Bonneville Power Administration
Power Function Review Technical Workshop
May 9, 2005

BPA Rates Hearing Room, Portland, Oregon
Approximate Attendance: 20

Draft Closeout Letter and Wrap-up

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

Introduction

Michelle Manary (BPA) opened the workshop, noting that it was the last of the technical sessions and an opportunity for wrap-up and Q&A on the draft Power Function Review (PFR) proposal. Staff members from most areas in the PBL are available today to answer questions, she said. The PFR closeout letter "is very draft" at this point, and your comments are welcome up to May 20, Manary added.

She went on to the table of spending levels. I have added a column entitled "Could be Updated for Rate Case," Manary pointed out. In addition to updates prior to the rate case, we could make changes as a result of recommendations made during the PFR comment period, she clarified.

Linc Wolverton (ICNU) asked if treatment of the period for amortizing capital outlays would be open for discussion in the rate case. Manary said that it would.

She started through the PFR decision areas on the table, noting that in the closeout letter, BPA proposed to remove $11 million associated with the Calpine geothermal project from the forecast of renewables costs in 2007 and 2008. The "maybe" indicates the forecast could be updated for the rate case if the ongoing arbitration on Calpine comes to a conclusion in time, Manary explained.

The budget figures in both renewables decision areas – Calpine and facilitation – are subject to change before the rate case, according to Deb Malin (BPA). The future of the Calpine plant is uncertain due to arbitration, and figures for facilitation are not yet nailed down, she said. We are working with a focus group and discussing things we could do to facilitate customer development of renewables, Malin explained. The $11 million forecast for the Calpine project is based on what the project costs "at $4 gas," she said. We are proposing to use part, but not all, of the $11 million for facilitation, Malin said.

If the Calpine project goes away entirely, would you provide $11 million for other renewables? Annick Chalier (PPC) asked. We will likely know about the outcome of the Calpine arbitration before the rate case begins, Malin responded. If the plant is terminated, that's something we would consider, she added.

Manary continued through the list of PFR decision areas and proposed reductions and increases. These budget numbers are the deltas from the initial PFR forecast, she clarified. The final numbers for the Enterprise Process Improvement Project (EPIP) will be out between the initial and final rate case proposals, Manary said. In the initial proposal, we will reflect an $8 million reduction as a result of EPIP, which we'll update later, she indicated.

When we update forecasts for the initial rate proposal and make changes in the budget numbers, would you want to meet again? Manary asked. Some of these changes are really important because 2007 is such a financial problem, Geoff Carr (NRU) answered. It would be valuable to bring it all together, he said. It would be nice to have an update every couple of months, Wolverton agreed. How about a session around September, the time of the initial rate proposal, and another in a couple of months? he suggested.

Manary pointed out that the "maybe" with regard to the Columbia Generating Station (CGS) forecast reflects the fact that the Energy Northwest (EN) board has not yet approved the cost-cutting initiatives proposed by EN management. Has EN assured us that if the board approves the budget reductions, they won't come back for more money? Michael Early (Alcoa/CFAC) asked. I'll check on that, Manary replied.

What would cause the funding for WECC/NERC compliance to change? Lon Peters (PGP) asked. We have a program review going with regard to WECC/NERC operating requirements for the Federal Columbia River Power System (FCRPS), Mike Alder (BPA) responded. We will have more certainty about the budget numbers for compliance by June, he said.

Carr asked about the tables on page 16 of the PFR closeout report. The first table compares the PFR base with the PFR base adjusted for debt financing of CGS capital, Manary explained. The second table reflects the concern about rising nuclear fuel prices, she said. The table reflects what would happen with O&M if certain items were capitalized and if fuel prices increase, Manary said.

She explained that the uranium tails processing project is part of the uncertainty surrounding nuclear fuel prices. The price goes up and down, but we should know soon about whether the uranium tails project will proceed, Manary said.

Does the $143 million budget for the integrated fish and wildlife (F&W) program depend on Council approval? Peters asked. Yes, Manary said. Bob Austin (BPA) explained that BPA and the Council are in discussions about a memorandum of agreement (MOA) on F&W costs. The MOA is two part, he said: the first is "the rules of the road" with regard to the F&W spending, and the second part is the budget. We think we are close to an agreement, and we expect to sign an MOA in late spring or early summer, Austin stated.

This figure reflects only BPA's responsibility for F&W, Val Lefler (BPA) said in response to a question about other agency contributions. Why does BPA alone have to spend so much money? Early asked. This budget should not reflect just a Council decision, BPA can also make a decision, he said. I understand that Greg Delwiche is preparing a response to parties that wanted an even larger F&W budget, and one point he intends to make is that the F&W spending is not all the responsibility of the hydro system, Early said. But where are the other agency's contributions? he asked. BPA pays the hydro share of the costs, and we get 4(h)10(c) credits for the non-power portion, Lefler replied. We take a 22.3 percent credit against the F&W expenses when we make our annual Treasury payment, she stated.

Manary went on through the list of decision areas, pointing out that the future of the Spokane settlement is "iffy," and BPA proposes to take those costs out of the 2007-2009 forecast. With regard to the Columbia River Fish Mitigation (CRFM) costs, if the Corps does not come to a decision about moving them to plant-in-service, you can debate their treatment in the rate case, Lefler said. But if the Corps makes a decision, we will include it in the rates, she added.

How can we affect the Corps decision? Carr asked. Can the customers be more involved in that? he inquired. BPA staff said they would look into that question and report back.

What if the Corps makes its decision after the rates are set? Howard Schwartz (WA ETED) asked. By the end of the rate case, we will have set our repayment schedule, Lefler stated. A later decision would not affect the schedule, she indicated.

There are CGS fueling outages in the schedule during the rate period, Pete Peterson (PGE) commented. What if they are longer than expected? he asked. That's a risk, and it could affect the 2007-2009 rate period, Manary responded.

What do we know about the CRFM decision schedule? Mark Thompson (PPC) asked. There is "a sense of urgency" at the Corps about this, but we don't have a schedule, Alder acknowledged.

Most of the "maybes" on the table relate to things that mean giving up any savings, Joe Hoerner (Tacoma) pointed out. Some could go either way, Manary replied. We tried to put our "best case" into the budget, but we will true things up for the rate case, she said.

And there is no chance the $11 million for Calpine would stay in the budget and $5.5 million would also be added to renewables? Doug Brawley (PNGC) asked. No, that won't happen, Malin answered.

It looks like the only "maybe" that could be beneficial for cost reductions is EPIP, Early noted. The $8 million is a goal we are setting for ourselves, Brian Crawford (BPA) responded. We feel comfortable with the $8 million – "we aren't being grossly conservative" either, he said. By the time the final rate proposal comes around, we would have identified savings that are actually related to EPIP work, rather than a forecast, Crawford indicated. The customers came up with a much larger number than $8 million, Hoerner said.

Manary went over the bullets on page 2 of the four-page meeting handout. The first relates to Corps of Engineers and Bureau of Reclamation savings as a result of benchmarking, she said. In the PFR, we heard from other utilities that they had ideas for cost savings and innovations that could benefit the FCRPS, Mike Alder (BPA) elaborated. There are several utilities we could sit down and talk to about costs and see if there are innovations we could incorporate into FCRPS O&M that would lead to efficiencies and savings, he said. We've been talking about getting this done by next April before the final rate case proposal, Alder stated.

Our benchmarking shows that the FCRPS O&M costs, excluding those associated with F&W measures, are lower than for other utilities, he continued. But if there are efficiencies we could gain, we want to sit down and talk about it, Alder said.

With regard to the Corps and Reclamation's "2012 program" and potential staff savings, the agencies have an efficiency program under way, but we don't know what the outcome will be, Alder stated. It's too early to say, but they offer the potential for cuts, he added.

The last bullet refers to the $40 million DSI "placeholder" in the budget, Manary wrapped up. A final number will be based on the DSI Record of Decision, but we wanted to have a budget number even though it will be replaced, she explained.

Participant Comments

If you look at the $80 million in savings you've come up with, it falls into two pieces, Early pointed out: first, there are changes related to financing, and second, there is a correction and actual costs you will not incur, at least not now. Of the second group, the biggest is related to CGS, where EN took an aggressive stance to get costs down, he said. If you add all of the reductions in the second group together, it's about $41 million – only CGS "has done the right thing and cut costs," Early stated. It is hard to believe this is all you could do, he added.

Before the PFR started, "we scrubbed the numbers" and we came in with the tightest budget possible, Manary responded. PFR was not about cost cutting, but about educating you on our costs and asking are they as low as possible, she said. The CGS budget was based on an old number, and it was high when the came into the PFR, Manary said. There was a lot of room to cut, she added.

We are trying to get rates down, yet when I compare the 2007-2009 forecast with the 2002-2006 actuals for the first 11 items on the page 32 table, there is a $194 million increase, Lyn Williams (PGE) pointed out. The purpose of our workshops was to explain what is driving the costs up, Manary replied. It's primarily three things, she said: debt management, Columbia Generating Station, and Corps and Reclamation O&M.

Your costs have only gone down the equivalent of a mill since you started, and we still have to deal with risk, Carr commented. The folks I work for are expecting a rate reduction, he said. The joint customers came up with cost decreases that were much greater than what you have laid out, and ours "weren't slash and burn," Carr said.

Kevin O'Meara (PPC) questioned why BPA is assuming IOU benefits are a big risk, if they are going into the budget at the highest possible level.

You are telling us that the PFR was to demonstrate to customers that these are the budget levels you need to operate, Early said. You rejected the customers' recommendation of conditional budgeting, and you have budgeted at a level that "you are comfortable with" in performing your mission, he said. What we want to know is, what is the minimum you can budget to perform the necessary functions, Early stated.

Has BPA done an analysis of the value of activities "on the margin"? Karin Bulova (Snohomish PUD) asked. In the PFR, we were asking, what is the lowest we can go and still meet our basic obligation, Manary responded. She pointed out that the Corps and Reclamation, for example, have many more projects they want to do on the hydro system, but we have said we won't fund them, she added.

But what is the minimum cost to perform your functions? Early asked. If a utility had to take a five percent reduction in its budget, it would still perform its basic functions, he said. "What is so special about BPA that you can't do that?" Early asked.

This budget is viewed internally as minimal and "bare bones," Manary said. It's what we think we can get by with, she said. BPA managers are not "comfortable" with these numbers, Manary added.

But what if someone said, the rate has to be 26 mills, "now do it"? Wolverton asked. You push against the Corps and Reclamation on costs, but "we don't see you pushing against yourselves," he said. A clear example is renewables, Wolverton stated.

This proposal is still draft, and it could change, Manary responded.

The 2002-2006 capital O&M for the Corps and Reclamation was $110 million, but it's forecast at $28 million higher, Williams pointed out. Why is it higher than the absolute minimum? she asked. Our asset management strategy set out two things, Alder replied: restore the reliability of the FCRPS and increase revenues by $50 million a year. We have not yet restored reliability, he said. We are also pursuing revenue increases as we make improvements, Alder said, adding that there is efficiency to be gained in such projects as the runner replacement at Grand Coulee. And we are gaining efficiency with the Near Real Time Optimizer, he stated.

In response to a question, Manary clarified that risk mitigation would be a rate case decision. Byrne Lovell (BPA) said BPA would propose a 95 percent Treasury Payment Probability in the rate case, "based on guidance from the Administrator." Data and information will be updated at the time of the rate case, he said. The "risk tolerance questions are not up for grabs," but we are open to considering how to address risk, Lovell said. Rate design issues will be addressed in the rate case, and we're open to talking about the approach to risk, he said.

Paul Norman (BPA) joined the meeting and asked for a recap of the discussion.

When you came out with your first PFR numbers, you made a presentation at PNUCC and were apologetic the numbers were so high, Early began. You asked for customers help to get them down, he said. The original numbers would have meant a rate increase, and there was no "political will" to accept a higher rate and the repercussions it would have for the economy, Early said.

Now, with the PFR closeout, you have identified $80 million in cost cuts that fall into two roughly equal pieces Early said. The first $40 million has to do with financing changes and basically things you will be paying later, and the second is made up of a $13 million correction, a $6 million settlement that you don't control, and the "big ticket" item is CGS, he pointed out. The $22 million CGS reduction represents "an aggressive stance" by EN, and a response to customers, who told them to get their costs down, Early said.

At the end of the day, even though you said months ago that the costs were too high, we see no real savings in most areas, he indicated. Yet there is no change in the political will about the acceptability of a rate increase – that hasn't changed, Early added.

And this could go even higher when you add in risk, which could mean another six to eight mills, Carr pointed out. We have not gone far enough in reducing costs, he stated.

This process was about full disclosure of our costs and to have you give us advice about how to manage those costs down, Norman responded. Our costs are $80 million less than when we started, "and that is not trivial," he added. I am motivated to get the costs down – "I have 27 mills written on the whiteboard in my office," Norman said. It's a real target, and if this is not good enough, that's a problem, he added. But we need to know where we can look for opportunities to cut, Norman said.

We will try to "sharpen our pencils" and identify areas, Hoerner said. But we heard that the cost levels are at "bare bones," and so I'm not sure there is room for improvement, he said. "With cost control, you are never done," Norman responded. I don't think we are done, he added. If all you want to tell us is "do better," that's okay, but it would be helpful to have you direct us to particular areas, Norman stated.

That is hard to do from outside the agency, Hoerner replied. "The door is only cracked so far," and we don't see the whole picture, he said. Have we not been forthcoming enough? Norman asked.

The "KEMA kind of thing" is the most helpful to us, Wolverton responded. We're at a disadvantage being on the outside, he said.

You rejected conditional budgeting, and that was the way we hoped you could help us, Bulova stated. It would also help us if you would say, “here are our programs, and if we eliminated *this* part, *this* would be the outcome,” she explained. Or suggest another way you could fulfill the responsibility, Bulova said. We are disappointed that you rejected the suggestion on conditional budgeting, she said. We would ask you to look at it again, inform us of the repercussions of eliminating things or doing them a different way, Bulova urged. That would be a benefit to you and to your customers, she stated.

Are you suggesting that if we look at our programs from that angle, we may see something new? Norman asked. Yes, Bulova responded.

I want to reinforce that you talked about tradeoffs, Early said. We asked you to explain what the consequence to our service would be if you did not do something, he said. But we just got a justification of the expense levels you put out, Early said.

It is hard to have this conversation in the abstract, Norman commented. I hear your point, but it’s a more meaningful conversation if we have it around a specific category of costs, he suggested.

We have not seen yet what would happen if you cut your budget 5 percent or 10 percent, Lon Peters (PGP) stated. “What would not get done or done less well – what would break?” he asked. We don’t know, but your managers do, he said. Without that type of analysis, “I’m flying in the dark,” Peters said.

Brawley pointed out that some of the cost justification is too general to judge. We hear that something can’t be cut because “it would jeopardize your mission,” he said. Maybe your essential services are too much for us to afford, Brawley said. Conservation is one example, he said. We still hear people say that the conservation budget does not need to be so high, Brawley said. Part of the problem is that you decided the Council’s goals were your goals, he added. Maybe customers should do the conservation – maybe it’s not part of your job, Brawley suggested.

There is no good answer, Wolverton commented. Sometimes the best way to approach cutting is to just say, cut 10 percent and see what happens, he stated. That’s why a target makes sense – you set it and figure out how to get there, Wolverton said.

Norman pointed out that he has only $100 million of BPA’s budget on which to affect direct cuts. As for the public purposes, I’m not sure it’s responsible to cut regardless of whether we know the effect, he said.

You almost have to make “a fiat-type decision,” Wolverton responded. There are probably categories that could not take a 10 percent cut, he acknowledged, but we are talking about proposed increases above 2002-2006 levels.

You are asking us to do more work and get more specific, Carr said. The KEMA analysis was the most helpful thing for us, he said. It got to the level of detail needed, Carr stated. We'll do the best we can, but we are up against not knowing what the tradeoffs are, he added.

Where we had that information, we gave it to you, Norman replied. It's hard to know the exact impacts of a 5 percent cut, he said.

To make an informed recommendation, it takes an analysis like the one KEMA did, Hoerner said. The only way we could do that is "to dive in, take up residence here, and act like auditors," he pointed out.

We're trying to give you that type of information, Norman responded. But you are saying we are not doing a good enough job – "that's not what I expected to hear, but I hear it," he said.

When we hear a vague reason like "it would jeopardize reliability," it's not enough detail for us to make a judgment, Williams said. We don't have enough information to know what that means, she said. If we have any information that could help you with efficiency, such as with our hydro operations, we want to sit down and talk about it, Williams added.

"I'm cautiously optimistic" there are things that can change before our final proposal, Norman said. We need to have this conversation – we need to get down to specifics, he said. The Corps and Reclamation feel they are doing a KEMA-type process internally with the 2012 program, and we could get value out of that by the first of next year, Norman added.

It comes down to a value choice, Hoerner said. We saw value, for example, in the Technology Improvement Initiative, he pointed out. It comes down to whether value is being created – we need enough information on that to make informed decisions, Hoerner said.

The frustration we have is that we are facing "a mass of costs" that will be put to bed, and then in the rate case, we will be talking about how much to add for risk, Carr pointed out. I want to get this part as low as possible before we put it to bed, he stated. "We need to make room for risk," according to Carr.

Peters asked whether there is benchmarking going on with hatchery programs. The Council has conducted the Artificial Production Review and Evaluation – it's an area that could be fruitful in the future, according to Bob Austin (BPA).

What would you do if you had to cut costs, if you were above market? Hoerner asked.

We have a lot of fixed costs – it's a somewhat inflexible cost structure, Norman acknowledged.

The meeting adjourned at 3:40 p.m.