *Northwest Energy Coalition (NVEC) argues that BPA's proposed power rate structure*
26 *does not encourage economic efficiency because of BPA's failure to give correct price*

1 signals. Because BPA's price is below market, BPA's customers will use power
2 unnecessarily. To provide a marginal price signal, NWECC proposes "any number of
3 'tiered rate' or 'inverted rate' mechanisms which are in common use around the country
4 to more closely approximate marginal cost rates." Weiss, WP-02-E-NA-01, at 26, lines 5
5 and 6. Please respond.

6 A. BPA cannot agree with NWECC on "any number of 'tiered rate' or 'inverted rate'
7 mechanisms" that are in use around the country because NWECC neither describes them
8 nor provides any detailed analysis to demonstrate the efficacy of such rate mechanisms.
9 As in 1996, BPA is proposing marginal cost pricing in its rate design. Such pricing
10 reflects the costs BPA incurs when it must purchase from the market. Although we are
11 mitigating our rate design in some cases, see Burns and Elizalde, WP-02-E-BPA-08, we
12 believe that once implemented, BPA rates with the marginal costs included will result in
13 greater economic efficiency than exists today.

14 **Section 3. Scope of Rate Case: BPA's Power Subscription Strategy**

15 Q. Alcoa, Vanalco, and Energy Services, Inc. (Alcoa, et al.) argue that BPA has relied upon
16 the decisions it made in the Subscription ROD or in private agreements outside the 7(i)
17 process to define the amount of power that it will sell to customer classes. Speer, et al.,
18 WP-02-E-AL/VN/EG-02, at 5. Please respond.

19 A. In developing rates, BPA must determine forecasts for sales BPA will make to BPA's
20 customer classes. BPA, however, does not establish its sales obligations to customers in
21 a rate case. Instead, power sales obligations are established in power sales contracts.

22 BPA's Subscription ROD did not establish a specific forecast of DSI sales to
23 include in BPA's initial proposal. As discussed in greater detail in the testimony of
24 Berwager, et al., WP-02-E-BPA-09, BPA worked with the DSIs to develop what is called
25 the Compromise Approach. The Compromise Approach serves as the basis for the DSI
26

1 sales forecast in BPA's Initial Proposal. The amount of DSI load BPA will offer to serve
2 at the Industrial Firm Power rate is being determined in this rate case.

3 The Subscription Strategy describes the manner in which BPA intends to serve its
4 preference customers. The Strategy did not establish a specific forecast of preference
5 loads that was included in BPA's Initial Proposal. The preference customer sales forecast
6 is being determined in the rate case.

7 BPA's Subscription ROD noted that regional IOUs can continue to participate in
8 the Residential Exchange Program after 2001. The Subscription ROD did not contain the
9 specific amounts of utilities' loads that would be eligible for the Residential Exchange.
10 Estimates for the Residential Exchange were developed and presented in BPA's Initial
11 Proposal and are subject to determination in the rate case. BPA's Subscription ROD
12 included a determination for settlement of the Residential Exchange Program for regional
13 IOUs. The settlement described in the Subscription Strategy was for benefits equivalent
14 to 1,800 aMW; and BPA is currently soliciting public comment in a separate process on
15 whether that amount should be increased to 1,900 aMW. Reflection of possible
16 participation in the settlements is properly based on the amounts BPA identified in the
17 Subscription ROD and the pending public comment process.

18 *Q. Alcoa, et al., argue that in the Subscription ROD and in a subsequent exchange of letters*
19 *with the state PUCs, BPA agreed to provide 1,800 aMW (and potentially 1,900 aMW) of*
20 *benefits, including 1,000 aMW of cost-based power, to regional IOUs. Speer, et al.,*
21 *WP-02-E-AL/VN/EG-02, at 5. Please respond.*

22 *A.* As noted above, the Subscription ROD included a determination for settlement of the
23 Residential Exchange Program with regional IOUs. (See Subscription ROD, page 51.)
24 The settlement described in the Subscription Strategy contains benefits equivalent to
25 1,800 aMW of Federal power, and was established in the Subscription Strategy, not in an
26 agreement with regional state PUCs. The state PUCs asked BPA to increase the amount

1 to 1,900 aMW. BPA is currently soliciting public comment in a separate process on
2 whether that amount should be increased to 1,900 aMW.

3 *Q. Alcoa, et al., argue that in the Compromise Agreement, BPA agreed to provide 870 MW*
4 *of cost-based power to signing DSIs. Speer, et al., WP-02-E-AL/VN/EG-02, at 5. Please*
5 *respond.*

6 *A.* As noted above, the Compromise Approach is discussed in greater detail in the testimony
7 of Berwager, WP-02-E-BPA-09. The amount of DSI load BPA will offer to serve at the
8 IP rate is being determined in this rate case.

9 *Q. Alcoa, et al., argue that it is wrong to adopt the allocation of power in the Subscription*
10 *ROD because there is an interrelationship between the amount of power sold to each*
11 *class of customer and the rate for that power, noting that large portions of past rate*
12 *cases have dealt with elasticities of demand for the rate classes. Speer, et al.,*
13 *WP-02-E-AL/VN/EG-02, at 5. Alcoa, et al., argue that BPA must use its authority to*
14 *acquire resources to provide an adequate, efficient, economical, and reliable power*
15 *supply rather than establish allocations of power to customer classes outside of the 7(i)*
16 *process. Id. Please respond.*

17 *A.* As noted above, actual sales to customers have never been established in a section 7(i)
18 process. Such sales are made through negotiations and power sales contracts.
19 Historically, sales forecasts in BPA's rate cases were based in large part on sales under
20 existing power sales contracts. In the current rate case, BPA is estimating or forecasting
21 sales for a rate period not covered by existing contracts. As noted above, BPA's forecast
22 of DSI sales, preference customer sales, and Residential Exchange Program sales are
23 being determined in the rate case. Residential Exchange Program settlement sales are
24 based on proposed sales as described in the Subscription Strategy, and may be revised in
25 a separate process. BPA is proposing to use its authority to augment the FCRPS
26 inventory as suggested by Alcoa, et al.

1 Q. *Alcoa, et al., argue that BPA has determined the proper rate for customers in another*
2 *forum and has worked backwards to force its costs and loads to support these rates.*
3 *Speer, et al., WP-02-E-AL/VN/EG-02, at 6. Please respond.*

4 A. BPA has not established the proper rates for customers in another forum. Prior to
5 development of the Subscription Strategy, BPA counsel advised that BPA's rates can
6 only be established in a section 7(i) proceeding, so the Subscription Strategy expressly
7 states that the Subscription Strategy does not establish any rates:

8 "It should be noted that BPA's Subscription Strategy does not establish any rates
9 or rate designs. The establishment of rates and use of rate design can be
10 determined only in a formal hearing under section 7(i) of the Northwest Power
11 Act. The comments and questions referenced above will be addressed in BPA's
12 power rate development process, which includes extensive opportunities for
13 public involvement. While final rate design decisions are not being made in the
14 Subscription Strategy, rate design approaches identified in the Subscription
15 Strategy will be part of BPA's initial power rate proposal, which is expected to be
16 published early in 1999."

17 *See, e.g., Power Subscription Strategy ROD at 115. Similarly, the Compromise*
18 *Approach did not establish any rates but helped develop BPA's Initial Rate Proposal.*

19 Q. *Alcoa, et al., argue that in the Subscription Strategy, the Administrator pledged that the*
20 *PF-02 rate would equal on average the PF-96 rate and this rate pledge was made before*
21 *the total costs to be collected for the rate period were determined. Speer, et al.,*
22 *WP-02-E-AL/VN/EG-02, at 6. Please respond.*

23 A. The Subscription Strategy notes that one of its goals is to "[a]void rate increases through
24 a creative and businesslike response to markets and additional aggressive cost
25 reductions." Subscription ROD at 3. The Subscription ROD also notes that "[t]he goal is
26 to have no increase in the current Priority Firm rate." *Id.* at 6. While BPA's goal is to

1 have no increase in preference customers' rates, these rates must be established in the
2 section 7(i) hearing. There is no guarantee that BPA's goal will be achieved.

3 *Q. Alcoa, et al., argue that BPA adopted a policy that the RL rate would approximately*
4 *equal the PF-02 rate. Speer, et al., WP-02-E-AL/VN/EG-02 at 6. Please respond.*

5 *A. The Subscription ROD states BPA's expectation that "[t]hese sales will be at a rate*
6 *approximately equal to the PF Preference rate, subject to establishment in BPA's rate*
7 *case and consistent with BPA's rate directives."* Subscription ROD at 16. This is
8 clarified by the Subscription ROD at 126.

9 BPA understands the parties' arguments regarding the level of the NR(1) rate
10 (now RL or PF rate) relative to the PF(1) rate. The Subscription Strategy signals BPA's
11 expectation that the rate for these IOU sales will be approximately equal to the PF rate.
12 BPA must establish its rates consistent with the rate directive contained in section 7 of
13 the Northwest Power Act, however, and in hearings conducted in accordance with the
14 procedures specified in section 7(i) of the Act. For this reason, BPA cannot state that the
15 RL or PF rates used for Subscription sales to the IOUs will be set at any particular level.
16 The level of the RL and PF rates can be established only in a section 7(i) hearing. While
17 it is possible that the RL and PF rates would equal the PF Preference rate, BPA cannot
18 make such a statement at this time.

19 *Q. Alcoa, et al., argue that BPA set the "conservation and renewable resource (C&R) rate*
20 *surcharge and rate credit" in the Subscription ROD. Speer, et al.,*
21 *WP-02-E-AL/VN/EG-02, at 6. Please respond.*

22 *A. BPA did not set the C&R Discount in the Subscription ROD. The Subscription Strategy*
23 *states that "[s]pecifically, in the rate case BPA plans to propose a base discount not to*
24 *exceed 0.5 mills per kilowatthour (approximately a total annual discount of*
25 *\$30 million)." Subscription Strategy at 18 (emphasis added). This is confirmed by the*
26 *Subscription ROD, which states the issue as "[s]hould BPA include a Conservation and*

1 Renewables Discount mechanism in BPA’s initial rate proposal?” Subscription ROD at
2 136 (emphasis added). Similarly, the Subscription ROD noted that “[t]hese are not final
3 decisions, but rather indications of the direction BPA’s initial rate proposal will take
4 when published in early 1999.” *Id.* at 137.

5 *Q. Alcoa, et al., argue that BPA engaged in negotiations with the DSIs for the purpose of*
6 *setting both the rate and amount of power that it would sell to the companies. Speer,*
7 *et al., WP-02-E-AL/VN/EG-02, at 6. Please respond.*

8 *A.* As discussed in greater detail in the testimony of Berwager, *et al.*, WP-02-E-BPA-09,
9 BPA’s discussions with the DSIs regarding the rate and amount of power that it would
10 sell to the companies were for the purpose of developing BPA’s initial proposal. The
11 DSI rate and the amounts of DSI power sales are being determined in the rate case.

12 *Q. Alcoa, et al., argue that the companies that agreed to the Compromise Approach are*
13 *precluded from arguing for service on terms other than those in the agreement. Speer,*
14 *et al., WP-02-E-AL/VN/EG-02, at 6. Please respond.*

15 *A.* BPA counsel has advised that parties are not required to contest every issue in BPA’s rate
16 proceeding and that parties may choose not to contest certain issues. For example, BPA
17 held rate case workshops prior to publishing its Initial Proposal. The purpose of these
18 workshops was to get potential rate case parties to understand what BPA was planning to
19 propose, in an effort to reduce the adversarial nature of this rate case.

20 *Q. Alcoa, et al., argue that in the Federal Register Notice for the rate case, the*
21 *Administrator attempts to exclude from testimony and argument in the rate case any*
22 *attempt to revisit decisions made in the Subscription ROD, including fish mitigation*
23 *costs, the TPP range, and the C&R “charge.” Speer, et al., WP-02-E-AL/VN/EG-02,*
24 *at 6-7. Please respond.*

1 A. BPA worked with customers and other interested parties for over a year in developing
2 BPA's Subscription Strategy Proposal, which was released on September 18, 1998, for
3 public review. BPA received voluminous public comments and evaluated those
4 comments in BPA's Subscription ROD, issued on December 21, 1998. Also on that date,
5 BPA issued its Subscription Strategy. Given that BPA had a separate public process to
6 develop the Strategy and, as noted above, no final rate decisions were contained in the
7 Strategy, it would not make sense and would be impractical for BPA to revisit all of the
8 issues decided in the Subscription Strategy in the rate case. For this reason, BPA noted in
9 the Federal Register that the rate case was to establish rates, not to revisit issues already
10 decided in the Subscription Strategy. Issues related to the Fish and Wildlife Funding
11 Principles, their implementation, and the TPP standard are addressed in the testimony of
12 DeWolf, *et al.*, WP-02-E-BPA-39. Issues related to "fish mitigation" costs and the TPP
13 range are addressed in the testimony of Lovell, *et al.*, WP-02-E-BPA-40. Issues regarding
14 the C&R Discount have been addressed in greater detail above, and in the testimony of
15 Esvelt, *et al.*, WP-02-E-BPA-55.

16 *Q. Alcoa, et al., argue that the Subscription process did not comply with section 7(i) of the*
17 *Northwest Power Act. Speer, et al., WP-02-E-AL/VN/EG-02, at 7. Please respond.*

18 A. BPA counsel has advised that BPA's rates must be established in a section 7(i) hearing
19 and that BPA's Subscription ROD did not establish any rates.

20 *Q. Alcoa, et al., argue that the Administrator has entered into agreements with parties to the*
21 *rate case to limit debate on several key issues and if parties cannot get their alternatives*
22 *into the record there is no chance that their alternatives will be adopted by BPA. Speer,*
23 *et al., WP-02-E-AL/VN/EG-02, at 7-8. Please respond.*

24 A. As noted above, BPA counsel has advised that parties are not required to contest every
25 issue in BPA's rate proceeding and parties may choose not to contest certain issues. If
26 parties choose not to contest issues, they choose not to present alternatives for the record.

1 Alcoa and Vanalco, however, have not executed any agreement that limits their ability to
2 raise issues in the rate case.

3 **Section 4. Residential Exchange Settlement and Rate Making Separation**

4 *Q. Alcoa, et al., argue that the impetus for the proposed Residential Exchange settlements*
5 *was that the state PUCs wanted more benefits, wanted the amount of benefits to be stable*
6 *and not subject to arbitrary change by BPA, and were concerned that, with the potential*
7 *sale of IOU assets, the Residential Exchange benefits might be jeopardized. Speer, et al.,*
8 *WP-02-E-AL/VN/EG-02, at 14. Please respond.*

9 *A. While we agree that the PUCs may be concerned about the issues regarding Residential*
10 *Exchange benefits to the IOUs, the settlement offer was established in the Subscription*
11 *ROD, not in an agreement with regional state PUCs. The settlement offer was for*
12 *benefits equivalent to 1,800 aMW. BPA did solicit input from the state PUCs on how the*
13 *1,800 aMW should be allocated and in that process the PUCs indicated a need for an*
14 *additional 100 MW to come to concurrence on an approach. BPA is currently soliciting*
15 *public comment in a separate process on whether that amount should be increased to*
16 *1,900 aMW.*

17 *Q. Alcoa, et al., argue that the value of the proposed settlement is \$675 million for the rate*
18 *period and the value of the Residential Exchange benefits is \$182 million for the rate*
19 *period and BPA does not explain why it would settle Residential Exchange claims for*
20 *more than the claims are worth. Speer, et al., WP-02-E-AL/VN/EG-02, at 15. Please*
21 *respond.*

22 *A. There are a number of variables that could result in the IOUs receiving substantially more*
23 *exchange benefits than forecasted in BPA's rate case, including the actual size of the*
24 *exchange load and the actual Average System Cost of the utility. BPA developed its*
25 *settlement offer based on the record of the Subscription ROD and BPA's general*
26 *recognition of these variables. BPA has not yet negotiated or offered the proposed*

1 settlement agreements. BPA will be conducting a separate public comment process on
2 the proposed settlements. The issue of whether the proposed settlements are well
3 founded should be raised in that forum.

4 *Q. Alcoa, et al., argue that BPA traditionally would serve the net requirements of its*
5 *preference customers and then would make arrangements to serve the DSIs. Speer, et al.,*
6 *WP-02-E-AL/VN/EG-02, at 15. Please respond.*

7 *A. BPA counsel has advised that BPA first serves its preference customers' net requirements*
8 *and then its IOU customers' net requirements. BPA has also traditionally implemented*
9 *the Residential Exchange Program. BPA counsel has advised that BPA has no statutory*
10 *obligation to offer the DSIs a long-term power sales contract under section 5 of the*
11 *Northwest Power Act for service after 2001.*

12 *Q. Alcoa, et al., argue that the proposed IOU sale reduced the amount of power that BPA*
13 *would otherwise have to serve DSI load under normal water conditions. Speer, et al.,*
14 *WP-02-E-AL/VN/EG-02, at 16. Please respond.*

15 *A. BPA counsel has advised that BPA has no statutory obligation to offer the DSIs a*
16 *long-term power sales contract under section 5 of the Northwest Power Act for service*
17 *2001.*

18 *Q. Does this conclude your testimony?*

19 *A. Yes.*