REGIONAL DIALOGUE TECHNICAL WORKSHOP NOTES
Benefits for Residential and Small Farm Customers of IOUs
Wednesday, February 5, 2003
BPA Rates Hearing Room, Portland, OR

1. Purpose of Today's Meeting.

Fred Rettenmund (BPA) welcomed everyone to today's meeting, and led a round of introductions and a review of today's agenda.

2. IOU Options.

Our goal at this meeting is to enter into a dialogue about what BPA needs to do, as well as what we would like to do, said John Saven. We agree with the statement Bonneville made at last week's meeting, that the customers should share in BPA's benefits and risks, he said. We think the goals you laid out last time are reasonable, and that your proposal should be fashioned with those goals in mind. The joint customers also believe that the settlement should be grounded in a numerical analysis of residential exchange program obligations, that the settlement should make Bonneville competitive under a range of market conditions, and that the residential customer benefits should be calculable based on external information, not established in a BPA rate case, Saven said. We believe that the joint customer proposal (JCP) did that, he added.

We want this discussion to be as engaging as possible, Saven said; hopefully, at the end of the day, you'll have a better understanding of what we were trying to achieve and why, he said; that's how we would like to use this time, rather than delving into the details of one approach vs. another.

Having listened to the different alternatives you presented at last week's meeting, said Mike Morgan (PGE), I certainly have sympathy for what Bonneville is going through. It's been a struggle to figure out what you want to accomplish and how to accomplish it, as well as how to keep volatility under control, Morgan said; we've already traveled down that road, and would like to give you the benefit of what we've learned. We've been there, and while that doesn't mean we have all of the answers, it does mean we understand what you're going through.

One thing I wanted to talk about is the possibility of an RL sale, in place of the residential exchange program over the long haul, Morgan said. One problem with that approach is that it would put Bonneville back in the power market on a regular basis; as you're aware, one of the joint customers' objectives is to reduce BPA's market presence. We think if you're back in the market long-term, your own competitiveness is at risk, because that will introduce additional volatility to the marketplace, he said.

Also, said Morgan, if you're looking for parity, with various customer groups receiving a share of benefits they're comfortable with over time, you need an RL rate that is comparable to your PF rate. Frankly, however, many of our preference customers would find that unacceptable, Morgan said -- it simply wouldn't look like what the system was intended to do, to them. Also, because that would be a power sale, you would be bumping into a 7(b)(2) situation, he added. Various other meeting participants expressed agreement with Morgan's comments.

One thing we could achieve in arranging a long-term solution is to make sure Bonneville plans whatever purchases it needs as far in advance as possible, said another participant. Are you saying it would have been prudent for BPA to have gone out in mid-2001 to purchase all of the power it needed? another participant asked. No, not at all, the first participant replied – what I'm saying is that if BPA had made arrangements to purchase the power it needed in 2001 five years before that, it wouldn't have been forced into some of the higher-priced purchases it had to make in 2001.

Marcus Wood (Pacificorp) said he had been asked to address the concept of a radically altered residential exchange. He noted that the joint customers are interested not just in a settlement, but in an enduring settlement. If that's going to happen, the agreement has to be in accord with the needs of all parties, and it has to be fair and equitable to everyone – not just the residential and small farm customers of the investor-owned utilities. For the following reasons, he said, we feel a radically revised residential exchange program is unlikely to meet those criteria. First, by giving Bonneville, via the in lieu provision, the option to choose whether to go with the market or with the residential exchange, you would be creating the same kind of risk you would face if Bonneville was to go back into the power purchasing market in a big way. Second, once you get into a power exchange, you run into 7(b)(2) problems. It has been suggested that we use a "cookbook" approach to simplify the residential exchange, and we could try that, but there are problems in that as well, he said – for one thing, without detailed analysis, somebody is going to get gored. Finally, and very important, is the basic effect of the in-lieu options as described on the equitable allocation of benefits, he said. One of the reasons we're sitting around this table is that BPA is in an untenable position – unless BPA can achieve a long-term agreement, customers will be free to choose the BPA resource if it is cheaper than the market, or the market if it is cheaper than Bonneville. What in-lieu does is impose precisely the same set of problems on the customers that Bonneville is trying to avoid, he said.

I like to think we've learned something in the last 20 years, said Marc Hellman (OR PUC); the idea behind the residential exchange program is to equitably share the benefits of the federal system, and I'm not sure this proposal does that.

Next, Terry Mundorf (WPAG) provided the joint customers' response to the financial approach described by Bonneville at the least meeting of this group. We believe the financial approach alternative offers the most opportunity to achieve the broadest range of policy goals without overtly breaking the law, Mundorf said. It is our joint belief that the proposal we made has a financial mechanism that achieves the bulk of the goals Bonneville has laid out, and would be permitted under the law, he said; we look forward to discussing which areas could be enhanced or rectified. There would be two necessary prerequisites to such a discussion, he said – first, that any analyses done by either side need to be transparent. The second is more policy-oriented, he said, highlighted by the pie charts distributed at the last meeting: you can have one of two objectives, but you probably can't both stabilize the percentage of the benefits distributed to the various customer classes over an array of market conditions, and stabilize the rates they're going to pay, said Mundorf. You can do one or the other, he said, but it's unlikely that you can do both. In our proposal, we have deliberately chosen to sacrifice the former – stable allocations – in favor of the latter – stable rates, Mundorf said. A second prerequisite will be for the customers to determine whether they share the policy goal of stabilizing the distribution of benefits from the federal system, he said. We need more clarity on the hierarchy of Bonneville's objectives, said Mundorf.

That's an excellent observation, replied Larry Kitchen (BPA) -- having some further discussion of where that balance lies could be fruitful, from a policy standpoint. When BPA staff saw the proposed settlement of the 2002 rate case, they wondered what had happened to the rate stability concept, he added.

We need to look at the concept of which other parts of this are important to you, including the level of the rate in comparison to other factors, said Rettenmund – obviously stable rates are important, but there are other considerations as well. I wouldn't completely disagree, but there is a prioritization issue as well, Mundorf replied – we need to ask ourselves what values we're trying to satisfy in our distribution of benefits. The influence of that distribution on rates is what gets us into trouble, frequently, he said. In our approach to this issue, we tried to lay out the sequence of questions – we felt that was the most orderly way to arrive at a satisfactory conclusion.

It seems to me that the distribution of benefits is always a one-sided equation on Bonneville's part, said another participant. In cases where BPA feels its residential and small farm customers are getting too large a share of the benefits of the federal system, BPA doesn't hesitate to change its policies to reduce that share. However, they never change those policies to increase the residential and small farm customers' share of those benefits when that share has been too low. Other customers expressed disagreement with this statement. Litchfield observed that a more intensive workshop, where everyone brings their calculator, is the only way to really reach resolution on this issue.

Kitchen noted that one concern Bonneville staff has is that they can envision certain scenarios, under the JCP proposal, in which rates would not be stable. Mundorf replied that if there are areas of the proposal that need further discussion, that is one of the purposes of today's meeting.

I don't disagree with what Terry said about the importance of achieving rate stability, said Kevin O'Meara (PPC), but I am concerned about the way Bonneville has defined "benefit" for the purpose of its calculations. The fact of the matter is, most utilities have their own resource base, and I don't think those resources should be ignored. Under 5(b), utilities are expected to use their own resources, some of which are below Bonneville's price, and others of which are more expensive, he said. The benefit that was intended to be conveyed to electric consumers through this program is access to equivalently-priced power; measuring how much power in aggregate a customer class can purchase and assessing how that compares to market doesn't really capture that very well. In the case of the customer class I'm most concerned about, said O'Meara, the DSIs would receive benefits only under the high-market scenarios. Somehow, you need to look at the concept of benefits more broadly than is indicated in these pie charts, he said.

We feel that the best opportunity for meeting Bonneville's goals is through a revised residential exchange program, said another participant, and we recommend having another workshop to explore that option further. The other point I would like to make is that, in terms of the in-lieu, and the risk it imposes on the IOUs, Bonneville is asking its customers to accept a certain level of risk. There may be times when Bonneville's rates are above market prices, he said; if the publics are paying more than market, at the same time, the IOUs should be contributing to the solution to that problem – that will help bring about comparable wholesale rates for the publics and IOUs as laid out in the statutes.

With all due respect, that is utterly fallacious, Linc Wolverton (ICNU) replied – if there was no in-lieu, by getting the difference between our average system cost and the Bonneville price, the cost of our power would be the same as the cost of Bonneville power charged to other customers. It is easy to demonstrate mathematically the effect of in-lieu during times when market prices are lower than Bonneville's price, he said – this would force our costs to be not only higher than market and higher than what Bonneville would be charging its other customers, but higher than the cost of our own resources as well. Some might consider that equitable, he said, but we do not.

It sounds to me as if you're talking about the deemer clause, Kitchen observed. That's correct, Wolverton replied.

That is essentially what we wanted to convey today, said Saven -- an answer to the question of what are we trying to do, and why are we trying to do it. I think we've raised reasonable issues for discussion, he said; we need further discussion about some of those issues, such as floors and caps for five years vs. floors and caps for the long term, benefit levels and how they are chosen. Those are things I would want to pursue if I was in your shoes, he said, but that's the next stage, after you fully understand our proposal. To the extent we can talk about whether or not our approach makes sense, what issues remain, and what further data and information we need to exchange with each other to make an informed decision, that's what we need to do next, Saven said.

Paul Murphy (Golden NW) made the point earlier that we shouldn't be looking only at the equal sharing of the existing market and its costs, because there are embedded resources, said Wolverton. I don't think the joint customers would disagree with that statement; in fact, the way the calculation worked was to put back in a number of CTs based on a forward projection. We took into account system resources and reasonable payments to equalize the bottom-line cost of power. That's why the "turbines" are 3,300 megawatts, not the size of the load; it's why the capital cost of the turbine is set lower than any of us believe you could build a turbine today, because we backed into a number that comes as close as we can get to achieving the outcome we all want.

I recognize that there has been a carefully crafted solution or settlement over the past 18 months, said Wolverton. Unfortunately, if you look at the numbers, that settlement is a very rich one for the IOUs, he said. If we're going to move forward, we need to revise the residential exchange program -- we need to start with the notion that we need to revisit the principles of the residential exchange, he said, and if something comes out of that process in terms of a settlement, then that's a possibility. Otherwise, he said, we have some serious problems with the current settlement. One other issue having to do with this compromise is whether people are really signing on for 20 years, or just through 2011, he added.

If there is one thing I've observed in recent years, it is the tension between residential loads and our large industrial loads, Kitchen said. There are some real questions about how to strike that balance in the future; given the fact that even white-collar jobs are now being shipped overseas, and we do have to think about what the job base is here in the Northwest.

There are some embedded lower-cost resources your industrial customers see, said Jack Speer (Alcoa). Also, one thing that struck me earlier was a comment about the equitable distribution of BPA benefits. The idea, to me, was to give access to those benefits at the wholesale power level to equalize those rates. It's an abomination to discover that residential consumers in Snohomish County are paying higher BPA rates so customers in Spokane can enjoy lower rates. We're not disputing that the current system isn't perfect, Scott Brattebo (PacifiCorp) replied – that's why we're proposing a new contract structure.

That's an interesting point, said Mundorf -- let me give you a perspective about why the settlement ended up where it did. We spent a year trying to make the residential exchange program work; we failed. But what I think we did eventually was to come around to BPA's view of the world, for better or for worse – that the exchange, as we have historically known it, did not provide a politically defensible distribution of the benefits of the federal system. In walking down the path we chose, after concluding that we couldn't do any better, we limited our choices to a power exchange or a financial exchange, Mundorf said. BPA felt that they needed to broaden the residential exchange. The bottom line is that while I am mortified at the mechanism they chose to achieve that goal, I'm not sure I disagree with the goal itself, said Mundorf – it all comes back to the question of what we're trying to achieve through this program.

The discussion of the "in-lieu" issue continued for some minutes. Ultimately, Kitchen said that, even if BPA adopts the JCP as written, it wouldn't be possible to escape the in-lieu issue, because customers would have the option of staying with their Subscription contracts and requesting a residential exchange contract. Not as long as you put the exchange trigger on the PF rate, Mundorf replied. Kitchen noted that a number of public agencies have higher average system costs than they had in 1999 as a result of 2000-2001. One of the things we're going to have to address before the rate case is the in-lieu issue, Kitchen said.

We've looked at that contract, and the math doesn't work, Mundorf said. But under the JCP, we would still have to offer residential exchange contracts, Kitchen replied -- this is a pivotal issue in the decision-making for many customers trying to decide whether to sign onto the JCP or stay with their subscription contracts. In my view, this is on the list, but it's not in the top 10 issues that have to be resolved in the next four weeks, Mundorf said. Probably the most difficult thing to resolve is going to be 7(b)(2) another participant observed.

One way to approach this problem, said Wolverton, is to say that the statute requires X, and argue from that basis. On the other hand, within the limits of BPA's discretion, we can attempt to arrive at a solution that is equitable and will hold up over the long term. While it may be amusing to discuss the intricacies of 7(b)(2), that's not going to help us arrive at that goal.

With respect to where we go from here, in my view, Bonneville needs to develop a proposal, said Mundorf. I would suggest that we schedule an in-depth discussion of our proposal, and another similarly detailed discussion of ASC. I would do that between now and the time you develop that proposal, to give us the maximum opportunity to influence your thinking, Mundorf said. I think that's a constructive proposal, Kitchen replied. To the extent that BPA is willing to talk through the details before it develops its proposal, that would be infinitely preferable to simply waiting for BPA to develop its proposal, and responding to it, said Saven. I agree, said Rettenmund – it doesn't make much sense for us to try to develop a proposal on this topic without discussing this issue further.

In response to another question, Kitchen said what he is struggling with right now, with respect to the JCP in general, is BPA's broad direction – there are certain scenarios in which the outcome of its provisions would not be acceptable. So you're still at the track choice stage of your analysis, rather than the details of the proposal? Mundorf asked. That's correct, Kitchen replied.

I'm surprised to hear that, said another participant – are you saying BPA wants to have to go to the marketplace to buy a significant amount of power? I'm saying that Steve Wright's number one concern is BPA's financial situation, Kitchen replied – whatever we choose to do over the long term, we need to solve that short-term situation first, and we need to be sure the JCP meets that need.

Maybe one way to deal with this is not to develop track choices, but instead to agree that we need a residential exchange program, Litchfield said. Let's look at your analysis of the JCP, he said, and talk about the areas where Bonneville sees potential problems.

Kitchen thanked today's participants for a very constructive discussion and input. Let us go back and review today's input, said Rettenmund, and we will get back to you with a solid series of next steps, including a next meeting date. With that, the workshop was adjourned.

Meeting summary prepared by Jeff Kuechle, BPA contractor.