PFR - 066

MAY 20 2005

Asgharian,Maryam A - T

From: Bleakney, Leann [lbleakney@nwcouncil.org]

Sent: Friday, May 20, 2005 3:26 PM

To: BPA Public Involvement

Subject: PFR closeout comment letter

Please find attached a letter from the Oregon members of the NW Power and Conservation Council regarding the renewables budget proposed in the PFR.

Thank you.
Leann Bleakney, staff
Oregon office
NW Power and Conservation Council
(503) 229-5171

<<MSE and JMD letter to BPA re PFR.5.20.05.doc>>

May 20, 2005

Mr. Steve Wright, Administrator
Bonneville Power Administration
PO Box 3621
Portland, OR 97208-3621

Dear Steve:

Thank you for the opportunity to submit comments on the Power Function Review closeout letter. The Oregon members of the Northwest Power and Conservation Council (Council) provide this letter on the renewable resources budget that will be considered in the upcoming rate case.

The Power Function Review focused on the Bonneville Power Administration's (BPA's) agency costs. As you move from the review to the rate case, we hope you will keep in mind that the best way to keep BPA's rates as low as possible is to avoid the cost of new fossil-fueled electricity plants for as long as possible. The notion of "stretching" currently available resources is a goal of the 1980 power act as well as the council's fifth power plan.

Renewable resources development should be guided by the Council's power plan, including a mechanism to facilitate utility acquisition of these important resources. The BPA is uniquely suited to pursue renewable resources development that would otherwise not happen. These activities benefit all of Bonneville's customers and the region at large. As the Council suggested in its power plan, these activities could include: 1) removing barriers to cost-effective renewable resources development; 2) developing storage and shaping services, developing transmission re-dispatch products and making transmission acquisition for renewable resources easier; and 3) developing research and demonstration projects. A fourth idea that recently has been suggested is a grants program to reduce upfront costs for renewable energy projects. BPA should explore such a program.

The state of Oregon is committed to renewable energy development in our region and has even developed a statewide Renewable Energy Action Plan. The Northwest is blessed with a variety of potential renewable resources that should be optimized.

Thank you for your consideration and your consistent commitment to renewable energy.

Sincerely,

(signed letter following)

Melinda S. Eden
Chair

Joan M. Dukes
Council Member

PFR - 067

MAY

Asgharian,Maryam A - T

From: mgr@bbec.org

Sent: Friday, May 20, 2005 3:35 PM

To: BPA Public Involvement

Subject: Comment on Power Function Review

Comment on **Power Function Review**
View open comment periods on http://www.bpa.gov/comment

James Johnson
Big Bend Electric Cooperative
mgr@bbec.org
(509) 659-1700
PO Box 348
Ritzville WA 99169-0348

BPA should look for efficiencies and cost savings in order to reduce its overall funding requirement for fish and wildlife from $139 million annually to some lower amount. Given the financial difficulties BPA is facing, cost-effective measures should be sought in all areas including fish and wildlife spending. A clear definition of the mitigation obligation of the federal hydrosystem should be established; a prioritized plan to address those obligations should be established; a comprehensive analysis of the cost-effectiveness of spending should be conducted; and, spending should be kept within the budget. Spending more money will not necessarily guarantee greater success for BPA's fish and wildlife program. Finally, BPA certainly cannot fund all activities associated with fish and wildlife mitigation, particularly those not attributed to federal hydro operations. BPA should work towards lowering its cost by achieving more cost-effective spending on fish and wildlife pro! grams.

PFR-068

May 20, 2005

Bonneville Power Administration
PO Box 14428
Portland, OR 997293-4428

Sent via email to: comment@bpa.gov

Introduction

Central Lincoln PUD is submitting comments concerning the BPA's 2005 Power Function Review. As a participant in the process I believe that it was flawed from the start because there was not a target rate established. Because there was no target rate established at the beginning of the process it was difficult to weigh alternative reductions other than to state that if the range of potential outcomes is 32 mills to 41 mills than proposed costs are unacceptable.

Central Lincoln is currently paying 21.5 mills for the balance of load customers served through the pre-sub contract. If that cost is escalated at 3.5% per year for five years the result is a rate of 25.5 mills in 2006 or a 20% increase. That is what we see as a reasonable rate. The program levels and risk profile suggested by BPA put the increase somewhere between 50% and 90%!

Central Lincoln supports the reductions suggested by NRU and believes that BPA should take all reasonable and prudent steps to reduce costs as distribution utilities have done over the previous five years. I offer two steps that Central Lincoln has taken in order to keep our retail rates in check:

1) Staff was 150 FTE in 2000, currently we are at 140 and the goal is 130 by 2011.
2) Spread a five year capital program over seven years.

Central Lincoln's residential and small commercial customers cannot absorb a 90% increase in wholesale power cost and our largest customer cannot absorb an additional 30% increase and in fact should reasonably expect a reduction of 20% in wholesale power cost. BPA must evaluate not only the final cost of its product but also the rate of change of that cost. Does it pass the reasonableness test?

Central Lincoln expects the Administrator to implement the suggestions made by the utilities that represent the consumers that pay the bills and ultimately bear all of the risk.

Below are several specific comments that we recommend to you and hope you will find them useful and in accord with recommendations of other wholesale customers:

Comment no. 1: **The TPP of 92.6% proposed for 07-08-09 is unnecessarily high and heavily impacts revenue needs forecasting.** In this current five-year rate period a TPP of about 88% has been used; given the ability to impose cost recovery charges on customer bills on an expected periodic basis there is no need to forecast revenue needs using such a strict parameter, even one as high as the 88% figure.

Comment no. 2: **While we appreciate several options (for risk mitigation) we believe the wisest course is to pay bills when they become due.** Paying at a much higher average rate for the three years based on modeling probables rather than on actuals is not sensible. Central Lincoln has been here more than 60 years and has provided electricity to its retail customers and paid its bills, including wholesale power, all that time. Volatility has become a fact of life because federal policy makers and parties in the industry have made it so. That does not mean that we should send ratepayer money to Bonneville for areas in the price curve that were never reached, or before they were reached. We suggest that your options include only those that are means to illustrate billing adjustments or surcharges on an as-needed basis.

Comment no. 3: **Use whatever is possible and feasible in the way of interagency loan or line of credit from TBL.** It is still the same agency. A loan from TBL is an emergency measure for the short term, to be sure, but is certainly available for short term use should there be a very sudden need in reserves or working capitol.

Comment no. 4: **It is hard to imagine that anyone is going to buy an eight to twelve mill rate increase to cover a modeled PNRR. So, we wish you wouldn't present such numbers as options.** As in comment 2 above we appreciate BPA's attempt to show us options but not those that are really not feasible. They are not options. As you say in the last paragraph on page 29 in regard putting an extra $500 MM into rates for PNNR, "This would lead to unacceptably high rates." That is an understatement. It's a waste of time, talking about the marginal solutions. It would create greater trust if we had to ask for those marginal options rather than having Bonneville acting as though they are real options.

Comment no. 5: **Is it time for a new revenue and risk model, something with more flow and fewer discrete iterations?**

Sincerely,

Paul Davies
General Manager

PFR-069

MAY 20 2005

Asgharian,Maryam A - T

From: Speer, Jack A. [Jack.Speer@alcoa.com]
Sent: Friday, May 20, 2005 4:06 PM
To: BPA Public Involvement
Subject: Power Function Review

Access to adequate amounts of BPA power at reasonable rates is vital to the operation of Alcoa's Intalco plant, and could make a significant difference at Alcoa's Wenatchee Works.

It is our desire to be treated like other long-standing customers served by BPA preference utilities, and therefore support comments submitted by the Public Power Council on the Power Function Review Process.

Sincerely,

Jack A. Speer
NW Vice President for Government and Energy Affairs

PFR-07C

MAY 20 2005

COMMENTS OF THE NATURAL RESOURCES DEFENSE COUNCIL ON THE BONNEVILLE POWER ADMINISRATION'S POWER FUNCTION REVIEW

May 20, 2005

Submitted by Ralph Cavanagh, Director, Northwest Energy Program
[rcavanagh@nrdc.org; 415-875-6100]

The Natural Resources Defense Council (NRDC) appreciates this final opportunity to comment on BPA's Power Function Review, on behalf of more than 45,000 NRDC members residing in Idaho (2,815), Montana (2,733), Oregon (16,661) and Washington (24,084). We participated throughout the Review's sequence of "Management-Level Meetings", and we also were active in the earlier "Sounding Board" process that looked for ways to reduce the agency's costs and enhance its revenues, starting in November 2003. Over close to two years now, we have had the opportunity with hundreds of other stakeholders to scrutinize every aspect of BPA's operations. We commend the agency at the outset for its commitment to transparency and its receptiveness to constructive criticism. No engaged participant in this process could possibly have emerged without enhanced respect for BPA's management and staff.

The Power Function Review process was dominated, in numbers anyway, by representatives of retail utilities who understandably want their principal commodity supplier to charge still lower rates. A repeated refrain was that the Administrator should "manage costs to ensure a 27 mill rate," regardless of the consequences for any of the agency's statutory responsibilities. The author vividly recalls similar calls from the early 1990s, which were premised on the assertions that BPA was no longer competitive with other wholesale suppliers and that the agency's utility customers could readily substitute for it in matters of stewardship. In light of the carnage that followed, no one could make either argument with a straight face today.

BPA has proposed an annual revenue requirement, exclusive of risk mitigation costs, of about $2.6 billion (down by about $260 million/year from the average for fiscal years 2002-2006).[1] At roughly $80 million per mill, this implies an average wholesale rate of 32-33 mills. "Managing" that down to 27 mills would require more than $400 million of cuts in annual BPA outlays. No remotely plausible way to do anything of the sort emerged from our many hours of deliberations together; indeed, utility representatives at the final meeting were heard to applaud Energy Northwest for its careful cost management, even though its costs to BPA are slated to rise 5.4 percent per year ($47 million);[2] NRDC concurs in the generally favorable assessment of Energy Northwest's efforts, but wonders why that same conclusion doesn't transfer to BPA itself,

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[1] Components of the Forecasted Expenses and Growth Rates in FY 2007-2009 (BPA handout at May 16, 2005 Management-Level Discussion Closeout Workshop, p. 3)

[2] Id.

which has a much stronger case based on the numbers (with non-Energy-Northwest costs DOWN by $306 million, compared to the FY 02-06 average).

In fact, from the perspective of long-term system needs and stewardship obligations, BPA needs to raise, not cut, its capital and operating budgets. Four examples underscore the point:

1. **BPA should restore proposed conservation budget cuts:** NRDC agrees with the Power and Conservation Council that BPA's *initial* conservation budget proposal was inadequate, and the additional proposed cuts of $5 million/year add insult to injury. The rationale for the cuts is that the Council inadvertently included in its regional conservation targets savings that would occur "naturally;"[3] it should suffice that the Council itself emphatically contests this rationale for retrenchment, and we join the urgent call for restoration. The Sounding Board meetings provided repeated evidence that the irrigation sector alone would justify that action, given the increasingly obvious economic (and environmental) value of water restored to the hydropower system from irrigation efficiency improvements (over and above the value of the saved electricity itself). We acknowledge and welcome the strong support of key representatives of the irrigation sector for an expanded efficiency effort. And like the earlier Sounding Board process, we note that the Power Function Review brought repeated affirmations of the extraordinary cost-effectiveness and resource value associated with all of BPA's conservation efforts, including the agency's participation in the Northwest Energy Efficiency Alliance. We are not yet close to the point of diminishing returns on these investments.

2. **BPA should provide full funding for renewable energy development:** In February 2005, BPA established a $21 million budget limit for "facilitation of renewable resources by its customers and others," a commendable objective that would justify a much more substantial investment. Given the storage and integration capacities of its hydropower system, the Northwest is uniquely positioned to convert "intermittent" renewable resources into a source of competitive advantage for the economy of the entire region. Yet, citing only "work to date with the Renewables Workgroup", BPA proposes to leave $13.5 million of the budget unexpended in FY 2007 and 2008.[4] We join RNP and NWEC in asking for restoration of these funds, based on abundant opportunities already identified by the agency's consultative process. As Rachel Shimshak and Angus Duncan can attest most eloquently, among others, the agency's expert renewable-energy advisors have left it with no lack of opportunities to use the full budget effectively.

3. **BPA should reverse a retreat from clean technology development:** BPA started this process with a grossly inadequate proposed budget for its Technology Innovation Program: less than $8.5 million over three years, or about one tenth of

[3] BPA, Draft Closeout Report: BPA's Proposed Changes to PFR Base Costs (May 20, 2005), p 4.
[4] Id., p. 8.

one percent of the agency's revenues (worse even than the deplorable average R&D record of the electricity industry as a whole). This would be grossly inadequate even to meet the ongoing needs of the Transmission Business Line's remarkably creative and promising Roundtable on Non-Wires Solutions. BPA acknowledges that "the energy industry is under-spending in this area" and that "the potential rewards from applied technologies can far exceed the development costs."[5] Yet the agency proposes to cut more than a million dollars from this budget, based on "customer concerns about adding additional costs during this rate period."[6] Customer interests are best served by restoring what already was by any measure an inadequate investment in better and cleaner technology to meet Bonneville's many demanding missions.

4. **BPA should meet its fish and wildlife obligations:** NRDC has listened for decades to demands by BPA's utility customers for more rigorous justification and accountability for fish and wildlife expenditures. As the Yakama Nation's representative contended so forcefully at the May 16 Power Function Review meeting, these customers should finally now take "yes" for an answer. They got the rigorous subbasin plans they have so long demanded. If they now refuse to support the necessary funding, in the face of overwhelming and specific evidence that the current budgets will leave key objectives unmet for generations, there is every likelihood that other authorities will intervene forcefully, with wholly unpredictable and unpleasant fiscal consequences.

CONCLUSION

Many in Congress and elsewhere continue to find in BPA's strikingly low wholesale rates a target of opportunity, and only a united front of diverse Northwest interests offers hope of a durable defense against onslaughts that will never cease. NRDC, RNP, NWEC and public-interest allies have stepped up repeatedly to defend Bonneville and its customers against efforts to redirect revenues or raise rates to punitive "market" levels, even as we have supported urgently needed strengthening of the agency's borrowing authority to meet regional infrastructure challenges. It is BPA's stewardship record that has earned that crucial support. Those who would put that record in jeopardy to meet arbitrary "rate targets" should give more attention to unanticipated consequences. Happily, as these comments indicate, there remains every hope of reconciling regional economic and environmental objectives in this proceeding, and NRDC looks forward to helping in every way possible.

[5] Id., p. 10.
[6] Id.

PFR-071

Asgharian,Maryam A - T

MAY 20 2005

From: troth@crpud.org

Sent: Friday, May 20, 2005 4:19 PM

To: BPA Public Involvement

Subject: Comment on Power Function Review

Comment on **Power Function Review**
View open comment periods on http://www.bpa.gov/comment

Thad Roth
Columbia River PUD
troth@crpud.org
503-366-3254
P.O. Box 1193
St. Helens OR 97051

BPA fish and wildlife mitigation is funded primarily by utility customers. As a customer of BPA, Columbia River PUD would like to provide the following comments on BPA's fish and wildlife spending. • Columbia River PUD supports BPA's proposal to shift funding for the Integrated Fish and Wildlife program to the proposed 70/25/5 allocation guidelines. We agree with BPA that Research, Monitoring and Evaluation should be more focused and better coordination should occur by all participants. We support funding that directly benefits fish and wildlife. • Columbia River PUD believes it is inappropriate to expect BPA's customers to mitigate for all the problems identified in sub basin plans. We object to paying for mitigation that is not directly related to impacts of the federal hydro system. • BPA's customers are currently paying nearly $700 million per year in fish and wildlife costs. Further increases to BPA's fish and wildlife mitigation programs are unjustified at this time. We believe that better coordination of existing efforts by stakeholders should be pursued before additional expenditures are considered. Thank you for your consideration in this matter.

PFR - 072

MAY 2 0 2005

Asgharian,Maryam A - T

From: Annick Chalier [achalier@ppcpdx.org]
Sent: Friday, May 20, 2005 4:46 PM
To: BPA Public Involvement
Cc: Manary,Michelle L - PFF
Subject: PPC PFR comments

Importance: High

PPCPFRcomments.pdf

Please find attached the Public Power Council's comments on the Power Function Review letter and draft report. A copy should also arrive by U.S. mail. If you have trouble opening the attached document, please let me know.

Thank you.

Annick Chalier
Associate Economist
Public Power Council
503.232.2427

Public Power Council

1500 NE Irving, Suite 200
Portland, Oregon 97232
503.232.2427
Fax 503.239.5959

May 20, 2005
Via Electronic and U.S. Mail

Paul Norman
Senior Vice-President, Power Business Line
Bonneville Power Administration
P.O. Box 14428
Portland, OR 97293-4428

Re: Comments on BPA's Power Function Review Closeout Letter and Report

Dear Mr. Norman:

As the Power Function Review (PFR) process comes to a close, the Public Power Council (PPC) would like to express its appreciation for the exchange of information and views the PFR afforded. Better information and deeper cost-analyses by BPA and its stakeholders are necessary elements of a defensible BPA budget. These elements, however, are not of themselves sufficient. At the close of the PFR, it is incumbent upon BPA to re-examine its proposed budget in light of the strong concerns expressed about potential effects on the region, and in light of many constructive suggestions offered by the Joint Customers in the PFR process.

Over the last four years, annual BPA power rates have been as much as 46% higher than the level originally set in May 2000. Moreover, these adjusted rates are significantly higher than historical rate levels. Together, we and Bonneville must work to ensure that this trend does not continue. We have taken seriously BPA's invitation to examine, understand, and comment on the various programmatic budget decisions it faces in the upcoming rate period. We expect BPA to take equally seriously our concerns, and those of our customers, for escalating budgets and unnecessarily high rates.

We also look forward to further discussion of revenues needed for risk. At this point, however, we continue to believe that BPA can achieve a power-rate target of no greater than \$27/MWh, inclusive of revenues for risk, in the next rate period. In the ensuing discussions on risk, we expect to work with BPA to achieve that target.

Informed by discussions within the Joint Customer group, PPC submits these comments on the various components of the PFR in response to the BPA closeout letter. We want to be certain you have as many of the customers' suggestions as is possible for your consideration, as you make the next round of decisions on what program budget levels to include the Power Business Line's (PBL) revenue requirement. We also provide initial comments and observations on the risks BPA's rates will be designed to mitigate, and comments on several policy decisions that may greatly affect how these risks are handled.

As the following remarks will show, our intent in these comments is not just to suggest ways for BPA to get to a particular rate target, but also to suggest ways BPA can change and improve the general budgeting process within BPA and its other business partners (Energy Northwest, the Corps of Engineers, the Bureau of Reclamation, and the Northwest Power and Conservation Council). These changes, we hope, will lead to an improved business relationship between BPA and its customers.

I. Transmission Acquisition

The transmission acquisition program is forecast at $189 million, approximately 7% of the total program costs that BPA reported on in the PFR process. These costs are for the purchased transmission services required to deliver power to loads and markets. The largest portion of these costs (68%) is associated with transmission and ancillary services that PBL buys to transmit secondary energy. The remaining costs are associated with transfer services (26%), third-party transmission and ancillary services (1%), reserves (4.5%), and telemetering (0.5%).

<u>Capture the proper mix of short-term and long-term transmission services for secondary energy sales.</u>

The costs BPA incurs vary depending on the volume of secondary energy available for sale. BPA uses forecasting techniques to estimate the monthly and annual expenses that PBL will incur for transmission to support secondary sales. In practice, BPA's goal is to use a least-cost mix of long-term and short-term transmission purchases to meet its secondary sales needs. BPA should ensure that its cost forecasting techniques capture the proper mix of short-term and long-term transmission purchases, compared to what BPA actually purchases, and that this mix results in the lowest cost to BPA. BPA should guard against approaches that over-estimate its revenue requirements for these transmission services, driving up rates unnecessarily.

Explore reducing the assumed transmission expense in the revenue requirement and adding a risk factor for transmission needed to support additional secondary sales.

BPA may view the potential variation in these transmission costs as "risk" to be addressed in its risk mitigation evaluation. Because transmission acquisition costs increase as the volume of secondary sales increases, the risk that actual transmission costs will exceed forecasted costs should increase as the risk decreases that secondary revenues will be less than forecasted. We would like to explore the possibility of BPA including in its revenue requirement a portion of its costs for transmission that are "fixed" contract amounts – and based on less-than-average-water assumptions. In its risk package, BPA could then model deviations from this fixed amount, for those additional costs beyond the fixed amounts when secondary sales are greater than what the fixed transmission services can support.

Remain active in the Transmission Business Line forums and processes that impact PBL rates.

PBL should continue to participate in the Transmission Business Line (TBL) rate cases and TBL business practice forums. There are several potentially expensive changes (see page 15 of the February 1 packet) facing PBL in using and delivering transmission services, including but not limited to changes in TBL rates, congestion costs due to transmission constraints, and changes to scheduling rules. PBL should do what it can within its control to seek and implement the most cost-effective options in response to these potential changes.

Verify the forecasting techniques used to estimate costs of third-party transmission.

The second largest cost component is for transfer services (26 %) representing the cost for providing third-party transmission via General Transfer Agreement (GTA) contracts, exchange agreements, and Open Access Tariff Transmission agreements (OATTs). BPA instituted a change in its forecasting method in 2005/2006. The forecasts under the changed methodology result in higher estimated cost for transfer services than in the past. BPA should verify that its forecasting techniques for both GTAs and existing OATTs, in addition to conversions to the Avista and Northwest Energy OATTs, are not overestimating the costs of services. In the draft closeout report, BPA identified a $4 million error in its forecasting of the wheeling costs for the South Idaho OATT. BPA should continue to scrutinize these formulas and incorporate in the final rate case studies any further reductions in forecasted expenses.

II. Conservation Program

BPA's Conservation program budget is highly dependent on the program design ultimately adopted by BPA. A final decision on this is expected next month. PPC has already submitted comments on BPA's draft policy proposal, in which we make the bulk of our Conservation program recommendations. We include some previously submitted comments here, however, because of their direct linkage to BPA's budget.

<u>Offer a portfolio of conservation program options.</u>

We offer qualified support for BPA's proposed rate credit, with no decrement to Block purchases. While a "no decrement" policy will not reduce BPA's overall costs associated with this program, customers note the great success of the present Conservation and Renewables Discount (C&RD), which has no accompanying decrement. The customers feel this is money well spent. We are troubled by other aspects of the proposed program design, however, including the restrictive Northwest Power and Conservation Council's (Council) measure list and the reduction in administrative support covered by the rate credit, to mention a couple issues included in our comments on the draft program proposal. These two specific issues are addressed in greater detail below.

<u>Adjust the Council-derived conservation target.</u>

We supported BPA's effort to quantify the amount of naturally occurring conservation included in the Council's target, and its intention to reduce BPA's portion of the regional target accordingly. Upon further reflection since submitting our comments on the program proposal, however, we question whether it is wise to reduce the budget by $5 million because of this reduction in the target. We encourage BPA to count the conservation achieved from the Investor-Owned Utilities' (IOUs) participation in BPA's future rate credit program toward the achievement of BPA's target. We also support an effort by BPA to develop a mechanism that would count the conservation accomplished when its customers going beyond their proportional regional share of the Council's conservation target, thereby reducing BPA's conservation responsibility. PPC offers its assistance in this effort so that BPA can make the appropriate adjustments by the time of the final rate studies.

Allow for more utility flexibility in the qualifying measure list.

We continue to have reservations about how realistic the Council's conservation target is, especially considering the supporting list of qualifying residential conservation measures. We believe that, up to the cost-effectiveness threshold, BPA should credit those measures not included on the Northwest Power and Conservation Council's (Council) measure list, thereby allowing utilities the flexibility to exercise judgment about what is cost-effective at the local level. Today's C&RD program does not exclude those measures the Council's complicated cost-effectiveness calculation deems non-cost-effective. If BPA follows through with its proposal to fund only the Council's "cost-effective" measure list, it will severely hamper conservation achievement for utilities with significant residential or rural loads. If utilities cannot meet the rate credit's requirements, they will lose their access to the program and pay more to BPA to help fund conservation in other utilities' service areas. This will weaken support for BPA's conservation program. The current C&RD program has allowed utilities with primarily residential loads to institute conservation programs with much success. The proposed post-2006 rate credit, however, will put utilities with mostly residential load at a disadvantage and will disrupt their ability to deliver conservation and serve their customers. The Council and BPA should not determine, exclusively, what conservation measures utilities' customers must install – utilities and their customers should also have a say.

Fund 20% of utilities' administrative costs.

BPA should cover 20% of utilities' administrative costs with the rate credit. If there are utilities that do not want 20% covered through the rate credit, they should be allowed to claim an amount less than 20%. However, these utilities are the exception, rather than the rule. BPA has proposed much more aggressive annual conservation targets than in the current rate period. BPA has also proposed excluding many residential measures. BPA's proposal includes increased monitoring, evaluation, and reporting requirements, as compared to the current C&RD program. For these reasons, utilities' administrative costs associated with participating in the rate credit program will stay the same or increase, but likely will not fall as BPA suggests.

Include a renewables alternative to the conservation rate credit.

We support BPA's inclusion of a renewables alternative in its conservation rate credit proposal, capped at $6 million per year. We are concerned that imposing complicating requirements on this option, such as requiring utilities to precommit three months prior to the start of the rate period a portion of their rate credit to renewables, will turn some utilities away from this option. Some utilities may need only rate-credit assistance for their renewable resource investment for one year. For others it may not make sense to invest in a renewable resource until a later year of the rate period. Some utilities may want up-front assurance that they will be able to use their rate credit for renewables for all three years. Giving customers the greatest practical number of options is the best policy choice and will help ensure a successful program.

If BPA persists in its desire to require its customers to commit a portion of their rate credit towards renewables investments in advance of the rate period, it should allow customers the option of using that credit for whatever year they wish during the rate period. In addition, if a utility makes this rate credit commitment but then is unable to find sufficient prudent renewable-investment opportunities by the end of the FY08, then for FY09 BPA should allow the customer to trade its remaining renewables credit with conservation credits from those customers who were unable to make the commitment prior to the rate period but wished to invest in renewables in FY09.

<u>Incorporate savings from the Enterprise Process Improvement Project (EPIP) and Revised Staffing Plan.</u>

BPA should incorporate in its final conservation budget all forecasted savings in Energy Efficiency Program and contract management generated by the EPIP evaluation completed this spring. Preliminary estimates indicate at least 15% in targeted savings are achievable. The initial PFR budget figure is $8.2 million on average for FY07-09, suggesting over $1 million in potential savings.

<u>Amortize conservation investments over their estimated useful life.</u>

The recovery period for ConAug (and its successor program) conservation investments should be depreciated and amortized over their estimated useful lives (as much as 20 years for some measures). With respect to ConAug, BPA's present policy is to amortize its costs over the term of the contract whereby, in the last year of the program (FY11), all ConAug costs will be expensed. This is an unnecessary requirement that causes undue and mounting rate pressure. In addition, it is inconsistent with BPA's practice in its original conservation program, namely the Legacy Conservation investments.

BPA has offered a compromise proposal to change it present 10-year declining amortization policy to a 5-year Straight Line amortization period policy for investments beginning in FY07. We believe BPA's compromise proposal is still too conservative, and additional debt service reductions should be pursued. While we agree that there is uncertainty surrounding BPA's rate structure post-2011, we believe the ratemaking complications that may arise from our proposal can be resolved. In fact, the complications may never arise, because there is no certainty regarding tiered rates post-2011.

III. Renewables Program

The customers support BPA's policy decision to move away from renewable generation acquisition and toward a facilitation role. This is appropriate given the region's growing recognition that customers will have to take on more responsibility for meeting their own load growth in the future.

<u>Terminate the acquisition of the Four Mile Hill Geothermal project.</u>

Pending the outcome of arbitration later this summer, BPA should do all it can to terminate its acquisition of the costly ($30 to 40 million, 50 MW) Four Mile Hill geothermal project, now set to go into rates in FY09. As noted in the February 8 PFR workshop, the sponsors of this project have missed key reporting deadlines related to the viability of the plant. For purposes of rate setting, we believe that inclusion of this cost in FY09 is unnecessary. Eliminating this cost would reduce net costs by approximately $11 million. Should BPA need to replace the 50 MW of energy from this resource with another resource, for purposes of balancing loads and resources, BPA has other, lower-cost options.

<u>Only fund facilitation grants if there are above-average nonfirm sales.</u>

We wish to emphasize BPA's long-term policy decision to spend *up to* a net of $21 million per year to support its renewable resource facilitation activities. The customers are not convinced that the FY07-08 (and potentially FY09) geothermal net costs should be replaced with "facilitation" cost placeholders of $5.5 million in FY07 and $11 million in FY08 (and potentially FY09). It is unclear what these funds would be used for or whether the expenditure of these funds would produce power benefits for the customers. We are concerned about putting placeholder budgets into the revenue requirement. We propose, instead, that if BPA has above-average nonfirm sales in these years, it could offer the proposed amounts of money in facilitation grants to its public and IOU customers for prudent renewable-resource investment opportunities on a year-by-year basis.

IV. Internal Operations

After reviewing PBL's PFR draft closeout letter and the spending levels associated with Internal Operations Charged to Power, PPC in consultation with the Joint Customers has identified several areas where PBL can reduce or hold costs. These include:

Adjust the budget for Power Non-Generation Operations.

When compared to other program spending levels, PBL has been doing a better job in this area, but further efficiencies can be achieved. Currently the FY07-09 average cost is $58.7 million/yr. We recommend using the FY05 SOY forecast and a two-percent inflation rate going forward to produce a revised average FY07-09 spending level of $55.4 million/yr, producing $3.4 million/yr in savings.

Reduce the Corporate G&A budget (exclusive of Information Technology costs) due to anticipated efficiencies from Phase I of EPIP.

BPA's FY01 actual G&A costs, excluding IT, were $33.7 million. The FY05 SOY forecast is projected to be $54.6 million, an increase of approximately $21 million in four years. Keeping in line with the PBL and TBL missions of holding costs to FY01 levels, we believe BPA's FY07-09 Corporate G&A budgets (excluding IT costs) should be based on FY01 levels, except that increases beyond BPA's control (such as those associated with security costs) should be allowed, and the allocation to PBL of the costs associated with industry restructuring should be reduced to 10% from 40%. We also recommend allowing inflation over the FY07-09 period. Instead of an average budget of $59.5 million in FY07-09, we believe the budget (excluding the industry restructuring costs) should be about $37.9 million assuming 2% inflation. These actions reduce BPA's expenses by about $21.6 million. PBL's portion of this reduction is $10.8 million, based on BPA's 50 % allocation factor for Corporate G&A costs between the business lines. If the industry restructuring allocation is reduced to 10%, the total reduction should be about $10.4 million.

This is our recommendation based on our rough estimate of how total Agency Corporate costs are allocated across the business lines. We received additional detailed information from BPA several days prior to the deadline for these comments that indicate that there may be less opportunity for savings in the portion of Agency Corporate costs assigned to PBL than we have estimated above. Nonetheless, our recommendations regarding potential savings for Agency Corporate costs remain valid.

Reduce the Information Technology budget due to anticipated efficiencies from Phase I of EPIP.

BPA has set as a reduction in corporate IT costs a target of 25% through its EPIP initiative. PBL should base this 25% reduction on the FY05 forecasted IT costs rather than on the average FY07-09 amount. Total Corporate IT G&A costs for FY05 are $58.5 million, with PBL's portion approximately $26.6 million based on a 45.5% allocation. A 25% reduction in this spending level is $7 million. In addition, by basing the reduction on FY05 levels, PBL must reduce another $4 million/yr from the FY07-09 levels for a total $11 million reduction ($7 + $4) in the projected FY07-09 annual average level.

Lower the allocation of Industry Restructuring cost charged to PBL.

The Joint Customers do not support the current methodology of allocating 40% of industry restructuring charges to PBL. At this point, restructuring is a transmission issue, and costs or benefits to PBL are speculative. Therefore, the PBL allocation should be reduced to 10%, which results in a $1.3 million/yr reduction in PBL industry restructuring costs for FY07-09.

Reduce the level of funding for Technology Confirmation/Innovation.

We agree with PBL's recommendation of reducing the level of spending to $1.3 million per year for TCI over the FY07-09 period. However, this program should be earmarked as one that is ripe for conditional budgeting and subject to additional reduction or even elimination in years where cost reductions are needed.

Aggressively pursue savings in the later phases (II-IV) of the Enterprise Process Improvement Project (EPIP) Phases .

It is somewhat challenging to derive an objective cost reduction from these future initiatives, because little data exists on the extent and timing of these efforts. Therefore, BPA should aggressively pursue savings in the future phases of EPIP and send a message from the top that these savings are expected from the Agency, not simply hoped-for.

Tie monetary awards to a measurable performance goal, aligned with customer interests.

We recommend that PBL maintain the increased awards and incentive amount as long as the methodology is tied to measurable performance goals. A primary component of these goals must be to align the awards with meeting specific customer financial objectives such as achieving a $27/MWh inclusive-of-risk rate target.

V. Federal and Non-Federal Debt Service and Debt Management[1]

Present BPA's "Sustainable Capital Program" to the customers.

An overall comprehensive forecasted capital spending plan was intentionally not included as part of the PFR process. Since capital spending is the driver for all future debt service and ongoing operations and maintenance costs, the customers' ability to weigh the implications of various debt management options is impaired. BPA agreed to present its sustainable capital program in response to repeated requests for this information by customers over the last few years. This promise had gone unfulfilled and the presentation is long overdue. The requested information would be very useful for customers in their efforts to understand the long-term consequences on rates of various debt management decisions.

The workshops focused on the results of previous capital spending levels, debt management actions, and the debt repercussions associated with forecasted future spending levels. Customers need a comprehensive look at capital decisions and their effects in future rate periods. Increases in capital spending and plant-in-service have lead to higher depreciation and interest costs, adding to our power rates.

Work with the other Federal Agencies to minimize the BPA rate impacts of debt management decisions.

The Corps of Engineers' (Corps) Columbia River Fish Mitigation Project (CRFMP) plant-in-service and the direct funding of the Corps and the Bureau of Reclamation (Bureau) are large drivers of costs in the FY07-09 period. Steps must be taken by the whole federal family to reduce these costs. To that end, we support BPA's decision to use the Corps' *Scenario B* schedule for repaying the costs associated with the $300 million CRFMP analyses.

Increase the amortization period of BPA-funded Fish and Wildlife capital investments.

We question some of the service-life provisions adopted by BPA. For instance, BPA-funded Fish and Wildlife (F&W) projects are amortized over only 15 years while Corps F&W projects are amortized over much longer periods of time. BPA said this was because the Northwest Power and Conservation Act

[1] Many of the recommendations in this section are repeated elsewhere in these comments, as they relate to specific program capital spending and debt issues. However, for completeness we chose to also keep them in the discussion focused on overall capital spending and debt management.

identified 15 years as the minimum life for F&W projects. We note, then, that 15 years is only a *minimum* requirement and that it is both appropriate and allowable to amortize some projects with longer lives over a longer period of time.

<u>Amortize conservation investments over their forecasted useful lives.</u>

As previously noted in the conservation section, customers are also concerned about the amortization of ConAug program costs. BPA has proposed changing its current practice of a 10-year declining amortization period to a 5-year Straight Line amortization policy for conservation investments beginning in FY07. We believe this change in policy is still too conservative and recommend extending ConAug amortization to cover the life of the conservation measures.

<u>Include the interest income on cash balances in the Bonneville Fund.</u>

During the PFR process, BPA noted that Federal Net Interest is projected to increase, due to increased capital investments for ConAug, IT, F&W, and Direct Funding for the Corps and Bureau. BPA's forecasts for years FY07-09 do not include interest income on cash balances in the Bonneville Fund or the effects of new Debt Optimization Program (DOP) actions. (The effects of DOP actions that have already been taken and that affect future years have been taken into account.) Should DOP continue, as expected, these forecasts may overstate BPA's actual future net interest expenses. BPA clarified in its closeout report that it will update its net interest assumptions in the rate case to reflect forecasted net interest on cash balances in the Bonneville Fund.

<u>Pursue opportunities to alter Non-Federal debt service associated with Energy Northwest.</u>

The major component of Non-Federal Debt Service is Energy Northwest (EN) debt service. During the PFR process, BPA identified a number of opportunities to decrease debt service expenses in FY07-09, including continuing DOP and pursuing savings from traditional refinancing actions (although BPA noted that the savings available from refinancing have largely been achieved and very little remains to be saved). Other areas identified as drivers of change were financing capital additions at EN (not traditionally financed) and financing the Uranium Tails Pilot Project. These two particular actions do not lower the non-Federal debt service but will lower the overall annual expenses associated with CGS. In its closeout report, BPA noted that it is leaning toward assuming debt financing for qualifying EN capital investments, for a saving of approximately $13 million. We support this effort. As we note below, we are concerned by the escalating spot market prices for nuclear fuel. We urge BPA to pursue debt financing of nuclear fuel for CGS. Finally, we request that BPA identify dollar values associated with the other potential areas of savings.

<u>Provide a comprehensive analysis of BPA's entire debt portfolio from the start of DOP through 2018 to show how BPA is addressing the potential bow-wave effect in long-term borrowing.</u>

BPA uses DOP to refinance EN bonds and uses the freed-up cash to pay off higher-cost Treasury debt early, which increases BPA's available Treasury borrowing authority. In the short-term this gives BPA more borrowing authority, and decreased borrowing costs; but in the long term there is a bow-wave effect attributed to the refinanced EN debt as well as the new debt that BPA will undoubtedly enter into with its restored Treasury borrowing authority. BPA should address this potential bow-wave by providing a comprehensive analysis of BPA's entire debt portfolio from the beginning of DOP through 2018.

<u>Provide assurance that EN debt reassigned to TBL as a result of DOP will in fact remain a TBL responsibility.</u>

BPA explained how Debt Service Reassignment will make this power rate case different from previous rate cases because of the interaction, in some instances, between PBL's responsibilities for the old, refinanced EN debt and TBL's responsibilities for the resulting new debt. If EN debt (which at present is PBL's responsibility to pay) is refinanced out to the 2013-2018 time period, and the savings are used to pay off federal debt that was TBL's responsibility, then TBL, instead of PBL, is getting the value of that refinancing. In theory, however, TBL is now responsible for paying off the refinanced EN debt. Customers need assurance that this will in fact be the case, and that the debt reassigned to TBL will not ultimately become a PBL responsibility.

<u>Work with customers to identify areas to reduce capital spending need.</u>

We believe BPA may be overstating its capital spending needs, and if this impression is true, it will result in overstating BPA's financing requirements, leading to artificial upward pressure on rates. Without the ability for customers to review and comment on a comprehensive overall capital program, the upward rate pressure could persist unabated.

VI. Columbia Generating Station Operations and Maintenance Costs

We concur in the following CGS proposals contained in BPA's draft PFR closeout report. In general, these proposals are consistent with the recommendations contained in our PFR comment letter dated April 13, 2005. Comments have been added where necessary to provide clarification or emphasis.

Include the forecast reductions proposed in the CGS long-range plan.

We concur in the decision to "Reduce CGS O&M costs by an average of \$22 million/yr per draft Energy Northwest plan." This commendable attitude of prudent cost-cutting should be maintained at CGS and extended into other major BPA cost areas, including BPA internal operations charged to power rates and Corps and Bureau O&M.

Do not eliminate the license extension spending for CGS in FY07-09.

We concur in the decision not to eliminate the license extension spending and believe that it is prudent to pursue re-licensing during this time period.

Debt finance qualifying CGS capital projects.

Two other CGS recommendations – borrowing to pay for capital items and borrowing to pay for fuel – are addressed in the Debt Management Section of BPA's draft PFR Closeout Letter. BPA proposes to "assume debt financing for CGS capital items, though this latter decision is one made within the rate case, not the PFR". We continue to recommend that the FY07-09 revenue requirement be reduced through use of debt (rather than revenue) financing of qualifying capital projects. This will reduce the FY2007-09 revenue requirement by an estimated \$13M/yr. The end-date for debt financing should be discussed during the rate case.

Pursue opportunities to lower the expense associated with procuring nuclear fuel.

Finally, regarding nuclear fuel costs, BPA's draft conclusion on nuclear fuel financing (Ref: Debt Management section) states:

> No assumption of fuel cost financing until EN develops its strategy for managing the recent run-up in nuclear fuel costs and changes its policy of not financing fuel generally. Final decisions on these topics will be made in the rate case.

We are concerned about the continuing trend of steeply rising spot-market prices for Uranium (U_3O_8). Timely approval of the Uranium Tails Pilot Project and debt financing of the nuclear fuel are essential for minimizing overall CGS fuel costs.

VII. Corps of Engineers and Bureau of Reclamation Operations and Maintenance Costs

Include BPA customer representatives in the Joint Operating Committee and associated workgroups.

We appreciate that BPA, the Corps, and the Bureau are working together to improve efficiency and reduce costs. We want to work with you on these efforts and appreciate your offer to meet with us on a regular basis. We urge the Federal Columbia River Power System (FCRPS) partners to consider at least one customer-member on the Joint Operating Committee (JOC) and other relevant workgroups. We realize that any customer-members on the JOC probably would not have a vote, but would act in a consultative capacity. The FCRPS partners would benefit from hearing additional perspectives and having opportunities to compare their decision making to that of other hydroelectric utilities in the region. In addition, we believe it is important for BPA and its cost partners to understand the effect on customers of the decisions they make, and a customer-member would enhance this understanding.

Measure program success on indicators other than amount of money spent on the program.

There is considerable concern about the measures that the FCRPS partners are using to gauge the success of the O&M and capital programs. We believe that looking at forced outages is one good metric for measuring success, even if it is a lagging indicator. At the very least, it is indicative of how well the actions that undertaken are working. Using the amount of money spent on a program to measure the progress in O&M and capital programs is *not* an adequate indicator. We urge that the FCRPS partners work hard to change a culture that has at times measured success by how much was spent in a given year. The goal should always be to spend the least amount to get a given result that produces the greatest return. The Corps and Bureau heard the customers say that they need a way to prioritize their O&M and capital expenditures. Highest priority should be given to investing in projects that restore revenue that would be lost absent the investment. The customers, especially those with hydro projects of their own, can provide the FCRPS partners valuable assistance. An additional benefit is that the customers will have greater buy-in on decisions if they understand those decisions because they have participated in the decision-making process.

Absorb some of the forecasted Corps and Bureau O&M expense increases.

BPA has stated that it will make a decision on revenue-requirement levels for the Bureau and the Corps in the PFR Process. However, detailed budget information is not available in the materials provided at the workshops. In order to make a fair assessment of Corps and Bureau costs over time, we need budget details from 1997 through 2009. We submitted a detailed request for the budget documents not included in the original presentation materials in March. We understand that many of the identified increases in the O&M budgets between FY02-06 and FY07-09 are driven by forces more or less beyond BPA's, the Corps', and the Bureau's control, but we urge these parties to find ways to absorb a portion of the $44 million annual average increase by removing some expenses that are discretionary and associated with lower-priority investments. It is possible that the Corps and Bureau will find such opportunities for efficiencies after additional benchmarking against other PNW utilities that operate hydro facilities. These efforts should be undertaken as rapidly as is possible so that any reduction in forecasted O&M expenses can be incorporated into BPA's final rate case studies.

<u>Revise the Asset Management Strategy adopted in 1999.</u>

BPA notes that in response to the Cost Review of 1998, it developed (with the Corps and the Bureau) an "Asset Management Strategy" for the FCRPS in 1999. This plan influences greatly the capital outlays BPA forecasts it will need for the Corps and Bureau in their collective desire to restore system reliability to industry standards or better through 2021. While the specific investments planned and made are updated frequently, the outyear capital budget figures are seemingly caught up in a dated picture of what the system might need to meet industry standards. We request a reassessment of this plan, to be completed with customer input. In the near term it would be useful if the Corps and Bureau would reshape their capital investments to levelize them over the FY07-11 period and not frontload them during the FY07-09 period.

VIII. Fish and Wildlife Program

<u>Accelerate the installation of surface bypass systems that improve fish passage and reduce foregone revenues.</u>

We support the accelerated installation schedule for surface bypass systems (SBSs), such as Removable Spillway Weirs (RSWs), in order to safely pass juvenile salmon and steelhead through federal dams. SBSs allow a more efficient use of water spilled over dams. Both fish and ratepayers benefit. RSWs should continue to be funded through appropriations and repaid over 50 years.

<u>Modify the Snake River fall Chinook transport vs. in-river migration study to ensure scientifically defensible results.</u>

The Action Agencies are proposing to implement a study of summer transportation in the Snake River during the last two years of the coming rate period. BPA's preliminary estimates are that the total study costs during the rate period will be about $46 million, which, spread over the 3-year rate period, is equivalent to increasing the Priority Firm rate by about 0.2 mills/kWh. As currently proposed, however, the usefulness and credibility of the study will be unnecessarily jeopardized.

First, the Action Agencies are proposing to implement the study while the SBSs are being installed, tested, and put into operation at the various federal dams. Thus, under the proposed schedule test fish will be subjected to different passage conditions during different years of the study, due to altered system configurations resulting from the installation of the SBSs. Although river conditions and operations are never constant from year to year, the variability introduced into the study by conducting it during installation of the RSWs is quite significant.

Second, significant new information about a "reservoir-type" life history observed for Snake River fall Chinook should be further explored and understood before undertaking the study. Conducting the proposed survival test prior to investigating the effects this life history could have on the data will impair the scientific credibility of the study.

In order to avoid these confounding effects on the study, the Action Agencies should wait to implement it until after installation of the proposed RSWs, and until the life history impacts can be determined. This would make the best use of BPA's research dollars.

The UPA adopts an adaptive management framework which allows the action agencies to make "appropriate adaptations or adjustments" to the action through the implementation planning and progress reporting process. We urge BPA and the other action agencies to utilize this adaptive framework, and modify the proposed study as suggested.

<u>Fund only baseline O&M costs and also provide greater clarity on the role of these hatcheries in meeting mitigation obligations.</u>

The customers propose that BPA include only the baseline O&M costs of $17 to $19 million per year and not the higher alternatives. Opportunities for cost savings, efficiency improvements, and cost sharing should permit some nonroutine maintenance to be funded. BPA also needs to better clarify the goals and purpose of these hatcheries, and how the hatcheries fit into recovery planning.

Finance over 50 years current and future CRFMP financial obligations.

Over $300 million of CRFMP mitigation analysis costs have accrued and will come into customers' rates. In order to minimize the rate impact of these mitigation analysis costs, they should be financed over 50 years. Customers should also be provided an accounting of what these studies have achieved. The customers support *Scenario B* as described on page 69 of the April 5, 2005, PFR Fish and Wildlife handout. This scenario best mitigates the rate impact of the CRFM Program.

Do not increase the Integrated Program budget until biological goals and objectives are developed and prioritized to meet BPA's legal mitigation obligations.

The 2001-2004 average budget for the Council administered programs is $139 million, inclusive of BPA's overhead. When capital expenses associated with the Integrated Program (hatcheries, screens, etc.) are included, the annual average is closer to $146 million.

The customers are supportive of BPA's initiative to increase the proportion of the existing Integrated Program that is allocated to *"on the ground"* projects such as habitat and production. That is, currently the proportion of money identified for programs such as coordination, research, monitoring and evaluation (RM&E), and data collection, is disproportionately high compared to more fundamental activities directly benefiting fish. We believe that changing this is a positive step.

Besides increasing the percentage of the program costs that go to on the ground work, however, we believe BPA should take additional steps relative to its funding of the Integrated Program. In particular:

- Any funding above the $70 million that is contractually obligated should be subject to annual review, and all contractual commitments should be reviewed regularly to the extent permitted by the contracts.

- All mitigation activities need to be thoroughly prioritized based on biological benefits.

- Any additional funding for the Integrated Program should not result in an increase in total fish and wildlife spending by BPA's ratepayers.

- The Action Agencies should conduct a comprehensive review of total RM&E to avoid duplication of effort, increase complementary aspects, and foster better sharing of information and study results.

- BPA should confirm that it will continue to include its overhead costs of $11 million per year within the Integrated Program budget.

Without these steps, we do not believe that BPA is justified in increasing its budget for the Integrated Program.

Additional Customer Comments

More must be done to reduce fish and wildlife mitigation costs.

BPA is responsible to its customers and the region for the level of its power rates. Because biological outcomes, not the amount of money spent, should be the indicator of a successful fish and wildlife mitigation program, we believe BPA has an ongoing and affirmative obligation to ensure that all fish and wildlife related actions and programs are assessed relative to their biological and cost effectiveness. Further:

- Fish and wildlife mitigation should be funded as a single budget to ensure that priorities are adequately addressed.

- BPA's fish and wildlife mitigation responsibilities are limited to the effects of the federal hydrosystem. BPA is not financially responsible for all goals and objectives identified in the various subbasin plans.

- Biological goals or performance standards must be established for each mitigation action.

- The Action Agencies should then use cost-effectiveness as a primary consideration when assessing viable alternatives to meet mitigation goals.

- The Council's Independent Economic Analysis Board should be adequately funded to provide the cost-effectiveness analysis of all mitigation activities in the federal hydrosystem.

- Customers should be allowed to participate directly in project assessments and decision-making regarding fish and wildlife mitigation.

Review and alter BPA's capitalization policy to allow large capital projects to be depreciated over their useful lifetimes.

BPA assumes that $150 million per year of new capital investments will go into service from 2007 through 2009 for CRFM and BPA F&W capital programs. The record shows that fish and wildlife investments going into service have been lower than what BPA is currently projecting.

- BPA needs to work with the Corps and Bureau to forecast better plant-in-service dates. Doing so would help reduce rate pressure.
- BPA should work with the regional fish and wildlife managers to develop a crediting system for habitat purchases that benefit fish.

XI. Risk Mitigation Packages and Tools

As BPA has noted, the issue of risk is going to be carried beyond the PFR process, and addressed more fully in the rate case. Although we are at a very early point in the discussion of these issues, we do have a few brief preliminary comments and observations on the risk issue.

Explain in greater detail the reasoning behind and magnitudes of perceived risk factors.

We are concerned that BPA may be overstating the magnitude of the risks it faces. Consequently, we request an opportunity to engage in more discussion with BPA staff to understand why they believe the risk magnitudes that BPA faces are so large. A case in point is BPA's treatment of the future financial benefits for the IOUs' small farm and residential customers. On page 10 of the handout that BPA distributed at the April 6, 2005, PFR risk technical meeting, BPA identified under "New Risks":

> IOU benefit risk in FY 2008 and FY 2009. A $10 change in market prices can raise or lower the benefit paid to IOUs to the cap or floor. There is a risk that rates will not be set high enough to recover the cost of potentially higher IOU benefits in the last two years of the rate period.

A similar statement is also made on page 7 of the handout.

The problem we have with these statements is that we believe having IOU benefits vary with the market helps hedge the variability in BPA's nonfirm revenues (which BPA states is also a key component in increasing BPA's risks). If IOU benefits are going up, that is because market prices are going up. If market prices are going up, then the price BPA receives for its nonfirm power is also going up. The reverse is also true of course, so if BPA is receiving poor prices for its secondary energy, the level of IOU benefits is also being reduced.

Obviously, this is not a perfect hedge against the variability in BPA's nonfirm revenues – IOU benefits do not vary with streamflows, which have a big impact on BPA's nonfirm revenues. In addition, the market price used to set the level of IOU benefits is set at the beginning of the year based on a forecast of market rates for that year, which can diverge from actual market rates during the year. Nevertheless, it seems clear to us that having IOU benefits vary by market price imposes *less* risk on BPA than a fixed level of IOU benefits, due to the hedging provided by the variability. The fact that BPA staff seems to think that having variable IOU benefits increases the risks faced by BPA implies a disconnect between how BPA views BPA's risk and how the customers view BPA's risk. This clearly needs to be resolved prior to BPA's initial proposal.

<u>Explore the alternatives to increasing the TPP standard in FY07.</u>

Another issue of great importance for the customers is BPA's stated goal of increasing BPA's three-year Treasury payment probability (TPP) from the current level of 80% to 92.6%. Under BPA's methodology for calculating a rate compliant with the current TPP standard, 20% of the probabilistic runs of BPA's computer model are allowed to "fail" (*i.e.*, BPA has to reschedule its payment to Treasury at least once in a three-year period). Under BPA's revised standard, only 7.4% of the runs are allowed to "fail" – a reduction of nearly two-thirds in the acceptable number of "failures." In other words, even if BPA devised a rate structure that halved the number of "failures" over the current standard, that would not be enough to meet the revised standard. Our calculations indicate that the planned net revenues (PNRR) required for TPP increases by 70% solely due to this change in the TPP standard, so we want to continue the discussion of the TPP standard, given that it requires such a large increase in the PNRR.

<u>Explore alternatives to a "PBL reserves only" policy for ratemaking and alternatives to doubling in FY07 the necessary minimum operating reserves.</u>

For purposes of future PBL ratemaking, BPA says it will segregate reserves attributable to PBL and reserves attributable to TBL, and then calculate the necessary PNRR solely based on PBL reserves. BPA states on page 10 of the April 6, 2005, handout that: "Starting period Power reserves are currently expected to be approximately $180 million. Starting reserves are only $80 million above the minimum liquidity reserves (working capital) PBL is assuming for the next rate period. Low cash reserves cause PNRR to be higher to offset the large number of "games" that fall below the $100M minimum liquidity reserve level in FY2007."

There are two points to be made about BPA's statement. First, it is clear that FY07 is the "pinch point" – the low level of initial reserves ensures that most of the forecasted failures to pay Treasury occur in FY07, as opposed to the other two years of the rate period. One of the reasons this happens is that BPA has decided to increase its minimum required PBL liquidity reserves from the current level of $50 million to $100 million beginning in FY07. If BPA elected to defer that increase in liquidity reserves for one year, from FY07 to FY08, it would increase available PBL financial reserves at the beginning of FY07 from $80 million to $130 million, thus easing the "pinch" in FY07. Making this one change would cause a reduction in needed PNRR. In earlier processes, we also learned that BPA has a number of cash management tools that it can use to deal with short-term cash-flow problems, and we would like to discuss with BPA whether subtracting a liquidity reserve from PBL's reserves really reflects BPA's actual financial needs, given the existence of these other cash management tools.

Second, while we believe the rates that PBL charges should cover PBL's costs, and the rates that TBL charges should cover TBL's costs, looking solely at PBL's financial reserves in isolation from BPA's overall reserves significantly overstates the risks of BPA not paying Treasury. For example, if PBL reserves fell below zero in one year, and then recovered the following year, that would count as a "failure to pay Treasury," even if TBL reserves were sufficient to cover the temporary PBL deficit. In modeling the risks of PBL "not paying Treasury," the existence of TBL reserves needs to be acknowledged when PBL reserves dip for a single year or two, and then recover. (If this actually happened during the rate period, it might well be desirable to have TBL's loan of reserves to PBL formally memorialized, to ensure that PBL in fact repays these reserves.) BPA makes a single Treasury payment out of a single Bonneville Fund, so BPA should not model an artificial construct that disregards that realistically TBL reserves will be used to cover short-run cash flow problems that PBL encounters.

Explore additional risk mitigation options.

We also want to discuss a range of possible other means for mitigating the risks that BPA faces, such as possible automatic adjustment clauses to compensate for poor nonfirm revenues during a fiscal year, stepped rates, and other cash managements tools at BPA's disposal. Among the things that BPA should consider is revisiting BPA's assumption that if BPA has a bad year financially, whether because of a drought or for some other reason, BPA's expenses would not be reduced during that year. Other organizations reduce their expenses in poor financial years, and if BPA did the same, it would improve BPA's ability to pay

Treasury. Given that one does not have a good snowpack forecast until well into the fiscal year, BPA could use "conditional budgeting" as part of its budgeting process. Under "conditional budgeting," BPA, as part of its normal budgetary process for the ensuing fiscal year, would identify those expenditures that would be eliminated or deferred if the water year turned out to be poor, or if BPA's finances were poor for some other reason. The ability to defer or eliminate a small proportion of BPA's overall budget could free up enough cash to make a significant contribution to BPA's ability to pay Treasury in a poor financial year.

X. Conclusion

We recognize that there is still time after the close of the PFR to review budget levels that will affect rates in FY07-09. We urge BPA to pursue all avenues for revenue enhancements and cost reductions that can be captured in its Initial Proposal and in its final studies for the Power Rate Case. The customers would like to help in whatever way is necessary to find revenue enhancements and cost reductions, with the ultimate effect of lowering rates. In addition, we ask to be invited to offer input in the future when BPA and its cost partners face decisions that will affect rates.

Thank you.

Sincerely,

/s/

Marilyn Showalter
Executive Director

cc: Michelle Manary

PFR - 073

MAY 20 2005

Bonneville Power Administration
Power Function Review Management Level Discussion
May 16, 2005

Rates Hearing Room, BPA Headquarters, Portland, Oregon
Approximate Attendance: 50

Draft Closeout Letter and Wrap-up

[The handouts for this meeting are available at: www.bpa.gov/power/review.]

I. Welcome

BPA Administrator Steve Wright welcomed the managers and thanked them for participating in the Power Function Review (PFR). The PFR has been a lengthy and valuable process, and it is part of a larger "culture change" at BPA that is focused on enhanced accountability and transparency, he indicated. The PFR builds on the Sounding Board effort – it's part of a continuous improvement process, Wright said. He noted that the PFR has benefited BPA internally. Preparing the meeting materials and presentations has increased focus internally on costs, and it has engaged the BPA staff to respond to questions raised by participants, Wright explained. Our cost partners – the Corps of Engineers, Bureau of Reclamation, and Energy Northwest (EN), have also been involved in the process, he said. This has all been quite valuable, Wright stated.

He called attention to a pie chart and table of BPA costs, pointing out that a huge part of the costs are associated with debt management. Wright also pointed out a comparison between expenses for the 2002-2006 rate period and the forecast for 2007-2009. In internal costs, we have kept costs stable without adding for inflation, a challenge I laid out to managers, he said. In other categories, there are increases, Wright acknowledged, noting that O&M for the Corps and Reclamation cover "the assets that create the value." The total on the table shows an overall expense decrease of 2.3 percent, he said.

At the end of this process we have decisions to make about costs for 2007-2009, Wright stated. I want to hear your comments before we bring this to a final conclusion, he said.

Paul Norman (BPA) asked for general comments before the overview of cost categories.

General Comments

Steve Eldrige (Umatilla Electric) started out with a comment on "the amount of process required to make decisions." It's not just BPA, "it's the Council, it's everyone," he clarified. It's too much for people to participate in, Eldrige said. I feel BPA made a tremendous effort to respond to the questions and concerns raised and to explain things, he said. If we look at the reasons for so much process, "I wonder if some of it is solely to keep an eye on each other and protect our interests," Eldrige commented. Someone should look at why we are so process oriented, he suggested.

As for the PFR conclusions, I'm happy we can reduce the budgets, Eldrige said. In preparation for the meeting, I looked over BPA's annual reports for the last several years, he said. Eldrige pointed out that there is no longer detail about who BPA sells power to and the number of employees. "I'm interested in those things," and I'd encourage BPA to return them to the annual report, he said. Eldrige also pointed out that in the last five years, BPA has been comparing its rates to the market. "I'd encourage you not to use that as the benchmark," he stated. Hydro costs have not changed that much – "it's what we have added on," Eldrige said. The market BPA is comparing itself to is largely thermal, and that ought not to be the standard, he said.

It looks like rates will end up around $30 a megawatt-hour (MWh), Eldrige said. We should do better than that, he wrapped up.

Ralph Cavanagh (NRDC) said he found the process valuable. There are key participants around the table, and we ought to have more opportunities to talk to each other, he said. Cavanagh said "extraordinary effort" was made with the BPA presentations for the PFR. If this adds value, it's worth my time, and I'll be back any time you convene a meeting, he stated.

We appreciate the time we have spent here, Steve Marshall (Snohomish PUD) said. We are in this together, and if you succeed, your customers succeed, he said. It looks like rates are going to go up rather than down, but this budgeting may be premature, Marshall said. It's a long time before the next rate period, and there is a lot of opportunity to look at cuts that could be made as a result of the KEMA study, he said. Marshall encouraged BPA to take the suggestions in a February 24 letter from PPC. Set a $27 per MW target inclusive of risk – have a goal, he urged. "I can't imagine the CEO of a large company saying he can't set an earnings target because of environmental laws" and because costs might go up, Marshal stated. When costs at our utility go up, we look to cut them back, not raise rates, he said.

Don't lock down your budget decisions now, Marshall advised. Every time you take money from the economy of the Northwest, the region loses jobs, he said. If BPA's rates remain as high as they are, one of our large industrial customers, Kimberly Clark, could leave, Marshall added. Set a target and work hard to achieve it– don't stop now, he said.

Where the rate number ends up depends on what the agency chooses with regard to risk, John Saven (NRU) stated. It's insufficient to take that topic into the rate case without giving policy makers in the region an opportunity to participate first, he indicated. I'd request we visit that question in a high-level discussion, Saven said.

Paul Davies (Central Lincoln PUD) said his utility is a presubscription customer and currently pays 21.5 mills. If that rate escalates at 3.5 percent per year for five years, the result would be a rate of 25.5 mills in 2006, or a 20 percent increase, he said. That seems reasonable, but if BPA goes with the cost level being proposed, it could mean between a 50 and 90 percent increase for Central Lincoln, Davies said. He pointed out that the PUD has been cutting costs, and staff numbers have fallen from 150 to 140 and will go to 130 by 2011.

Our residential and small commercial customers cannot absorb a 90 percent increase, Davies stated. Georgia-Pacific, our largest customer and the largest employer in the county, could see a 30 percent increase with what you are proposing, he said. We expect the Administrator to implement cost reductions and to give us a reasonable rate, Davies concluded.

Dwight Langer (Northern Wasco PUD) said he has participated in the PFR because it is an opportunity to forge solutions. The PFR process is intensive and the issues complex, he acknowledged. BPA has been very open and responsive in trying to balance the goals of customer groups, Langer said. The relationship between BPA and its customers is a partnership, and I think it is growing stronger, he added. Controlling costs is "a continual fight," and everyone in the room is trying to deliver on that, Langer said. I appreciate BPA's dedication to the process and to its customers, he wrapped up.

We have appreciated the transparency and have learned more than ever about BPA's cost structure, Nancy Hirsh (NWEC) said. We are trying to be responsive to rate pressure, but we don't want to lose sight of the long term in meeting the short-term pressures, she said. Specifically, I'm talking about conservation and renewables, which have long-term value, Hirsh said. We urge you to take a hard look at how to balance the investments, she said.

<u>Cost Categories</u>

Norman picked up with a description of BPA's cost categories. We have to nail down the costs for our initial rate proposal, but we have nine or 10 months beyond that to continue to work on costs, he said. "It's not pencils up on costs," Norman said. Today, we want to get a sense of your major points of view on our draft PFR conclusions, he said.

Starting with debt service, Norman went over issues raised during the PFR. There are two things outstanding in this category, he said: treatment of the Columbia River Fish Mitigation (CRFM) costs and pushing EN bond repayment beyond 2018.

Eldrige asked about the 3,000 MW of additional load BPA says it will be serving in the next rate period. Is that an increase in public power load or is it a result of publics selling non-federal resources and putting load back on BPA? he queried. Norman acknowledged that there is confusion about two separate contexts for 3,000 MW. Public utility load on BPA was 3,000 MW less in 1997-2001 than we forecasted for 2007-2009. Separately, there was a jump of 3,000 MW from 2001 to 2002 because of the decision to serve IOU and DSI load, and public utility load increases, he explained. Would you put that explanation in writing? Eldrige asked.

BPA's 5(b)9(c) policy did not allow us to sell our Centralia resource and replace it with federal power, Kevin Clark (Seattle) pointed out. With regard to conservation financing, I don't see the rationale for allowing only a five-year payback, he said. Why isn't conservation capitalized over the useful life of the measures? Clark asked.

Our original decision related to the fact that contracts went to 2011, Norman responded. The five years was a compromise, he said. But we are in the process of putting in place a long-term contract structure, Norman said. Until we sort out that structure, we do not feel comfortable with a duration that goes longer term, he said.

This is also an issue about our sustainable access to capital, Wright said. If you go to 15 years, you triple the amount of investment capitalized over time, and that has an impact on our access to capital, he said. And we are talking about large numbers, Wright added.

I would encourage you to have "a complete and frank discussion" with your customers, before you extend the EN debt beyond 2018, Joe Nadal (PNGC Power) stated. You need to discuss the propriety of that, he said. Do you have a time frame for that decision? Nadal asked. We are beginning to talk to the EN board, but we don't have a time frame, Val Lefler (BPA) responded.

Norman moved to the Columbia Generating Station (CGS) costs, noting there are two refueling outages in the three-year rate period, which is reflected in the costs and exaggerates the escalation in those costs from 2002-2006. EN has proposed a $22 million reduction compared to what we presented at the PFR opening workshop, he said. They are a being aggressive about cost management. We still have the outstanding issue of fuels costs, and we are working with EN to try to manage that, Norman reported.

EN did a good job of presenting its budget, Jean Ryckman (Franklin PUD) said. They achieved a 10 percent reduction from where they started, she added. They also took issue with mandates they have gotten from Washington, D.C., Ryckman pointed out. I think we could learn from that, she said, noting that sea lions and ocean fishing are such issues for the BPA customers. We shouldn't just accept the costs, we need to look at what is being imposed and see if it makes sense, Ryckman stated.

I would also commend EN, Eldrige said. "They took our message to heart," he said. It would be helpful if everyone presented uniform budgets, Eldrige added. CGS "is out of the money" in today's market, he commented. They might not be in business if it weren't for the guarantee that BPA buys the output, Eldrige indicated. "The pressure has to stay on them" – they have such a large impact on your costs, he said.

For "the rate hawks" at the table, CGS is the single largest source of upward pressure on costs, Cavanagh pointed out. They are a larger impact than the Corps or Reclamation, he said. The Corps and Reclamation made good presentations too, and there is a rapid payback on the investments they propose, Cavanagh indicated. He urged the group not just to look at costs, but also to consider the value that is gained. The Corps and Reclamation investments are an attempt to gain more revenue from the system, Cavanagh pointed out. They are talking about "a change in the maintenance philosophy," and that could lead to big gains, he stated.

With regard to the Corps and Reclamation costs, this group suggested benchmarking the federal hydro projects, Norman said. We have other projects on the river, the Mid-Columbias, to compare ourselves to, he noted. We've talked to Grant PUD, and I expect that benchmarking effort will be kicked off soon and will be done in time for final rate setting, Norman said. The Corps is doing its own internal look at costs through its 2012 Project, and that could also yield cuts in time for the final rate proposal, he said.

No one in the workshops suggested not making the rehabilitation investments in the Corps and Reclamation hydro projects, Clark pointed out. Our problem has to do with the O&M increase since the 1990s, he said. They haven't justified the additional $46 million annually that is being proposed, Clark said.

The amount of increase doesn't seem unreasonable, Eldrige said. I have a concern about whether the system is operating as a whole – it still seems like there is a project-by-project mentality, he said. There are economies of scale to be gained on things like routine maintenance, and I hope they are taking advantage of that, Eldrige stated. He also pointed out that the system is heavily engineered and needs engineering expertise. "We can't have a bookkeeper running a system that is so heavily engineered," Eldrige said.

With respect to BPA's business partners, there is not enough rigor in that process, and it needs "shoring up," Kris Mikkelsen (Inland) stated. Before the partners come in to make a presentation to us, they should have to go through a rigorous process to justify their costs, she said.

We do have a rigorous process, and that needs to be made more apparent, Norman replied.

One suggestion was to get customers more involved in the Joint Operating Committees so we better understand the costs, Randy Gregg (Benton) stated. I also encourage you to push the Corps and Reclamation to lower employee grades and examine their own internal processes, as BPA is doing, he said.

Paul Elias (McMinnville) encouraged the operating agencies to keep up with capital programs at the hydro projects. "It keeps expenses down," he said. "They are trying to move from a breakdown to a preventive maintenance approach," and that reduces costs overall, Elias commented. We should be seeing that effect in the O&M budgets, he said.

Langer pointed out that $300 million in CRFM studies is coming due. I get the impression that figure was a surprise, and you should work to prevent that kind of thing in the future, he said.

With regard to transmission costs, we've seen some improvement since the original PFR numbers, but there is not much more prospect for more reductions, Norman continued.

Clark questioned whether there is "a double count" in the transmission costs. He recommended that BPA budget the minimum, based on dry conditions, and address the issue as part of risk mitigation.

There was a wide range of views about the appropriate funding level for the fish and wildlife (F&W) integrated program, Norman said in moving to the next category. We settled on a $4 million increase from where we started, he said.

I keep seeing in your presentations that the reason rates are going up is because of the increased benefits BPA is providing, Ryckman said. She expressed concern about some of those "benefits" – I think when we provide benefits, BPA has a duty to fund only those projects that are the effect of BPA operations. I went to one of the regional PFR public meetings and was dismayed to see it held in a building where there were posters and bumper stickers displayed that talked about taking out dams, Ryckman commented. We should not be providing funding beyond BPA's responsibility – others should pay for that, she stated. I encourage you to continue to focus on programs on the ground and not to provide funding for "unfounded research projects," Ryckman said. And we need to set goals for F&W, she stated.

This process has been good until this last step, Ed Sheets (Yakama Nation) stated. The F&W managers worked with BPA to come up with a cost for implementing the subbasin plans, he said. BPA and the Council spent $15 million to develop the plans, "which give you the goals you are talking about," according to Sheets. The subbasin plans developed expectations about implementation, he said. In developing costs, the F&W managers looked at funding implementation of the plans over 10 years, Sheets said. I thought we were making good progress, but in this proposal "it looks like BPA has ignored F&W managers," he stated. There is no salmon fishing going on now, and that is hard on the tribal communities, Sheets said.

With BPA's funding proposal, it would take decades and decades to achieve results, he continued. The proposal doesn't factor in inflation, and it also relies on a shift away from research, monitoring, and evaluation (RME), while scientists are telling the region to do more RME, Sheets said. The tribal managers are frustrated, he stated. They want to work these issues out in the region, but where is the willingness to do that? Sheets asked. If they cannot work things out here, the tribes may take other actions, he said.

I am sympathetic to economic conditions on the reservations, Eldrige said, but he questioned whether it is BPA's responsibility to address them. The early settlers decided they needed to farm to survive "because nature does not always provide," he said. I think the harvest situation is tragic with spring chinook this year – we still set fishing levels before the escapement is known, and it's a poor process, Eldrige said. I'd encourage BPA to keep the budget pressure on F&W, he said. We do not have an agreement on where we want to go, and we don't know what the investment will achieve, Eldrige said. He also questioned how well the Council's F&W program is coordinated with the ESA.

While the dams have had an impact, so have the 10 million people who live here, the freeways they've built, as well as many other aspects of modern life, Eldrige said. BPA should not come up with all of the money for fish recovery, he said. What are the casinos, the states, and other sources contributing? Eldrige asked.

I echo those comments, Marshall stated. One way to enhance meeting our goals is to pay attention to what happens at the time the fish are trying to return to spawn, he said. We go to great lengths to try to prevent "accidental loss" at the dams, but just before the run comes back, we have sea lions eating salmon and ocean harvest going on, Marshall pointed out. We have sent comments to the Pacific Fisheries Management Council asking why they are setting a harvest level on endangered species just at a time when they are ready to spawn, he said. If BPA is going to try to recover fish with everything that is in the subbasin plans, then money has to be put into preventing harvest when the fish come back to spawn, Marshall stated.

This is the most expensive environmental recovery plan in the world, he said of the region's fish recovery effort. "Yet we have no plan to prevent intentional killing," Marshall stated. We can't continue business as usual, where everything we do is offset by other actions, he said.

We have been listening for years to the need for goals and objectives, and we now have them in the subbasin plans, Cavanagh said. If budgets are cut for F&W recovery, "blunt instruments will intervene," and it will eventually cost us all more money, he advised.

I'm surprised that utility managers are now acting as "marine scientists," Steve Weiss (NWEC) said. I think we can discount those opinions – "the numbers taken in harvest are trivial," he said. These are just "silly solutions" people try to come up with, Weiss said. Many, many people are paying the bills, he continued. And the populace in the region is supportive of paying that bill, according to Weiss. The bill is relatively small and should be put into perspective – "it's not that much," he said. The customers talk about "foregone revenues," but that is "a fictitious number," Weiss said. It assumes that the river belongs to electricity production, he stated.

The Yakama Nation will be in Washington, D.C. next week to work on the sea lions, Sheets reported. With regard to harvest, the tribes are very sensitive, he said. Over the years, the tribal harvest has averaged 7 percent, according to Sheets. How much lower should it be? he asked. If you cut harvest, more fish will come back, but you have to fix the habitat to get a good return for the additional fish, Sheets said. The Council decided the issue about BPA's responsibility, and "organizations around this table endorsed that outcome," he stated. The goal is to double runs to 5 million fish above Bonneville Dam by 2025, Sheets said. The average is now 2.5 million – we aren't there yet, he added.

If you include the replacement power costs, F&W recovery is 28 percent of Umatilla's power bill, Eldrige stated. We spread $7 million among 9,000 customers, he said. Not everyone pays for this – does BPA "get checks from Starbucks and from PGE"? Eldrige asked. We will do our part, that's our responsibility, he stated. But until we have a goal, we'll never come together, Eldrige said.

I want to encourage BPA to continue to improve the quality of the F&W program, Tom Karier (NPCC) stated. I'd like to see you approach the program with the same passion you put into transmission and power production, he said. I've been pushing for accountability and being systematic in the program – BPA is now doing a good job, but it has taken 20 years, and it is overdue, Karier stated. There is a lot to be done with the data system, and it will take a lot of effort to make sense of all of the information, he said. I'd urge you to continue on the path you started, realizing you may have to double your effort to get there, Karier said.

We heard that there could be $46 million in foregone revenues associated with the in-river transportation study that has been proposed, and that this cancels out the gain from the installation of removable spillway weirs (RSW), Saven said. We also heard that this is a measure out of the Updated Proposed Action, so "we can't touch it," he said. The customers have suggested not doing the study, cutting back the scale, or delaying it until the RSWs are in place, Saven stated. We asked our attorneys about the flexibility under the Biological Opinion to do that, and "I'd like to assert vigorously," there *is* flexibility with the design and when this study is done, he said. The $46 million is a lot of money – it's too much given other demands, Saven said. He urged BPA to talk to the other agencies about changing the transportation study plan.

There is a lot of difficulty with costs that are "a step removed" from BPA, such as the Corps, Reclamation, and F&W, Marilyn Showalter (PPC) stated. The players with the direct responsibility for those costs are not here, she said. Given that, you need to think carefully about placing transmission costs into another institution, specifically an RTO, Showalter advised. Doing so would create the same type of situation, and you need to think about that, she said. There is a very big difference between BPA's direct costs and costs that are another step away and out of your ability to control directly, Showalter pointed out,

Norman moved on to explain the "other cost" category, which includes $40 million to serve DSIs. With regard to efforts to reduce internal costs, we don't have the results yet for our process reviews and other recent cost management initiatives but had comments that we should included an estimate of that potential, he explained. We proposed an $8 million placeholder, Norman said.

I would compliment you on your transparency in this area, Gregg said. The downside to that is customers are more familiar now with the line items, he added. Gregg suggested BPA set inflation at 2 percent and back out $20 million more in costs associated with IT and general corporate overhead. Get back closer to your 2001 levels, he urged. With regard to the industry restructuring costs, I'm not convinced 40 percent should be allocated to power since this effort is largely aimed at transmission, Gregg stated.

PBL and TBL are doing a great job in cutting costs, but it is disappointing to see Corporate is not following that lead, Clark said. There are "phantom" IT costs included in the numbers and nothing to back up some of the other costs, he said. The Corporate costs continue to rise – there was a $14 million increase going in, and there is still a $6 million increase, Clark stated. There is a good example being set by the business lines that is not being followed by Corporate, he summed up.

I'm confused by the numbers you are using – I don't see it, Wright said. Yes, we need "to run those numbers to ground," Norman agreed.

Simultaneous with the PFR, we were defining the future structure of our conservation program, Norman continued. We adopted our share of the Council's goal in the Fifth Power Plan as our target, and we set "an aggressive per MW cost" for meeting that target, Norman acknowledged. The reduction we have made since the PFR opening numbers reflects the conservation we think will occur without a BPA investment, he said.

"This is an issue closest to the heart of the Council's mission," Karier commented. We commend you for adopting the Council goal as your target, but we are confused about your proposal for treating IOU conservation, he said: you are not responsible for meeting an IOU-related target, but you have conservation and renewables discount funds going to them. We also have a concern about whether you can achieve the target with the budget you propose, Karier went on. The consequence could be that "you play catch up" and pick up the additional costs in the next rate case, he said. If you don't catch up, alternative generation will be needed, Karier pointed out. What happens if you fall short? What assurance do we have you will meet the target? he asked.

Cavanagh said he had not heard anyone tell the Council at its Portland hearing that the conservation target was too high. He noted that the conservation targets in California are now higher than those in the Northwest. I am concerned about the inadequacy of funding and suggest we target the money toward irrigation efficiency, where we could save both electricity and water, Cavanagh said. To see BPA cut the conservation budget from where it was at the beginning of this process "is troubling both in substance and symbolism," he said.

Weiss said he wanted to reiterate that the display for conservation costs should indicate that there are offsetting revenues to be gained. He took issue with BPA's analysis of the difference between the market and the potential revenue from the conservation resource. The benefits are between $20 million and $30 million over the three years – conservation will reduce rates, and you should count it as an offset, he added. If not, you should hold the revenue in a reserve fund to backstop the conservation acquisition target, Weiss said.

I would echo the Council's concern about the budget for conservation, Sheets stated. Conservation will keep costs lower and benefit the environment, he said. I'm also interested in the suggestion about targeting irrigation efficiency – that could provide water for fish and for increased generation, Sheets commented.

All customers pay for conservation, and they are being lumped together despite the need for a more tailored approach, Rick Lovely (Grays Harbor) said. We have never stopped doing conservation and we own renewables – we are trying to avoid buying higher cost resources, he stated. But the way the program is being laid out, we are being penalized, Lovely said. We don't like the ConAug program, and it is a challenge to realize that if we don't participate, we still pay without getting any benefit, he said. I would encourage BPA "to design a program that works for all customers," Lovely stated. We used to be a participant in Centralia, and we were decremented 52 MW for that and experienced "a huge penalty" for replacing that power, he said. We're working within the community on conservation and renewables – but the way the program is structured is not fair to all customers, Lovely stated.

I would echo Tom Karier's comments, Hirsh stated. We commend BPA for adopting the Council's target, but because of the way you are treating the IOUs, 52 MW is not your true share, she said. We would like to see you revisit that issue, Hirsh stated. I would also like to reiterate the concern about the funding level and the lost opportunity that will occur, she said. It will be more expensive in the next rate period "to fix" things, Hirsh said. If the funding level is too low, as many think it is, we need to know how you will address that, she said.

Consider not making the $5 million cut in conservation and hold that amount in reserve as a contingency to either put toward the irrigation effort or use as a backup if the you don't meet the target, Clark suggested.

We have been proactive about conservation, and it has become more expensive for us to gain conservation savings, Ryckman said. I would ask you to reconsider the list of cost-effective conservation measures, she said. Don't discount additional measures that may be feasible, Ryckman recommended.

I'd support Jean and Rick's comments, Nadal stated. "One size does not fit all with conservation," he said. Our members have met their five-year target for conservation already, Nadal pointed out. We need flexibility for customers in different areas so "we can capture the potential out there" – otherwise we will miss some, he said.

We were concerned about locking into a cost-effectiveness list, Karier responded. We think the Regional Technical Forum can be a source of information on that, he said.

Generally, the conservation BPA should fund is what would show up in a utility's Integrated Resource Plan, Eldrige commented. You need flexibility in the program that falls outside "a static list," he added. For example, there are opportunities with food processors in our area that take time to develop, Eldrige said. We are willing to work with the irrigators on efficiency, but the irrigators should get credit for the water and energy saved this time around, he stated.

Snohomish has a big conservation program, and we plan to continue, Marshall stated. We don't want to be punished through the design of the program – we need to be able to meet local needs and have local control so the program addresses needs in our community, he indicated.

Norman explained that the Calpine geothermal plant expenses were removed from the budget in the first two years of the next rate period, which means an $11 million per year reduction. That has been partially offset by a budget for renewables facilitation activities, he said.

Cavanagh said the change in the renewables budget represents a substantial decrease from the original PFR numbers. He said the region has the potential to become a national and world leader in the development of wind resources and suggested the funds be dedicated to such an effort. It is worth the expense to get this going, and it is "our strong recommendation," that you put the funds back, Cavanagh said. The amount is small, but the benefit is large, he stated.

If you are going to develop wind, having a flexible river to integrate the resources is a big benefit, Kevin O'Meara (PPC) pointed out. To maintain that potential, I'd advise caution in taking the flexibility from the river system by imposing fish operations, he said.

This is not just about wind, Hirsh said. The biomass potential in this region is unprecedented, she said. There are other small resources BPA could help customers with – you should help facilitate these resources, Hirsh urged.

Developing small resources doesn't always work because of their location and the need for transmission capacity, Eldrige pointed out. He suggested it would be more helpful to help local utilities absorb the energy from small projects into their systems, rather than to send the energy out onto the grid. You could facilitate that, Eldrige said.

We've teed up the issue of risk in the PFR and looked at options, Norman said. The issue will continue into the rate case, and it may be the biggest factor we address there, he said. We have heard your point about reconvening a management-level group on risk before the rate proposal, Norman added.

The numbers in the draft closeout get us to 27.5 mills, and we're looking at 31 mills or more before you add cost adjustment recovery mechanisms, Michael Early (CFAC/Alcoa) said. We are probably not looking at a rate decrease, and we are probably looking at the same rate or something higher, he said. The issue I'm concerned about with the customers is how we want to bear the risk, Early said. Risk should be a partnership – I'd urge you to put conditional budgeting back on the table for discussion, he stated.

I don't want to see BPA ties its hands too much with the risk mechanisms, Weiss stated. Things come up – we have big uncertainties with fish, and you have to be able to cover yourself, he said. The Administrator needs discretion, Weiss said.

There may be opportunities now that will be too late when the rate case starts, Marshall said. I'd urge you to look at borrowing money with a line of credit or some other mechanism to meet the uncertainties related to hydro operations, he said. But it will require planning and work, and I'd encourage you to start that thinking process now, Marshall advised.

With regard to the Treasury Payment Probability, there are many things predicated on a 10-year-old study, Saven said. I'd encourage you to be more creative about approaching how your financial plan is put together, he said.

Wrap-Up

It is extremely helpful to hear your comments "face to face," Wright said. I don't want to make a conclusion now about the PFR results, but this has been valuable, he said. The "biggest take away" for me is the progress that is being made with your understanding of BPA's financial issues, Wright said. There has been real progress, he stated.

You are asking, and I have asked myself, why rates can't go down to $25.50 per MWh, Wright continued. There are a lot of benefits that we are now providing – we're serving more load, increasing F&W and conservation funding, and increasing IOU benefits, he said. People are receiving a lot of benefits that flow through to rates, Wright said.

"The issue I struggle with is the near-term versus the long-term tradeoffs," Wright said. We've been cutting budgets, and there is "not a lot of fat left," but there are short and long-term tradeoffs, he explained. These are hard decisions and they are value judgments, Wright added.

With regard to a rate target, people have said we lack a real target, he went on. We could solve the issue of a target, but it might be in a way that would not be acceptable to our public customers, Wright said.

As for risk, we are still recovering from the energy crisis, the loss of the fish cost contingency fund, and six years of drought that have left us with low reserves, he said. We also pushed costs off into the future, Wright added. "The problem gets a lot better if we have a good water year next year," but we won't know that before this process is over, he said. Risk will be a big discussion, and I appreciate John's suggestion about having more policy dialogue on this issue – I want to actively pursue that, Wright stated. "This is time well spent," he concluded.

The meeting adjourned at 12 p.m.