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CURRENT



SELLING BPA POWER IN THE 21ST CENTURY

POWER SUBSCRIPTION STRATEGY

The Bonneville Power Administration has adopted a Power Subscription Strategy to guide its power sales contracting and rates starting in fiscal year 2002. The success of the subscription process is the cornerstone to BPA's ability to serve the Pacific Northwest. It will provide the revenue base that will enable BPA to carry out its mission to bring the least expensive electricity possible to its Pacific Northwest customers, to meet all of its environmental obligations, and to spread the benefits of federal power as widely as possible to Pacific Northwest consumers.



The subscription strategy reflects BPA's continuing evolution. From its early years of building the transmission system and selling power from federal dams so electricity could reach the far corners of the Pacific Northwest, BPA has become an agent for delivering economic and other public benefits. Part of the strategy, for instance, deals with mechanisms to ensure that BPA can meet its share of salmon and steelhead recovery costs in the Columbia Basin while still keeping federal power affordable.

The strategy charts a course whereby an increasingly precious resource, federal Columbia River hydropower, will be spread equitably throughout the Pacific Northwest. And in doing so, BPA will meet both the letter and spirit of existing law.

The strategy also clears the path for power rates for 2002 to 2006. BPA expects to begin its formal rate-setting process in early spring 1999.

BPA released its Power Subscription Strategy Proposal on Sept. 18, 1998, for public comment. Nearly 200 individuals and organizations responded with about 600 pages of ideas and suggestions. Commenters included BPA customers, general and special purpose governments, public interest groups, tribes and individuals. These comments led BPA to make changes to its proposed strategy that reflect a wide range of interests.

GOALS UNCHANGED - BRING VALUE TO THE REGION

Fundamental goals driving the final subscription strategy decisions have not changed. They are as follows:

- ◆ Spread the benefits of the Federal Columbia River Power System as broadly as possible, with special attention given to the residential and rural customers of the region;
- ◆ Avoid rate increases through a creative and businesslike response to markets and additional aggressive cost reductions;

- ◆ Allow BPA to fulfill its fish and wildlife obligations while assuring a high probability of U.S. Treasury payment; and
- ◆ Provide market incentives for the development of conservation and renewables as part of a broader BPA leadership role in the regional effort to capture the value of these and other emerging technologies.

That there was virtually no debate about the goals indicates they are sound and reflect regional desires and expectations. The healthy debate about *how* to achieve the goals has improved the quality of BPA's decisions.

GETTING FEDERAL POWER TO ALL CORNERS OF THE REGION

In its September proposal, BPA proposed to sign contracts with customers from about mid-November 1998 to about November 1999. Public utilities would have had first call on the current inventory of 6,300 average megawatts of power. Then investor-owned utilities (IOUs), as a settlement of BPA's residential exchange obligation, could collectively sign contracts for as much as 1,500 average megawatts to serve residential and small farm consumers. This 1,500 average megawatts would have been about 1,000 average megawatts of power with additional power, or a financial benefit equivalent, up to 500 average megawatts. Direct service industries could have purchased whatever amount of power was available as well as some interruptible power.

In comments on the proposal, publicly owned utilities strongly advocated their preference rights and generally supported some sales to investor-owned utilities to serve residential and small farm consumers. Investor-owned utilities and public utility commissions of Idaho, Montana, Oregon and Washington pointed out that the amount of power and financial benefit proposed was less than half of the residential and small farm IOU load in the region. They recommended an increase up to at least 1,800 average megawatts.

BPA agreed with the merit of the arguments, and is increasing the target for sales to investor-owned utilities to 1,800 average megawatts, with the first 1,000 average megawatts in power and the remainder in power and/or financial benefits. The amount of power will increase to 2,200 average megawatts in 2007 to 2011 for investor-owned utilities that sign 10-year contracts. By accepting power and financial benefits, the investor-owned utilities would forego their residential and small farm exchange rights for the duration of their contracts.

Direct service industries told BPA that they were not interested in the interruptible product, and that they wanted the opportunity to purchase as much firm power as might be available. BPA made such allowances for them in its final strategy.

BPA will open subscription to all eligible regional buyers at the same time. The agency is planning to purchase some power to augment the existing system.

BPA responded to comments by extending the time for signing contracts to 120 days after the final 2002-2006 power rates record of decision is signed. This will give utilities and direct service industries time to make their decisions and go through their individual policy and regulatory processes.

MANAGING RISK IN AN UNPREDICTABLE ENVIRONMENT

In its Power Subscription Proposal, BPA outlined a number of financial contingency measures. Not only must the agency plan for uncertain hydro runoff and market conditions, but it also must plan for yet-to-be decided costs for fish and wildlife recovery in the Columbia River Basin. The proposed contingency measures included building net revenues for reserves, using the “fish credits” allowed by the Northwest

COMMITMENT TO FISH AND WILDLIFE

In its final Power Subscription Strategy, BPA is remaining committed to meeting the “Fish Principles” that were announced earlier this year by Vice President Al Gore. A summary of those principles follows:

1. BPA will meet all of its fish and wildlife obligations once they have been established;
2. BPA will take into account the full range of potential fish and wildlife costs (\$438 million to \$721 million);
3. BPA will demonstrate a high probability of Treasury payment (at least 80 percent and seek to meet 88 percent);
4. To meet the range of fish and wildlife costs, BPA will design rates and contracts to best meet those costs in the post-2006 period;
5. BPA will minimize rate impacts on power and transmission customers (BPA’s goal is to avoid a wholesale rate increase for power requirements customers);
6. BPA will adopt rates and contract strategies that are easy to implement and administer;
7. BPA will adopt a flexible approach to respond to a wide variety of fish and wildlife costs; and
8. BPA will use a combination of cost reductions, rate contingencies and reserve levels to achieve these principles.

The final Power Subscription Strategy meets these principles, and BPA will carry the strategies into its power rate case where the principles will guide the agency in setting its final rates.

(The full set of principles can be ordered from BPA. See the end of this document.)

Power Act and adopting a cost recovery adjustment clause (CRAC). As a final emergency backup, BPA proposed, if needed, a temporary surcharge on transmission in the form of a “loan” that would have to be repaid from future power sales. (See *Keeping Current*, Getting Power to the People of the Northwest, September 1998)

Customers and public interest groups responded to these proposals with widely varied positions and suggestions. Many public utility customers cautioned against carrying too large an amount in reserves because it can lead to inefficiency and relaxation of stringent cost management principles. They urged BPA to put a ceiling on any power CRAC and generally did not object to an emergency transmission surcharge. Investor-owned utilities and direct service industries, on the other hand, purchase large amounts of transmission from BPA. They were less favorably inclined toward any transmission surcharge and more accepting of a power CRAC that would apply to those receiving benefits of federal power.

BPA remains committed to a high probability of U.S. Treasury repayment in all the years of the rate period 2002 to 2006. Specifically, BPA relies on a high probability of meeting not only its costs of power, but also all other costs for which the agency is responsible, from Washington Public Power Supply System bonds to fish recovery efforts. (See box on page 3, *Commitment to Fish and Wildlife*.) Since all these obligations must be paid prior to Treasury repayment, if BPA is able to meet its scheduled repayments to the U.S. Treasury, it has enough money to meet all of these financial obligations. (See box, *Why Treasury Payment is Important*.)

Taking all comments into account, and in light of its statutory responsibilities, BPA made some adjustments and clarifications to its treatment of the listed financial contingency measures. The specific ceiling and operation of a CRAC will be taken up in the rate case. BPA will set its rates to attain the desired Treasury payment probability, without a transmission surcharge. In subscription contracts, as in existing pre-subscription contracts, BPA and power purchasers will retain their existing rights regarding any transmission surcharges.

WHY TREASURY PAYMENT IS IMPORTANT

Meeting annual interest and principal payments for loans from the U.S. Treasury is important for two reasons. BPA can borrow from the Treasury, but it must repay interest and principal when due. BPA has authority to *defer* payments to Treasury in the event of exceptionally bad water years or other factors, but the inability to meet Treasury payments on time and in full could fuel attempts from outside the region to take control of the Columbia Basin’s hydropower system.

The other important factor in meeting annual payments is the fact that Treasury payments are last in line of all BPA’s financial obligations. Other obligations include such things as payments on Washington Public Power Supply System bonds, funds for salmon and steelhead restoration, payments to suppliers, and payments to utilities for purchased and exchanged power. So the ability to meet Treasury payments is the truest indicator of BPA’s financial solvency and its political viability.

In addition, BPA will consider some dividend sharing should good market conditions and resolution of fish and wildlife funding happen.

DESIGNING POWER PRODUCTS FOR FLEXIBILITY

BPA will move forward with its power and other service products with little change from the strategy proposal. There will be core products including full service and other firm power products. Full-service customers can expect some differences in heavy- and light-load hour charges, as well as load variance charges. BPA will meet the load growth of full-service customers as part of the full-service product. Core

products also include firm power blocks and partial service. Prices for these products will be subjects of the power rate case.

BPA will offer, as proposed, customized products at bilaterally negotiated prices.

The third category of products, non-subscription products, will be sold on an as-needed basis. Prices for these products will be negotiated under BPA's firm power products and services (FPS) rate schedule.

Both the "Slice of System" (a percentage of the federal system generation) and actual partial service products will be offered, but BPA will continue to hold product design meetings beyond the final subscription strategy. BPA intends to make final decisions on product designs before the initial rate proposal.

ESTABLISHING FAIR PRICING AND KEEPING RATES LOW

As expected, the proposal drew a great deal of comment on pricing strategies. Publicly owned utilities appreciated the need for mechanisms to control the size of the federal power system, but told BPA that tiered rates were not the appropriate mechanism. They provided several good alternative ideas, and BPA has changed the strategy. There will still be a basic priority firm (PF) rate and all publicly owned utilities will pay that rate. However, utilities may face additional charges for placing new load on BPA after subscription has closed. (New load would occur when a preference customer has taken load off BPA, but then decides to return to the federal system or when a new customer requests service.) The added cost of purchasing resources for a new load will be reflected in a targeted adjustment charge to be developed in the rate case. If enough existing federal base system power is available, the price would equal the priority firm rate. If such power is not available, the charge would reflect any purchased power costs incurred to meet the load. The charge also will be tied to a notice period after which the entire customer's purchase will revert to the priority firm rate in the next rate period.

This approach would also apply to qualifying new tribal public utilities. For any new loads placed on BPA which are currently served by a utility's own generating resources, BPA intends to propose a rate that reflects the costs of purchasing power to meet that load.

To avoid contracts expiring all at once at the end of the five-year rate period, BPA will offer the lowest, cost-based rate to utilities willing to sign 10-year purchase contracts. Other incentives for contracts of less than five years will be in effect.

The investor-owned utilities that choose to take power and/or financial benefits rather than participating in the residential exchange program will be able to buy power at rates that BPA expects will be approximately equal to the price of priority firm power. Making these sales to investor-owned utilities for service to their residential and small farm customers is a settlement alternative to participation in the Residential Exchange Program. Publicly owned utilities supported this in their comments, as did investor-owned utilities and their regulators and state governments. BPA believes this mechanism to be a workable and fair approach to settling the residential exchange, and appreciates the comments and suggestions that led to this solution.

For power sales to its direct service industries, BPA expects to develop an industrial firm power (IP) rate in the 1999 rate case that BPA expects will be approximately equal to the priority firm rate. The IP rate is tied to the PF rate with the addition of an "industrial margin," and other adjustments. In addition, BPA is working with these customers on measures that include bringing low-cost power to BPA, adjusting the shape of deliveries, risk-sharing pricing, adjusting the volume of sales and interruption provisions.

Many rural public utilities urged BPA to continue the low-density discount without the proposed changes. BPA was persuaded by these arguments, and intends to continue the discount with only minor modifications. BPA expects to keep the overall cost to its current level. BPA will retain the kilowatts-to-investment ratio used to compute the discount.

Likewise, the BPA Power Business Line will, for the delivery of federal power, retain its current payment policies for general transfer agreements (GTA). BPA's Transmission Business Line is expected to make a proposal soon regarding GTA service for delivery of non-federal power.

LEADERSHIP IN CONSERVATION AND RENEWABLE RESOURCES

BPA intends to take a renewed leadership role in energy efficiency, renewable resources and new distributed energy technologies. BPA believes that the region will realize substantial value through lower energy costs, less pollution emissions, less investment in transmission and distribution infrastructure, better customer service, and higher reliability by taking advantage of these technologies. This becomes especially important when the region is not in a power

surplus, and new generation resources are being developed.

BPA plans to act as a regional catalyst for capturing this value primarily through market mechanisms, and without returning to BPA's historic check-writing role. The conservation and renewable discount proposal is one means of accomplishing this goal. Other steps BPA is taking in this direction include:

- ◆ Continuing to develop additional renewable resources, within the expenditure cap recommended by the BPA Cost Review;
- ◆ An aggressive effort to create and market "green" power products from BPA's system and the new renewable resources;
- ◆ Working with the Bonneville Environmental Foundation;
- ◆ Continuing the market transformation effort BPA is currently funding; and
- ◆ Continuing the significant "legacy" conservation programs.

FOSTERING A GREEN NORTHWEST

In fulfilling its vision for the near future, BPA is working with the region to develop a "green" Northwest energy system. In addition to conservation and renewables, the green strategy also embraces achieving an effective fish and wildlife plan and exploring new environmentally friendly technologies such as distributed generation.

As evidence of this initiative, BPA is working closely with the new Bonneville Environmental Foundation launched earlier this year to help market environmentally preferred power. Another key element in BPA's "green" initiative is addressed in the subscription strategy, where BPA is including a conservation and renewables resource rate discount program to promote utility investments in conservation and renewable resources. The objectives for this program discount are as follows:

- ◆ Support the Comprehensive Review's recommendation of dedicating "3 percent of the revenues from the sale of electricity services" to cost-effective conservation, renewable resource development and low-income weatherization in the Pacific Northwest;
- ◆ Continue BPA's role as a catalyst in furthering the region's public purposes goals;
- ◆ Support state legislatures and regional power planning organizations as they establish direction for the region's development of conservation and renewable resources;
- ◆ Produce real, measurable efficiency gains and renewable energy supplies; and
- ◆ Support and maintain BPA's competitive rate position in the power market.

BPA believes that this program, along with its other green power initiatives, will preserve the Pacific Northwest's conservation and renewable resource leadership role.

BPA intends to consult extensively with regional interests to find other opportunities to create environmental value and customer value through these technologies.

The conservation and renewable rate discount is proposed to be \$30 million initially for BPA customers that voluntarily choose to implement a wide range of energy conservation and renewable resource measures. As part of the dividend mechanism mentioned above, the discount could be substantially larger when BPA's net revenues are high. BPA plans to rely on a regional forum to develop clear direction about what would qualify for the discount. It is very important to BPA that the discount applies to *new* investments and not be used for existing conservation or renewable resources. The discount will be developed in BPA's upcoming power rate case. (See box on page 6, *Fostering a Green Northwest*)

SETTING CONTRACT TERMS TO OFFER CHOICES

The proposal for option fees, coupled with the proposal's tiered rates for some public utility load, raised concerns among preference customers. The agency therefore looked for and found other mechanisms to meet the goals of these mechanisms.

In its final strategy, BPA dropped payment of option fees that assured the lowest, cost-based rate in future rate periods. Rather, the length of a lowest-rate guarantee to a BPA customer will be the length of its contract commitment. BPA has the right to design different rates in subsequent rate periods. BPA is also agreeing to absorb the first 250 average kilowatts of a full-service customer's load loss resulting from future retail access rules.

BPA will offer several options to utilities should they lose retail customers when and if some form of retail access rules are adopted. Options include the so-called "walled-off load" option, conversion of sales to excess federal power and asking BPA to re-market excess power.

When it comes to doing individual, bilateral contract negotiations, BPA is staying with its proposal. It will, however, set several standard contract provisions through a public process. The current plan is to draft three standard provisions and allow a comment period. They include provisions for cost recovery, dispute resolution and uncontrollable forces.

NEGOTIATING AND SIGNING CONTRACTS FOR THE 21ST CENTURY

Policies adopted in the final Power Subscription Strategy will guide BPA's initial rate proposal for the 2002 to 2006 period. That process is under way with the scheduling of several pre-rate case workshops. BPA hopes to file its initial rate proposal in April of 1999. In the meantime, some utilities and direct service industries may want to begin contract negotiations so contracts will be ready to sign once rates are known.

The endpoint of subscription – executing contracts that carry commitments of the strategy and power rate case – will be about four months after the end of the rate case, tentatively expected to be about October. Some utilities will want to sign contracts for the lowest, cost-based power without waiting to see final rates, and the agency will accommodate those purchasers. Those utilities and direct service industries that want to wait for the final rates before signing will also be accommodated. BPA is presuming, however, that such contracts will be negotiated and waiting only for final rate information.

Subscription to inexpensive federal power has been, and will continue to be, a complex process. This is a natural result of the need to balance multiple interests and provide equity among a diverse group of customer classes and, at the same time, use the federal power resource to the best advantage for the region as a whole. BPA deeply appreciates the willingness of all interests to help with this process, and pledges to do its best to ensure that the resource is used wisely for the benefit of everyone in the Pacific Northwest.

THE POWER RATE CASE

BPA and its customers and constituents talk a great deal about “the rate case” or “the power rate case” or simply “the 7(i) case.” They are all the same thing. All those terms refer to the quasi-judicial proceeding required by the Northwest Power Act’s Section 7(i) which governs the process of BPA’s rate setting.

This year, for the first time, the *power rate case* is differentiated from the *transmission rate case*, which will follow. BPA, like many other large electric utilities in the country, is separating its transmission function from its power function. This is to comply with the National Energy Policy Act of 1992 and the subsequent Federal Energy Regulatory Commission regulations. Power and transmission rates will be set in separate processes from now on.

The Power Subscription Strategy creates direction and program decisions that BPA will then use as part of the basis for its power rate proposal. An actual proposal on pricing power and service products will be made in the rate case, as well as setting the actual level of planned net revenues for risk, the cost recovery adjustment clause and more.

BPA hopes to begin the power rate case by April 1999 and finish by October 1999.

NEED MORE INFORMATION?

In addition to this publication, the following publications related to subscription are available on the Internet by going to BPA’s subscription Web site: <http://www.bpa.gov/power/subscription>.

To order paper copies call BPA’s Public Information Center at 1-800-622-4519.

- ◆ Power Subscription Strategy, Dec. 1998, 24 pgs. (DOE/BP-3125)
- ◆ BPA Power Products Catalog, Dec. 1998, 42 pgs. (DOE/BP-3130)
- ◆ National Environmental Policy Act Administrator’s Record of Decision, Power Subscription Strategy, Dec. 1998, approx. 25 pgs.
- ◆ Power Subscription Strategy Administrator’s Record of Decision, Dec. 1998, approx. 175 pgs. (DOE/BP-3129)
- ◆ Fish and Wildlife Funding Principles, Sept. 1998, 4 pgs.
- ◆ How BPA’s Subscription Strategy Implements the Fish and Wildlife Funding Principles, Dec. 1998, 4 pages (DOE/BP-3124)

- ◆ BPA Targets More Cost Savings, Close-out on Cost Review Recommendations, Oct. 1998, 4 pgs. (DOE/BP-3111)
- ◆ Cost Management Implementation Plan, Oct. 1998, 18 pgs. (DOE/BP-3107)
- ◆ The Region Speaks, Summing Up Issues ‘98, Oct. 1998, 6 pgs. (DOE/BP-3110)
- ◆ Issues ‘98 Comment Analysis, Sept. 1998, 49 pgs. (DOE/BP-3108)

If you have questions about the Power Subscription Strategy, please contact your BPA account executive or call the nearest BPA office listed below:

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