Building the Framework for the Integrated Program Review

Informal Meeting Notes (for external distribution)

BPA Rates Hearing Room, 10:00 a.m. – 5:00 p.m., Tuesday, January 31, 2012

BPA Administrator Steve Wright opened the session at 10:15 a.m. The Rates Hearing Room was essentially standing room only, with about a hundred attendees in the room and many others participating via the conference telephone.

Disclaimer: **These are informal, unofficial meeting notes. They are intended principally to capture remarks made by external parties, in paraphrase form. This is not a verbatim transcript.**

Participants represented BPA power and transmission customers, consultants, constituent interest groups, state energy departments, public utility commissions, and the like. Also present were a limited number of BPA executives, managers, and senior staff.

Owing to the size of the audience, Wright dispensed with introductions. He thanked participants for attending today's session, described as a kickoff to the upcoming Integrated Program Review (IPR), a prelude to developing BPA's Fiscal Year 2014-2015 rates.

Wright said the meeting was a response to an earlier IPR effort's "lessons learned." A key outcome of that process was the suggestion that BPA should host a meeting early in the next IPR process, before the internal budgeting process has commenced, as a way to give folks insights into where we may be going.

He said there has been no internal scrub on the numbers that will be presented today; they came directly out of the FY 2012-2013 IPR. One exception, he noted, was that the secondary revenue figures have been updated to reflect lower gas prices.

We also want to discuss access to capital issues, he said, but with a focus on budget levels. He introduced "emeritus BPA economist" **Mark Roberts**, recently retired after 36 years of service, for his presentation on "Economic Outlook for the Pacific Northwest; or If this is recovery, why don't we feel better?" (This and other meeting documents are available online at www.bpa.gov/corporate/Finance.)

Economic outlook presentation: Roberts

Roberts gave his overview of the "Great Recession," a crisis he characterized as particularly deep and long. The good news is, things are looking up, but the bad news is that things are still at a low. The Euro-Crisis is the single biggest risk to the world economy—will it be a controlled recovery? Globalization is with us: what happens to countries abroad affects us here.

He explained the several principal drivers behind the economy. The outlook is for slow growth, he said, with substantial unemployment and continued movement toward a service economy, which tends to have a built-in wage disparity.

At the conclusion of Roberts' presentation, **Scott Corwin** of the Public Power Council (PPC) quipped that the presentation depressed him. He asked Roberts whether he had looked at electricity trends, to which Roberts responded that he had not, adding that a quick analysis would reveal that service industries tend to be less energy intensive.

Dwight Langer of Northern Wasco County PUD asked about the federal deficit and the degree to which it impacts trends for the nation.

Roberts said that the bulk of the profession sees most near-term issues (e.g., unemployment) being urgent. The deficit is important; it is not sustainable. We need to do more to get the current economy growing, he said. Today's austerity programs are an underlying cause of the poor economy. We need near and long-term resolutions.

Bob Hammond of the City of Richland asked, re: Slide 11, whether there was something to be read into the last three or four curves indicating a steep (slow) recovery.

Roberts said his takeaway is that the economy is demonstrating less speed in the recovery compared to the fifties. Today's rate of recovery is related to an increasingly settled workforce, where families have two wage earners, meaning reduced labor mobility.

Charles Pace, a consultant, commented by phone on Slide 18, regarding Greece-Ireland vs. Germany, that some think it represents a "mispricing" of risk. He asked whether the recent fiscal pact by 25 members of the EU (European Union) to impose additional discipline and provide a firewall would be sufficient to mitigate risks.

Roberts said there might be a basic mispricing of government bonds. The economic union is beginning to appreciate the peril of having common monetary policies with different fiscal and cultural qualities of the constituent countries. There is a sorting-out of factors, he said, and a large discovery process is taking place.

As to Pace's question about what the ultimate solution to the Euro-Zone may be, Roberts said it may require a high firewall. So far, the market has not been impressed with what they have seen. Markets will continue to test the firewall. They need to see greater commitments and serious changes in the structural qualities of these countries. When one thinks about Greece, etc., how they do the harder work of changing how their economics function is where the real solution will come from. But to compel changes is very difficult.

Rachel Shimshak of the Renewable Northwest Project asked whether there is a group of "contrarians" out there who may think differently about the situation than what Roberts has described as being the mainstream view.

Roberts said that there are contrary views—but they are even less optimistic. How to get the product flows and currencies to change will require significant changes in how we and the Chinese think of economies. They are experiencing social difficulties, strikes, and poor working conditions. Contrarians will say things will get significantly worse. Other experts think the U.S. is on the brink of an industrial renaissance—that there is the potential for things to come out better, much sooner. But right now, the Chinese economy is tending to slow down.

GM economic panel presentations

After a short break, **BPA Deputy Administrator Bill Drummond** introduced the featured seven-member panel of utility general managers. He said that after the last IPR, we learned about a desire to describe what was going on in the local economies. He said the panel had been asked to address the matter.

The first panelist was **Heber Carpenter** of Raft River Rural Electric Cooperative (Malta, Idaho). He referred back to one of Roberts' slides depicting state economies. Carpenter said that Idaho has many of the problems that plague all of the Northwest. He pointed out that the statistics show Idaho's non-metropolitan annual income to be $29,000, compared to Washington's $41,000. Idaho, he said, falls under the poverty line for 16 percent of rural people.

Things are tough, Carpenter observed. The governor just talked about Idaho having a small surplus; it comes from rural agriculturally based economies. Farm incomes are up about 20 percent, but small businesses are still struggling if they are not attached to the ag sector. What concerns us as a utility, Carpenter said, is that many ag operations in our area are deep well operations that use electricity, which constitutes about 30 percent of their costs. If we see electricity having large wholesale increases that we have to pass on, that could stall out one of the bright spots we see in our area.

Bob Hammond of the City of Richland (Washington) said that in his role, he works for the city. Richland's story, he said, is a little different in that his area has had steady growth through the recession. The city is projecting heavy non-residential load growth in the next two years. We are into serving Tier 2 load, he said, and the city has not changed its retail rates since 1994, having maintained their rate levels by spending cash reserves. Our rates are not aligned at all with the Tiered Rate Methodology (TRM), he said. We are not sending any price signals to retail customers, and this is resulting in a gap.

Our community, Hammond said, depends on the Hanford industry, with about $2 billion a year coming in from the federal government related primarily to clean-up activities. These, he said, will sunset in 20 years. We are trying to replace our Hanford base with a robust high-tech economy.

We expect to qualify under the state's I-937 RPS (renewable portfolio standards) law requiring us to achieve a three-percent renewable resource target. Our efforts, he said, have been to capture our total utility costs and to allocate Tier 2 costs appropriately, in a way that also meets the customers' needs and helps replace jobs. Conservation programs need to become self-funding, with less reliance on BPA programs.

We need to identify and fund our own programs, he said, for system reliability, demand response, and renewable resources. What we need from BPA as a partner is consistent upfront information about BPA's business plans. For decisions we can influence, we would like access to BPA employees, to work with them early on in the process. We want access to major long-term BPA plans and policies. Current planning does little to help us with our long-term planning needs. We would like less BPA involvement in reaching our targets on our own.

We want to work on how BPA is prioritizing its programs, he said, and working with the Corps, Bureau, and other parties. We want to understand what BPA issues the city can influence and put planning resources on, vs. those decisions we cannot influence. We want to know the information, he said, so we can pass it onto the ratepayers.

He said BPA's account executives are very good. He wants to continue to be able to use "EE Central," and it needs to be fully ready for use. He said BPA should not waste time developing workarounds. BPA, he said, has lost credibility with Richland's policy makers and customers because of the funding gap, capital overspend, and other Energy Efficiency (EE) glitches. The TRM and Richland's normal regulatory challenges are difficult enough without adding issues we can avoid, like the EE problems.

Hammond said he appreciated today's meeting and the invitation to speak. He looks forward to working more closely with BPA in the future, working together to avoid mistakes in the future.

Steve Boorman of the City of Bonners Ferry (Idaho) used an analogy to describe the economic situation in his area. He said his old Chevy pickup is ready for an upgrade. If he had $30,000 in the bank, he could finance it, but he also has kids going to college. The Boorman family has a fixed income budget.

He compared the local timber and wheat farming industries. The former is experiencing 14 percent unemployment. Revenues for related businesses are flat or fixed, but expenses are rising—for example, the price of diesel and electricity.

Bonners Ferry's largest customers—a lumber mill and a wood products concern—are competing nationally. Boorman said electricity costs are impediments to these employers. Wages are flat. State workers have seen decreased income due to furloughs. Some businesses are in a survival mode.

We can control ongoing expenses, he said, but we have difficulty controlling capital expenses. Capital expenditures require careful planning, and we are paying careful attention to our capital investments.

At the end of the day, he said, the Boorman family will end up driving their old rig for a few more years. They are following the old adage, Watch the pennies and the dollars will take care of themselves.

Steve Klein of Snohomish County PUD (Everett, Washington) said his utility is BPA's single largest customer. Our utility is relatively young (1949), he said, compared to the private utilities that formed in the 1800s. His utility has served as a local economic engine. Snohomish's load has grown by leaps and bounds, and is now actually larger than Avista's. Of the local utilities, only Puget Sound Energy is larger than Snohomish.

We have not put our entire load growth on BPA, he said. We are pursuing resources, following the legacy of renewable hydro benefits. We have looked at wind, biomass, etc., to the point that now, eight percent of our resources comes from wind. The pressure of growing quickly has put rate pressure on our utility. This, combined with NERC and WECC rules and regulations, makes it a challenge to manage the utility. (NERC is the North American Electric Reliability Corporation; WECC, the Western Electricity Coordinating Council.)

As to the economics locally, we have lost Kimberly-Clark, our last large industry. The aerospace industry, on other hand, is going gangbusters (Boeing tanker production). But a segment of our society continues to suffer (Kimberly-Clark).

Our low-income program discount participation level has doubled and now makes up two percent of our revenue. Historically, utilities have done a good job withstanding BPA rate increases, but utilities are finding this more and more difficult to do. At a Rotary Club meeting, we were talking about the various cost impacts on us as a result of being BPA's largest customer.

The president, Klein said, appoints the BPA administrator, who tries to manage the federal asset for the Northwest. The administrator has a BiOp (biological opinion) that people are not necessarily working together on, yet he makes a decision to provide a billion more dollars for the BiOp. This means $110 million will come out of our community based on the administrator's decision. I support the decision, but we need to do more to educate the community about BPA's decisions—that there is a cost to them. If I cut tree trimming and there's a windstorm, people lose power. People say spend on salmon, but when the bill comes due, you want me to cut tree trimming.

The idea of withstanding a BPA rate increase does not work anymore, he said. The programs are going to have to stand more on their own. Have we done everything as a region to keep the impacts as low as possible? Folks who say we need to move into a tiered rates world may not know what they are asking for.

We have the highest penetration of electric vehicles, biomass, and solar distributed generation. A tiered rate design doesn't work for us because I have times where I am paying negative prices to keep these distributed generation systems going. Tiered rates is a blunt instrument.

"I am the future," Klein said, speaking figuratively as Snohomish, and with so much going on in real time in our system, we need to pay attention. Many things that society is doing are already happening on their own, he said; we do not need BPA to push or support such initiatives.

Jasen Bronec of Glacier Electric Cooperative (Cut Bank, Montana) said, referencing the numbers on Slide 3, that he has a different picture of the economy and unemployment in Western Montana. While Eastern Montana may have only three-percent unemployment, it is not so in Western Montana. Our customer base, he said, is residential and commercial. We have seen increased activity with oil, gas, and wind generation. Even though those are good activities in our area, they have done little to stimulate our local economy or bring in many jobs.

Cooperatives, he said, have their hands full, in the midst of regulator and governance issues. We have a governor who has his own ideas what to do about BPA assets.

Looking at unemployment rates in Western Montana, Lincoln County faces a 17-percent unemployment rate. As to counties within the BPA service territory, it is important they be recognized for their unique changes and economic hardships. To clarify some of the changes, Flathead County has a 14-percent unemployment rate; Granite, 13.5 percent; Glacier, 13.2 percent, and so on. Those numbers are a lot larger than what is reflected on a state level. Glacier County, in the 18-64 age bracket, has a high percentage below the poverty level.

Our ability for spendable income meeting the needs of putting a roof over our heads and paying for electricity is limited because we are economically disadvantaged. The local LIEAP office is being cut more than 50 percent. (LIEAP is the state's low-income energy assistance program.)

All Western Montana coops are being hit hard by the economic downturn. Most coops report new services at only ten percent of normal. The wood product industries are hit the most. We have seen a loss of 417 jobs—more if you consider related jobs.

We need BPA to have stable, predictable rates, he said. This is important to the end-user. Among BPA customers, this should be the primary concern. Third parties who are non-beneficiaries need to be more conscious of the impact of their funding requests. BPA needs to plan, scrutinize budgets, and hold departments accountable.

Larry LaBolle of Avista Corporation (Spokane, Washington) said that in contrast to his colleagues at the table, he is not a utility manager; he is the "IOU voice" on the panel.

Our tie to the costs of the federal system, he said, is not as close as yours. We have service areas in Medford, Spokane, Coeur d'Alene, etc., and so we see similarities in what moves up or down. Underneath what is a stable economy now (not necessarily good, but not declining), there has been quite a bit of churning among economic sectors. Federal, state, and local government employment is declining substantially in our service territories. Hospitality is a big driver, but it is stagnant and underperforming. Housing is at an idle and not contributing much.

On the brighter side, he said, manufacturing is picking up and expected to increase. Job growth in the private sector is outstripping the loss in the government sector. We are seeing some growth in information services and engineering. Education is up in terms of economic activity—sadly, in part because people lost their jobs and are going back to get trained in something else. All financial institutions are suffering fee increases. This has an impact on students and will curb growth.

The economy and Avista's customers get pinched, such that the size of the pie that families have to spend on goods and services is shrinking. The portion they are spending on energy is increasing in both absolute and proportional terms.

We are making dramatic investments in our system. Large information systems call for large power supplies, and this requires a big investment. Our T&D (transmission and distribution) investments are driving double-digit rate requests, resulting in seven-to-eight-percent rate increases. It is hard to see how that will change, and this is having a profound impact on customers and how they feel.

We have been communicating with customers what is going on, telling them about the future of energy costs and educating them. We are refocusing on customer service. It helps if customers feel there is some increase in value of the product. We have seen credit issues and collections increase. About 50,000-60,000 of our customers are at or below the federal poverty level. When a substantial component of our customer base is in this situation, rate increases have a profound impact.

LaBolle said he had recently talked to **Kris Mikkelsen** (general manager of Inland Power and Light Company, Spokane), and she mentioned similar highlights. Seventy percent of Inland's customers are residential. People are building few new homes. Reinforcement projects to increase feeder capacity have been put on hold pending a pick-up of loads. She has not seen the increase in credit collections that she had expected. Her sleuthing is founded on the fact that most of Inland's customers are rural and do not move much. It might be said somewhat tongue in cheek, it is easier for them to pay their electric bill than it is to pack up and move.

LaBolle asked how the IOUs could stay meaningfully engaged in the process of looking at federal costs and rates—doing so in a helpful way, one that helps with cost control. We are wrestling with that, he said, in that we are substantially disconnected from the PF price.

Dwight Langer of Northern Wasco County PUD (The Dalles, Oregon) said that this Thursday marks his fortieth anniversary of years in public power. While I find the current situation exciting professionally, he said, these are economically challenging times.

As to the economic picture for Oregon, unemployment stands at 8.9 percent, down from 10.6 percent a year ago. Yet, Oregon has the fourteenth highest unemployment in the U.S. If "Poverty" were a city in Oregon, it would be a city larger than Portland. Oregon has the highest percentage of use of food stamps in the country. We are tied with Hawaii, he said, for the highest income tax rate among the states.

Residential electricity rates "pre" the enactment of renewable standards, he said, were increasing a little over one percent annually. Post-RPS residential rates, by contrast, have increased 18 percent; industrial, 15 percent. It is worth noting that the full impact of the RPS will not be fully realized until 2020. The plan to replace Boardman with renewables, coupled with the governor's ten-year energy initiative trending away from gas generation, illustrates the increasing costs our customers are already facing into the future. The impact to our customers is significant.

Wasco County has the second highest property tax rate in the state. Seasonally adjusted unemployment is 8.1 percent. Sixteen percent fall below the poverty line. Eighteen percent receive food stamps, and half of these are families with children under 18. Two-thirds of our students qualify for free or reduced-cost lunches. BPA's wholesale costs, he said, have a significant impact on our ability to retain and attract residential service.

As to the strategic drivers affecting BPA's rates, success is to be measured by low-cost power and energy, and system reliability. The more competitive and lower cost our power supply, the better and healthier our economy. Our mission, he said, is to provide an adequate supply of energy at affordable prices.

Regarding past successes, the biggest threat to competitive rates was addressed by the Regional Dialogue contracts, which protect and secure the FBS for the region at cost-based rates; other threats included the Residential Exchange Program (REP) and unknown Fish and Wildlife (F&W) costs. As a result of the region's collaboration, he said, we find ourselves with a new Regional Dialogue contract, a new REP contract with known rates, and two years' stability of costs under the BiOp.

We are grateful for these important past successes, he said, and we must continue to build on them. We support BiOp measures based on the best available science.

As to identifying challenges for the future, Langer mentioned the Canadian Treaty, Environmental Redispatch, and the development of an operating philosophical strategic plan for BPA's O&M (operation and maintenance) and capital costs.

We are well positioned, he said, with the above decisions and are where we should be at this time. Northern Wasco and the U.S. do need to grow. Economic development depends on accomplishing our joint mission, which is securing an adequate supply of energy at affordable prices.

BPA's being in the black, as described in Steve Wright's letter, was due primarily to cost management. That is the kind of manifestation of appropriate planning we appreciate, and we applaud BPA employees for the savings.

BPA's capital level should be no less than its depreciation expense. Additional financial tools should be developed if that standard cannot be met. We support centralized conservation programs with the current features; they make good sense.

BPA is Northern Wasco PUD's largest partner. The agency is and will be for decades our community's most important partner. Without the lowest prudent rates, our mission at home is limited. We must remain competitive.

Audience questions

At 11:40 a.m., Drummond said we have heard from the customers, and he wanted to give constituents in the room or on the phone a chance to speak.

Ray Ellis of Lincoln Electric Cooperate said his area has the highest unemployment in Montana. Many of our people, he said, would like to "have" an economy. We have lost sawmills—they are gone. We are struggling to find a way to make ends meet as a community.

We want desperately to figure out how to have a 9.5-percent rate increase on our members. We cannot stress the importance of what the wholesale power impacts have on us.

Roman Gillen of Consumers Power said that his system is 73 years old. They are making difficult decisions about scarce capital. We need to make investments in our network, he said; growth has caught up with us.

We are experiencing capacity issues at our substations. We are reviewing a long list of projects needing careful decisions on how to spend money. There must be a good wholesale power supply system. It does not do any good for us to do anything without that. We need to make sure the system remains the best in the world.

Break for lunch

At 11:45, Drummond thanked the panel and turned the meeting over to Steve Wright, who adjourned the meeting for lunch.

Presentations on rate drivers

The discussion resumed about 1:00 p.m., with Wright saying that this session came out of the last IPR of two years ago. We put together a set of strategic drivers, he said, referencing the handout “Building the Framework for the IPR.” He asked the audience to focus on what BPA thinks the big changes are from the previous rate case.

He introduced BPA executive **Greg Delwiche**, senior vice president for power services, who would speak about the “Strategic Drivers for Rates” in power; BPA Senior Vice President **Brian Silverstein**, would talk about transmission; and **Claudia Andrews**, BPA’s acting chief financial officer, would address debt and debt structure, with an emphasis on costs coming up for FY 2014-2015 rate period.

Power rate drivers: Delwiche

Beginning with Slide 5 of the handout, **Senior VP Delwiche** said this is a look at what we think the biggest drivers behind power rates will be. What we hope to get out of this discussion is the drivers—what we need going forward, the drivers that can be influenced.

He presented a history of rates from 1984 to the present, saying the past two rate increases have been a bit above inflation, something we are very concerned about. Preliminary information presented today comes out of the prior rate case, he said. The numbers are two years old; they are stale and intentionally have not been refreshed.

He said we are looking at a huge reduction in projected net secondary revenues linked to projections of low gas prices. Uncertainty is significant. We are not optimistic about the projections. The program expenses to be established in the IPR process are up $130 million.

Referencing Bob Hammond’s earlier question about what cost categories can be influenced, Delwiche said that they include CGS (Columbia Generating Station) operating expenses, Corps and Bureau O&M, EE operations, and F&W. It is harder to influence debt expense because we are following a fixed repayment schedule. A conversation he wants to have is, what investments are necessary to sustain the long-term value of the system.

He acknowledged the three challenges Dwight Langer had cited: the Columbia River Treaty, Environmental Redispatch, and finding a balance in O&M and capital investments needed to maintain value.

Steve Klein asked a clarifying question re: Slide 15, trying to understand the composition and allocation of the debt service figure—how the amounts shown in purple and green are to be interpreted.

Barney Burke of Jefferson County PUD thanked BPA for making them BPA’s newest customer. He said he wanted to raise the wind and power conflict. At Port Angeles, he said, a former BPA executive had come to speak about ammonia as a future source of power.

Burke said he had read in *Clearing Up* that BPA is experimenting in peak-power technology. He said he wanted to encourage more development along those lines, to avoid wasting surplus power. He urged BPA to develop technologies that look forward, because many people would appreciate that.

Kevin Owens of Columbia River PUD said that BPA’s presentation fell one page short—there should be a page devoted to the credit and revenue side, not just the expense drivers. He said it is troubling to see 42 percent of the credits wrapped up in secondary sales; there is a lot of risk to doing that. He encouraged BPA to devote time to the matter so we don’t have all our eggs in one basket. With a vast amount of variable resources that we have added to the system, he said, we are not gaining the true benefit and value of the hydro system. We need to expand the value of the system on the capacity side, not solely on the energy side, because otherwise there is too much risk, too much variability.

Mike Raschio of Elcon Associates had a question about the capital expense figures for the Bureau and Corps; specifically how much is related to Grand Coulee Dam and how it compares with FY 2012-2013 levels.

Delwiche said that the amount is on the order of $200 million, adding that as to project staging, it is not wise to have too many units out at any one time. He said we are at the maximum level that we can sustain and still operate the system.

Delwiche called on **Kathy Hacker** of BPA's federal hydro projects group for further insights. She said that for the capital program, the budget is around $219-220 million for FY 2012-2015. Reclamation, she said, is about two-thirds of that. Most investments for Reclamation are at Grand Coulee.

Jack Speer of Alcoa said that part of the revenue credits are sales to the DSIs (direct service industrial customers). Revenue from the IP (industrial firm power) rate to the DSIs is greater than what BPA would receive selling the power into the market. He asked whether BPA, knowing that Alcoa's contract is under challenge, has looked at the risk that the contract could not be continued.

Delwiche said that is a risk factor with a possible rate effect, adding that we have not tried to quantify effects for today's analysis.

Mark Walker of the Northwest Power and Conservation Council thanked BPA for its strong support of the conservation targets in the council's Sixth Power Plan.

Heber Carpenter said he wondered whether BPA has a projection for variable cost of Energy Northwest (ENW) for the FY 2014-2015 period.

Brent Ridge, the chief financial officer of ENW, responded by saying that variable costs mean different things to different people. He asked Carpenter to elaborate, to which Carpenter responded that he meant "any cost you wouldn't incur if the plant didn't run." Ridge said fuel cost would be such a cost.

But, he noted, we also experience costs due to the outage (when we do things to take advantage of the outage). He said that there might be little economic benefit to shutdown when we economically dispatch the plant.

Carpenter asked for quantification, and Ridge said the variable cost of the plant is about $37 per megawatt-hour (he defined variable costs as O&M costs divided by output).

Tom Karier of the Northwest Power and Conservation Council asked over the phone for help in finding the presentation materials. Referencing the capital budget figures, he asked whether BPA would be looking at alternatives where you don't have a ten-percent reduction, or whether BPA will be locked into that for this analysis.

Delwiche said we are not locked into the ten-percent scenario, but we have a major access-to-capital challenge, to which Karier responded that the ten-percent cut does not appear to do much to extend the borrowing authority.

Delwiche said he was correct, that the ten-percent reduction is not a cure-all, nor a silver bullet, but is a tool in the toolbox.

Scott Corwin said he appreciated the responsive way BPA had laid out the information and the fact BPA had staff here today. Many items deserve greater scrutiny, he said.

As to the capital discussion, Corwin said PPC appreciated the way it is bifurcated and that it warrants a good discussion. That lays into rates way into the future, he said, depending on approaches used. It is a valuable discussion for the longer term, too, and PPC is looking forward to being involved in that process.

He asked for clarification of the expense driver related to the F&W $20 million—whether it is an MOA (memorandum of agreement) adjustment.

Delwiche said that in the IPR we had presented cost information for both FY 2012 and 2013 and into the future (FY 2014-2015). What you see here, he said, is just FY 2014-2015 from the previous IPR—two-year-old estimates.

John Saven of Northwest Requirements Utilities (NRU) asked about the expense drivers chart on Slide 15, showing ENW, the Bureau of Reclamation, and the Corps of Engineers with 25 percent combined. If you pull out the capital component, he said, they are a third of the entire expenses.

A general question for BPA, he said, is that as we proceed forward, what role does BPA play for purposes of analyzing these numbers and bringing a product forward? Will I get proposals from these organizations, he asked, or will they be proposals that have been negotiated and scrubbed by BPA as being the best proposals to bring forward?

Delwiche said that Saven would receive something in between what he has described.

We are interested in your perspective, Delwiche said. We will work with the Corps and Reclamation to develop a budget, but we do not want to go dark and bring something forward that has no ability to be influenced. We want the conversation to be collaborative and interactive—what are the drivers and why?

Rick Lovely of Grays Harbor County PUD stepped to the microphone. Delwiche asked in jest whether he was here to sign the REP, to which Lovely responded good-naturedly, "When hell freezes over."

Lovely said his community has a 13-percent unemployment rate, and that they go back and forth with Ferry County in Washington for the honor of worst unemployment. As to the Council's comment, he said, conservation along with RPS and loss of load puts us in jeopardy of being able to maintain our Contract High Water Mark. Bringing on renewables at the same time jacks up the cost to ratepayers.

We have embarked on a campaign in our utility to cut costs, he said. We have 13 fewer employees, with salary freezes. We are working with the union to negotiate a moderate rate increase. We understand utilities require a lot of capital. But you must pick the capital projects that save on the O&M side. What I don't see—it causes me a concern—is that we have had to double our conservation budget, yet we have to pay BPA to maintain a conservation bureaucracy. I don't think we should have to support a bureaucracy when at the same time we have to maintain state targets. We don't have a choice. We pay you money, you do good stuff, but let those of us that have to do this, do our own.

Within your own agency in your departments, I'd really like to see this agency show that you understand the pain in the region, that you have less employees, less costs. Show us documentation that you're doing that. I don't see it. Your explanations about fish costs are great, but there's a huge revenue loss because of it, for resources we don't need.

At some point, he said, we as a region have to slow down. As an example, in the eighties when the economy suffered, a lot of generation had been started in the late seventies. No projects have been built from 1995 on except River Road. We now have a huge surplus and cost aggravation. When are we going to wake up? We have to put the brakes on. We can't afford this.

Delwiche responded that we had intentionally set up today's discussion to use two-year-old information so we could have the kind of conversation Lovely was suggesting; that's what the IPR will be all about.

David Plotz of Lewis County PUD said his area was experiencing a high unemployment rate. Based on my two IPR experiences, he said, I do appreciate your bringing us into the conversation this early, especially as you approach other departments like the Corps and Bureau. Thank you. I hope you continue to hear the voices that you hear to day to minimize costs and rates, and that you start with a blank slate. Things have changed since last time, he said, and they haven't changed for the better.

Charles Pace referenced Slides 16-17 re: F&W expense drivers. If you look at the August 2 decision by Judge Redden invalidating the BiOp, he said, it calls for efforts by the action agencies to reevaluate the efficacy of prudent reasonable alternatives and flow augmentation. He asked whether BPA is looking at potential impacts on expenses of complying with Judge Redden's order.

Delwiche said these numbers do not reflect this, and that Pace had identified a risk factor.

Terry Mundorf of the Western Public Agencies Group (WPAG) referenced Slide 16 re: the net secondary line item of $95 million with five-percent change. When I think of secondary, he said, I think of making up money you lost in the last rate period. I fear that the next rate period might be worse, and then you will have to take into account risk factors. There is a tendency to put money in rates for risk factors.

He asked whether those numbers take into account both the make-up from the current rate period and the risk premium for the next rate period.

Delwiche said neither is factored in. We have reserves, he explained, and as long as we meet our Accumulated Net Revenue thresholds that avoid triggering the CRAC (cost-recovery adjustment clause), that's considered good. The forecasts presented today of next period's rates are merely the rate that is needed to cover our $3 billion in costs minus the approximately $1 billion in credits. There is not a risk factor that is quantified and included in the rate. The risk-mitigation strategy is the Treasury note (providing additional borrowing authority) and the potential for a CRAC.

Mundorf asked whether BPA had determined that the tools used in the last rate case are going to be sufficient to allow BPA to "get to a happy place" with respect to secondary revenues, without putting dollars in rates.

Delwiche said that it was a rate case issue, to which Mundorf responded that having some metrics on that would help the discussion.

Scott Corwin said he had heard the basic response that "it's a rate case issue." But it's worth it, he said, to the extent you can, to go through the assessment of potential need for a risk adder, because obviously it's a big driver.

Delwiche said BPA would try to find a way to do that.

Phil Rockefeller, a Power Council member from Washington State, asked about Slide 17 re: strategic approaches, specifically the F&W comment to continue implementing the accord and ESA obligations.

I'm sure BPA is aware, he said, that provisions of the Northwest Power Act extend beyond that—not only BiOp requirements, but also overall recovery and mitigating for non-ESA impacts. Don't ignore that parameter as you look forward to FY 2014-2015 budgets.

Delwiche said that no matter how hard one might try, it's easy to accidentally leave things out. It's an oversight, he said, acknowledging that the power-act obligations are one of our statutory obligations.

Ben Tansey of *Clearing Up* asked via phone whether there was any room for further restructuring of ENW debt—or is that "all worn out"?

Claudia Andrews said this would be a key topic of her upcoming discussion. The matter of license extension is expected next fall for the plant.

There may be some opportunities to consider debt extension and restructuring, she said, noting that BPA has done debt optimization, debt extension, and debt restructuring to address rate impacts.

This time, she said, we could have another challenge with license extension. We've never extended debt beyond the operating life of the plant. If it occurs (an extension to 2044), that timing might be optimum to look at debt timed with the plant life. There may be opportunities to explore in that area.

Heber Carpenter asked whether any work or information is available to prove that the investments being made in CGS make long-term sense as far as the plant's economic viability. If you look at forward gas prices, he said, there might be a chance we'll spend all this money and end up with a project that has a higher cost compared to alternatives.

Delwiche said that we have not run that scenario, but we'll take Carpenter's comment as input going forward. BPA's analysis of condenser replacement indicated that the long-term value of the plant warranted the investment. That plant delivers a huge amount of value to the region, he noted, and our support for license extension reflects that value.

Wendy Gerlitz of the Northwest Energy Coalition said that in today's materials, there was not a lot of information about the EE budget. We have concerns, she said, that the numbers represented here, such as the ten-percent capital reduction scenario, may not allow BPA to meet the Sixth Plan targets. We've heard about long-term investments. EE is one of those programs that has proven that investments will reduce rates in the long term.

Our analysis, she said, shows you're not currently on track to meet the target; you'll be short 30-55 megawatts (MW), with a budget shortfall of $60-120 million in 2014 required to meet the target. We'll continue to pressure you on this. Release more information so we can look more closely at how you're meeting the target. The presentation doesn't show anything about the low-income weatherization program, which helps end-users in the region.

You've heard how economies are struggling and federal assistance has been cut. The region is hurting, yet the IOUs and some of the publics (e.g., EWEB, the Eugene Water and Electric Board) are providing weatherization assistance. BPA must step up to do the same. Your budgets are stagnant the last five years. Weatherization installation providers tell us they could expend more if necessary.

Delwiche said that the $5 million is reflected in our future budgets. We'd be happy to sit down with you, he said. We believe we will hit the Council's targets. We hit a record 117 MW last year at a significantly lower unit cost.

Gerlitz countered that the targets don't match up with spending. We'd appreciate the opportunity to look at that some more, she concluded.

Charles Pace referenced the Environmental Redispatch ROD (record of decision). He said the payment of negative prices might cost $50 million in 2012. On p. 16, he said, the effects of integration of wind isn't modeled, noting that the payment of negative prices should be factored in. In your request for rehearing, he said, BPA is looking at paying some reasonable amount for negative prices.

He asked whether BPA could share what a reasonable amount of negative price payments would look like.

Delwiche said that the answer is subject to settlement discussions, and that because of a confidentiality agreement, BPA chooses to not respond.

Steve Klein said he felt driven to make a plea to everybody—it's a frustrating topic. My heart—my employees, my community—is in the same place as the Council, BPA, and the Northwest Energy Coalition.

Conservation is the number one tool in our tool belt, he said, expressing a frustration that BPA has no customers in Snohomish County; those people are PUD customers. They hire me and I manage the utility.

Conservation is acquired by my PUD. The frustration that I can't seem to convey, he said, is that when I take ratepayer dollars and ratebase it, we don't borrow the required $20 million a year for the program, then spend it and acquire conservation, and then spend the entire year pleading that we met the regional conservation target to get our money back—it does not make any sense. Anyone who does see the sense, please see me today. It doesn't mean I'm against regional efforts to do things together. But when BPA imposes more borrowing for conservation, you're borrowing for the same kilowatts that you've borrowed for it to be generated. I'm not understanding why people can't understand the position I'm coming from.

Terry Mundorf said that Klein makes a good point. I used to think, Mundorf said, that the practice of BPA running conservation dollars through the books came from the rate test. I'd think there'd be more openness to what Steve proposes, he said, because his point is correct.

Mundorf said BPA should explore in more depth the reason for running conservation through BPA's books. The historical reason may no longer be with us.

Delwiche acknowledged the message heard from both of the commentators.

Regarding Slide 20 and generation inputs, **Clay Norris** of EWEB asked whether BPA's expectation is that the market will be able to supply additional "incs" and "decs" instantaneously, or whether some buildup would be required.

Delwiche said that if the agency's need for inc/dec reserves outstrips the capability of the hydro system, we would put out an RFP for third-party supply, and expect we could gain supplies in relatively short order.

Steve Kern of Seattle City Light asked whether BPA is factoring in—adding back—a shorter-term life of units that are being subjected to more operational variation for providing balancing reserves for wind.

Delwiche sought to paraphrase the question by asking whether Kern meant that BPA's balancing service rates are priced to cover the increased wear and tear on machines. He said BPA is trying to gather information on what might constitute a solid foundation to look at incremental wear-and-tear implications and how to price it to recover those costs in the next rate case.

Transmission rate drivers: Silverstein

Senior VP Brian Silverstein spoke next from the handout section on Transmission Services.

Mike Raschio asked whether the information excludes provision of ancillary services, to which Silverstein responded that they are excluded.

Clay Norris referenced a slide showing a total revenue requirement of $140 million, compared to Slide 16, where the change in secondary revenue is shown as $95 million.

Given the relative size, he asked, have you studied anything that could be done on the Transmission side to provide greater access to markets to alleviate the impact of secondary revenue? Have you looked at ways to improve access to markets via transmission build-out to offset secondary-revenue dollar impacts?

Silverstein said that was a great question, noting that we've completed investments in the AC (alternating-current) intertie to make greater use of the assets we have, such as the addition of series capacitors and voltage support regimes.

We have operated for decades under a nomogram, he said, pushing it out of traditional limits and making additional sales. People will find a higher availability of the AC intertie as a result.

We're looking at refurbishment of the DC (direct-current) circuitry at Celilo to squeeze a few more megawatts out of the line to California. We are making big-picture investments, and parties like British Columbia and California have spent a significant amount of time to review building a brown-field upgrade of the intertie, a $3-5 billion investment. But given the current state of California laws, they decided it was not a prudent thing to do at this time.

Dave Arthur of M-S-R (Modesto Irrigation/Santa Clara/Redding) asked whether, in light of transmission increases and the market price of sales to California, BPA plans to reduce secondary sales to reflect the increased share Transmission would get at COB (California-Oregon Border).

Silverstein said we have not done the detailed rate analysis looking at secondary sales and the impact on use of the intertie. The California intertie, he said, is fully sold out for long-term commitments. Short-term revenues are relatively modest on the Transmission side. Your question, he sought to paraphrase, is whether Power Services will factor this into its analysis.

Mike Raschio asked whether the SI (Southern Intertie) rate is expected to jump due to the DC system upgrade, to which Silverstein responded that, yes, it is a key driver.

Raschio continued asking about the DC upgrade, saying that a news release spoke of a 100-MW increase in capacity. He asked whether the terminal equipment will give an additional 500 MW of capacity to the extent other upgrades are done in the south, plus AC network upgrades.

Silverstein said that was correct. The terminal will be able to carry 600 MW more than today, he explained, but only if the California parties upgrade their lines. They don't have the clearances to carry the higher current without such upgrades.

Raschio asked whether the graphs showing the NOS (network open season) project assume all aspects being completed, including the Montana upgrade.

Silverstein said that we had used older data, but nonetheless believe we can accomplish the ten NOS projects, adding that original cost estimates will be updated in the IPR.

Charles Pace referenced Slide 31 re: the PTSA (precedent transmission service agreements) reform initiative, asking whether BPA can maintain rate neutrality and still accomplish PTSA rate reform.

Silverstein said it appears to look like there would be net losses; the matter is in negotiation with the parties.

Brenna Moore from Clark County PUD inquired about assumed NOS incremental revenues and whether BPA also assumed some offsetting transmission credits.

Silverstein said BPA had accounted for them.

Rick Lovely inquired how BPA handles connections of a customer that is connecting to the system, where the principal beneficiary of the system is the customer, asking whether BPA demands that they pay all costs up front.

Silverstein said it depends on the situation. For generation interconnections, BPA follows FERC rules (under which parties have to advance funds). Over time, he said, if they start taking transmission service, they will be taking transmission credits.

As to what time frame, he said it depends on the investment and megawatts of transmission they request. In some cases, it's paid off in five years; in other cases, in 20 years.

There were several additional questions from Raschio, Kern, Moore, and Lovely, leading up to a break at 2:50 p.m.

Financial rate drivers: Andrews

At 3:10 p.m., **Claudia Andrews** said that she would be presenting "all the fun stuff"—

specifically, two topics: reserves and debt service. She referenced Slide 34.

Kevin O'Meara of PPC asked when a decision would be made on the CGS license renewal.

Brent Ridge explained that it would occur in late June; it's with the NRC (Nuclear Regulatory Commission), he said.

O'Meara asked about the variable rate asset match, whether there is a risk that it will be more expensive if interest rates go up.

Andrews said yes, adding that she wanted the opportunity to talk about it further, noting that the last time, we had a process that paralleled the IPR. She said she would expect a similar process this time.

O'Meara said he was nervous about doing things that assume interest rates will stay low.

Andrews said that this and other suggested issues like the contribution schedule of the decommissioning trust fund might be topics of discussion at the next QBR (Quarterly Business Review), on May 1.

Conclusion

Steve Wright sought to bring the meeting to closure at 3:30 p.m. We're ready to wrap things up, he said, and we are very appreciative of people being so thoughtful and committing their time.

He explained that individuals had approached him during the break with positive feedback on the meeting format. We're trying to be a learning organization, he said, to do this the best way we can that works for you.

He thanked the individuals who served on the regional economic panel and, in closing remarks, acknowledged that the audience had seen some really big numbers from us. Big rate increases are not something we want, he said.

We are putting out numbers that are not baked. He said he had worried about people's reaction, but that it had worked really well. People made thoughtful comments, taking them in good spirit.

He said the next phase is the traditional phase, and that we have work to do internally looking at budgets. If you have follow-up questions, he continued, the best way to participate is through the QBR process. We will pick up the full-scale IPR in the May-June timeframe.

He asked attendees to complete the evaluation form. BPA tries to listen, he said, and we try to be responsive. Feedback is helpful to us and hopefully to you as well.

Steve Taylor of Mason County PUD No. 1 said that while he liked Slide 21 (transmission rate analysis of forecasts), it would be nice to have something similar for the Power side.

Wright said this was hard to do because of the secondary forecast, but that we would give some thought on how to do it, including letting participants pick a number.

Bill Drummond said he wanted to put in a plug for the April-May timeframe to discuss capital projects.

Today, he said, there was a lot of focus on expenses. You'll have an opportunity to see BPA's capital projections and the analysis to justify them.

We'll come out into the region to hold a series of road shows, provide information, and take comments.

ADJOURNED 3:35 p.m.

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