Pre-Decisional

WP-07 Power Rate Case Workshop

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7(b)(2) Rate Test

BONNEVILLE
POWER ADMINISTRATION

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Section 7(b)(2) of the Northwest Power Act directs BPA, when establishing wholesale power rates, to conduct a test that involves the comparison of two sets of projected wholesale power costs for the general requirements of BPA's public body, cooperative, and Federal agency customers. If the average set of costs reflecting BPA's normal rate development exceeds the average set of costs reflecting five specified assumptions, an amount of costs to be reallocated to other rates is calculated. If the test triggers (costs greater than benefits), BPA develops a lower PF Preference rate and a higher PF Exchange rate. A higher PF Exchange rate results in lower REP benefits for exchanging utilities and lower costs for BPA's public customers.

- **The Section 7(b)(2) Rate Test Methodology requires that the 7(b)(2) Case world be modeled exactly the same as the Program Case real world except for:**
    - Serve only those DSIs that are within or adjacent to public agency service areas.
    - Public load is served by the FBS.
    - Exclude the Residential Exchange program.
    - 7(b)(2) resource acquisition stacks are defined and sorted least cost first.
    - DSIs provide no reserves and resource financing benefits due to BPA backing are not achieved.

- **The test is a cost/benefit analysis from the point of view of the Public customers.**
    - Costs: *(increase trigger)*
        - Residential Exchange Program (REP) costs.
        - Continued service to the DSIs.
    - Benefits: *(decrease trigger)*
        - Nonfirm sales to the top-quartile of DSIs at higher prices than market.
        - Restriction rights on DSI load.
        - Financial benefit of BPA backing of resource acquisition.

- **Pre-1996 7(b)(2) Rate Test.**
    - Costs:
        - Large gross REP costs.
        - BPA at L/R balance, so small cost of continued service to the DSIs.
    - Benefits:
        - Small benefit of having a ready DSI market for BPA secondary sales.
        - Large benefits of having DSIs provide generating reserves ~$150M/yr.
        - Small benefit due to BPA backing of resource acquisition.
    - Rate Test results
        - Benefits and costs in balance.
        - 7(b)(2) trigger at or near zero.
        - PF Exchange rate equal to PF Preference rate.
        - Net REP costs ~$140 to $200 million per year.

- **1996 Rate Case 7(b)(2) Rate Test.**
    - Costs:
        - Large gross REP costs.
        - Due to Public load diversification, BPA at L/R balance, so small cost of continued service to smaller DSI load.
    - Benefits:
        - DSIs served with firm, therefore there is no benefit of top-quartile sales.
        - No restriction rights on DSI load. Therefore no generating reserve benefit.
        - Change in tax code eliminates financial benefit attributable to BPA backing of resource acquisition.
    - Rate Test results
        - Benefits and costs no longer in balance.
        - 7(b)(2) trigger is 3.2 mills.
        - PF Exchange rate much higher than PF Preference rate.
        - Net REP costs ~$70 million per year.

- **2002 Rate Case 7(b)(2) Rate Test**
    - May 2000 7(b)(2) rate test was conducted assuming the IOUs would not sign their Subscription REP Settlement Agreements.

- **2007 Rate Case 7(b)(2) Rate Test.**
    - Costs:
        - Possible large gross Public REP costs.
        - Net IOU settlement costs ~$300 million per year.
        - Program Case near L/R balance with only FBS, so small cost of service to smaller DSI load (or moderate cost of monetary settlement with DSIs).
    - Benefits:
        - DSIs served with firm, therefore there is no benefit of top-quartile sales.
        - No restriction rights on DSI load. Therefore no generating reserve benefit.
        - No benefit attributable to BPA backing of resource acquisition.
    - Likely rate test results:
        - Benefits and costs remain out of balance.
        - Wide range of possible 7(b)(2) triggers: 1.0 to 5.5+ mills.
        - PF Exchange rate could be much higher than PF Preference rate.
        - Possible Public REP net costs ~$25 to $150 million per year.

- **2007 Rate Case Issues That Affect Outcome of 7(b)(2) Rate Test.**

    - Non-dedicated Mid-C resources in or out of 7(b)(2) stack?
        - If Mid-C resources are out, the trigger is lower.
        - If Mid-C resources are in, they would be re-priced higher in 2007 and would have smaller non-dedicated portions in 2007 with a smaller effect on the rate test than previously thought.

    - Treatment of IOU REP settlement costs.
        - Are these program costs associated with the REP?
        - Are these exchange resource costs?
        - Are these costs analogous to the net cost under the traditional REP?
        - Are these costs associated with the REP such that they will not be in the 7(b)(2) Case?

    - Treatment of BPA Service to DSI load.
        - Whether dollars to the DSIs are the same as “served by the Administrator” is a legal issue.
        - If they are not in the 7(b)(2) Case, the trigger would be larger.
        - If DSIs are “served by the Administrator” in the Program Case:
            - How large should the 7(b)(2) Case DSI load be?
            - Which plants would be eligible for power?
            - How should the concept of “elasticity of demand” be used?
        - The larger the DSI load in the 7(b)(2) Case, the smaller the trigger.

    - Treatment of conservation in the 7(b)(2) Rate Test.
        - Is conservation an FBS resource?
        - Should annual programmatic conservation financing in the 7(b)(2) resource stack be modeled as it actually occurred?
        - Should annual programmatic conservation financing in the 7(b)(2) resource stack be modeled to comport with “sound business practices,” with respect to total expense vs. capital?