Other Integrated Program Review 2 Follow Ups

March 2015

FINANCIAL DISCLOSURE

This information has been made publically available by BPA on March 10, 2015 and contains information not reported in BPA financial statements.

Rates Questions

1. **How realistic is the rough projection of a 6-8% rate increase from BP-16 to BP-18 and can you provide more details behind the increase?**

   "Please provide a breakdown of the forecasted 6 to 8 percent rate increase, listing the drivers for that increase, and the total dollar amount and percentage increase each driver contributes to that increase."

   Response:
   The intent behind BPA's presentation was to provide some context about potential future rate pressure in light of a phased in approach to expensing conservation. However, it is difficult to provide this context so far in advance of a rate case. Recall that we started the 2014 IPR with an 11% increase based on un-refreshed information for IPR costs. This rough BP-18 estimate is being produced over a year and a half before the initial proposal for BP-18 and will undoubtedly change. That said, this estimate may provide some information to help customers consider a change to expensing conservation because such a transition to expense yields upward pressure on rates.

   To put this estimate in context, more than half of the projected increase is associated with costs that will be decided through the 2016 Integrated Program Review. If recent history is a guide, the internal and external vetting associated with past IPR processes could result in reductions. The remainder of the increase is driven by capital-related costs and by costs that are determined in the rate case.

   Table 1. Annual Average Increase in IPR Costs* Compared to the Previous Rate Case ($ in millions)

	Years	IPR Kickoff	Final IPR	Change	Effect on Rates^
2010 IPR	FY'12-13	$155[1]	$105[2]	$(50)	(2.5) %
2012 IPR	FY'14-15	$117[3]	$80[4]	$(37)	(2) %
2014 IPR	FY'16-17	$66-76[5]	$12	$(54-64)	(2.5)-(3) %

* Includes CGS, Fed Hydro, Renewables, EE, Non-Generation Operations, Fish & Wildlife, Northwest Power Conservation Council, and Internal Support.
^ Uses rule of thumb that $20M is equal to a 1% change in rates
Note: There was also a drop of more than $60M in IPR costs between the IPR and IPR2 for FY'10-11.[6]

***Unlikely to Change: Settlements and Legal Agreements* (~2.5% Increase)**

There are only a few major elements of the rate projection that have a high degree of certainty due to legal agreements and or contracts that include funding levels exchange, fish and wildlife, revenue credits, and SE Idaho load service expenses).

[1] 2010 IPR Final Close-Out Letter. (10/27/10) Page 15.
http://www.bpa.gov/Finance/FinancialPublicProcesses/IPR/2010IPRDocuments/Final%202010%20IPR%20Close%20Out%20Letter%20and%20Report.pdf
[2] Ibid.
[3] Building the Frameworks for the Integrated Program Review. (1/31/12) Slide 16.
http://www.bpa.gov/Finance/FinancialPublicProcesses/IPR/2012%20IPR%20Meeting%20Materials/ipr-general-manager-meeting-013112.pdf
[4] 2012 Integrated Program Review: Final Close-Out Report. (10/12) Page 11.
http://www.bpa.gov/Finance/FinancialPublicProcesses/IPR/2012%20IPR%20Documents/2012%20IPR%20FINAL%20LETTER%20AND%20CLOSE%20OUT%20REPORT.pdf
[5] Building the Frameworks for the Integrated Program Review. (1/08/14) Page 14.
http://www.bpa.gov/Finance/FinancialPublicProcesses/IPR/2014IPRDocuments/Building%20the%20Framework%20for%20the%20IPR%201.8.2014.pdf
[6] BPA. IPR2 FY2010-11 Power and Transmission Program Levels. (4/24/2009) Page 5.
http://www.bpa.gov/Finance/FinancialPublicProcesses/IPR/2009IPRDocuments/Draft%202010%20and%202011%20report%20final%20final%20report.pdf

Somewhat Likely to Change: Capital-Related Costs (~1% Increase)

Based on current borrowing plans and interest forecasts, capital-related costs (depreciation, amortization, and interest expenses) are projected to increase about $18 million[6] from BP-16.

Likely to Change: Other IPR Program Decisions (~3.5% Increase)

To develop this rough estimate, BPA developed a preliminary forecast of IPR costs based on the best available information. For example, BPA used 2014 long-range plans for the Columbia Generating Station, Corps of Engineers and Bureau of Reclamation. These plans are likely to change.

Likely to Change: Rate Case and other Study-Based Costs (~0%)

The remaining costs are largely based on current price and inventory models that will be updated in the next rate case including Transmission Acquisition and Ancillary Services, Secondary Revenues and other costs.

2. **"At the March 10, 2014 workshop, BPA distributed a handout entitled "CIR Workshop: Investment Portfolio Optimization." On page 9 of that handout, BPA indicated that the preliminary forecast for the power rate change for BP-18 was a rate change of -0.1%. Please indicate the changes in assumptions that caused BPA to go from a -0.1% forecasted rate change for BP-18 a year ago to the 6-8% rate increase forecasted in the IPR-2 handout." The Rate change information released in the CIR process included the following significant variances:**

Response:

There are two major issues to keep in mind when considering the different forecasts. The first issue is we need to look at each analysis across time. Each is a comparison of BP-18 rates compared to the BP-16 forecast. The CIR presentation showed a BP-16 rate increase of 10.4%. BP-18 results are essentially flat when compared to that result. The IPR2 forecast has a much different starting point than the CIR. Now the BP-16 rate increase is just 7.2%. If the costs for BP-18 remained the same, updating the BP-16 rate forecast would result in a 3% rate increase for BP-18. The second issue is that all of the data used in the rate forecasts has been updated since the CIR affordability cap was created. The CIR analysis was based on cost data from the 2012 IPR. The IPR2 data started with 2014 IPR costs with internally-developed adjustments. Power prices, loads, and net secondary sales forecasts are also different. All of the differences in cost and revenue elements account for the remaining difference.

Budget Questions

3. **"On page 17, BPA states that after reviewing spending levels in FY 2016-17 that "known changes yielded minimal reductions to programs". What would the power side of BPA have to do to reduce spending levels enough to reduce the power rate increase by 1% (i.e., a decrease in spending of approximately $20 million)." Same question but for a reduction of 3% ($60M) and a reduction sufficient to eliminate the power rate increase ($96M).**

Response:
Through the IPR, BPA undertook a thorough review of its program and internal costs. This review resulted in proposed program and internal expenses for Power that increased less than the rate of inflation and are virtually flat once the undistributed reductions are factored in. While BPA feels that these funding levels are sound, BPA is open to taking additional actions to mitigate the rate increase associated with moving the EE capital program to expense. To that end, BPA is continuing to look at ways to cut costs or take on additional risk.

Fully mitigating the rate impact will be challenging as about 70% of the costs in Power rates are fixed or modeled costs that include capital-related costs, settlements, power purchases, and regulatory requirement costs such as the Fish & Wildlife Program and Energy Efficiency. The remaining 30% of costs in Power rates are programs that would be partially or fully cut to mitigate the rate impact of a shift to expense.

While we cannot yet say exactly what we would have to cut to mitigate the rate impact, a high level understanding of the impacts can be found by examining the "Risks and Impacts of Operating at Below Proposed Levels" sections of each program summary in the IPR Initial Publication.

a. A 1% ($20 million per year) reduction to Power rates would require some combination of staffing reductions, maintenance deferrals, and/or possibly cancelation of some O&M projects. These actions could result in shortened asset lives and therefore incurring replacement costs sooner. Reductions may also limit Bonneville's ability to respond to unforeseen external cost pressures. Additionally, upward cost pressures would be added in future years.
b. A 3% ($60 million per year) reduction in rates related to program spending would have more severe effects than those described in 6a above. Some projects would need to be canceled as opposed to just being deferred. Approximately $60 million in reductions would require cuts to service levels and their associated benefits.
c. Reductions sufficient to eliminate the Power rate increase (about $96 million per year) would result in even more severe outcomes than those described in response to question 6b. It is likely that programs would be canceled or delayed and for a longer period of time. For a sense of scale, $96 million is more than Power Non-Generation Operations (Power's internal operating costs), is one third of Corps of Engineers and Bureau of Reclamation O&M costs, or more than one third of Columbia Generating Station costs. Reductions of this magnitude would likely result in losses to generation reliability and performance and may jeopardize accomplishing BPA's mission.