

INDUSTRIAL  
CUSTOMERS OF  
NORTHWEST  
UTILITIES

KEN CANON  
EXECUTIVE DIRECTOR

June 13, 2005

Paul E. Norman  
Senior Vice President  
Bonneville Power Administration  
Post Office Box 3621  
Portland, OR 97208

**RE: ICNU Comments on BPA's Regional Dialogue – Second Phase**

Dear Paul,

These comments are in response to your May 11, 2005 letter regarding the opportunity to comment on the second phase of the Regional Dialogue. Throughout this process, much has been written and many discussions have taken place regarding the critical issues that are part of this dialogue. While many can agree on the fundamental principles to be addressed, little actual consensus has occurred. BPA and its customers face the daunting challenge of addressing a twenty year future premised on having the new policies comply with the antiquated Regional Power Act. In addition, with the power market high in relation to BPA's PF rate, most publics will have little option but to sign whatever 20-year BPA contract is offered. The challenge to BPA is to act as if a competitive market exists or could exist in the future, even if that is not currently the case.

**Principles**

The following principles have been enumerated as being the foundation for BPA's Regional Dialogue:

1. Clarify responsibility between customers and BPA for developing new resources.
2. Equitably allocate the long-term benefits of the existing federal system to customers.
3. Create a common interest among BPA's customers that aligns interests in BPA's performance.
4. Provide 20 year take or pay power sales contracts that will be easily understood, durable and enforceable.
5. Enhance the ability of BPA to meet its Treasury obligations.

6. Provide long-term rate making policies that clarify the allocation of existing costs and benefits as well as the clear assignment of the costs of meeting future load growth.
7. Create a policy and contractual environment that reduce litigation.
8. Ensure that BPA and its customers have a cost management process that provides funding for necessary services while providing low rates

Of these principles, the easiest to satisfy is the enhancement of the ability to make BPA's Treasury payment. Combine 20 year take or pay contracts with BPA's existing rate making discretion and the Treasury payment will indeed be enhanced. Meeting the other principles will require BPA to make tough choices among customers. In addition, to be successful in creating a new era with its customers, BPA must be willing to ensure that its contracts and process are perceived to be balanced and fair by its customers.

## **Answers to Questions Raised in BPA's May 11, 2005 Letter**

### **1. Service to public utilities**

We generally support the allocation process as developed by the Public Power Council. As to providing customers with more rate stability and predictability, a rate methodology is just part of the equation. Other important elements are cost control and the rate setting process itself. Changes to the rate setting process such as an independent Administrative Law Judge and having BPA costs as part of the rate case would help to ensure more rate stability and predictability. Reaching agreement between BPA and its customers on the appropriate method to address risk is also key to rate stability and predictability. As to newly formed publics, we believe that BPA should provide PF power for up to a set amount (75 – 100 MW) for newly formed public power utilities. BPA would not augment for that amount unless a new public power load was created. Specifically, BPA would not acquire power to hold in reserve for a new public. Instead, BPA would augment at the time a new public needed power and all other BPA purchasers would have their allocation decreased by a proportional amount.

### **2. Residential Exchange**

ICNU does not support the current method of establishing residential exchange benefits. From our perspective, it ignores the 7(b)(2) rate test. In addition, the use of the "market" instead of Average System Costs (ACS) methodology leads to residential exchange benefits that are too large. ICNU supports the use of one of several methodologies. We support using the traditional ASC methodology coupled with the 7(b)(2) rate test. This is provided for in the Regional Power Act. Another alternative would be to set the residential exchange benefits at a certain level for a specified PF rate (i.e. \$180 million benefit if the PF was 29 mills/kWh). The amount of benefit would go up as the PF rate drops and vice versa. We have also been considering a variation

of the current “market” formulistic approach but with a specific provision for the operation of the 7(b)(2) rate test.

### **3. DSI Service**

Early in the Regional Dialogue process we supported limited service to the DSIs. Now, we have modified our position. We do not support service to the DSIs at a PF equivalent rate (or any lower rate). Since there is no statutory provision for this service, BPA’s only criteria for making this decision is to determine the pain threshold of PF customers at different levels of DSI service versus the probability of keeping some DSI customers operating. Both of these factors are unknown. While some PF-based customers (including ICNU) were once willing to consider some level of DSI subsidy, the growing DSI financial demands and the potential for an increase in BPA’s base rates have led many to urge BPA to limit sales to the DSI.

### **4. Resource Adequacy Standards**

This issue is not yet ripe for a decision. While the Council has begun to work on this issue, its ultimate resolution is still some time in the future. Much depends on the specifics of such a standard and how much regional utility consensus exists in support of the standard. BPA’s support of such a standard could lead to a perception that BPA is doing so in an effort to actually limit those publicly-owned utilities that wish to diversify away from BPA.

### **5. Cost control and dispute resolution**

BPA cost control is at the heart of whether any of the issues discussed in the Regional Dialogue make sense for BPA’s customers. It is not just whether BPA can be less than market, the importance of cost control is the extent to which BPA can keep its cost-based rates low. Several critical issues are encompassed by the term cost control. These include customers having the ability to influence BPA policies before policies are actually established. Policy development is the first step in incurring cost obligations and therefore is a critical stage for meaningful customer involvement. A second component is cost and financial transparency. Ensuring that customers know BPA’s financial condition helps to avoid surprises. Third, for those activities that BPA does fund (either directly or through the Bureau, the Corp or ENW) ensuring that they are conducted efficiently should be an ongoing endeavor. BPA’s current Enterprise Process Improvement Program (EPIP) is a good start in operating more efficiently. Implementation of that effort will speak volumes as to BPA’s intentions regarding meaningful cost control.

While cost control is critically important for customers with long-term take or pay contracts, enforcement of any cost control mechanism is difficult. Having contractual off ramps is one solution, although of limited use due to market conditions. This is an

area that needs more work and in which BPA needs to show more creativity and flexibility.

In summary, ICNU looks forward to commenting on BPA's draft ROD for the Regional Dialogue. At this time, we still question whether resolving the question of resource development is worth twenty year, take or pay contracts, the agony of power allocation and limited enforceable cost control mechanisms. It has been our recent experience that public power utilities have as many challenges developing resources, as does BPA.

Sincerely,

Ken Canon