Tiered Rate Methodology Rate Case

DIRECT TESTIMONY

May 2008

POLICY OVERVIEW:
Cherry, Bliven, Wilson
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## INDEX

### TESTIMONY of

DIANE CHERRY, RAYMOND D. BLIVEN, and SCOTT K. WILSON

Witnesses for Bonneville Power Administration

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TRM-12-E-BPA-02

TESTIMONY of

DIANE CHERRY, RAYMOND D. BLIVEN, and SCOTT K. WILSON

Witnesses for Bonneville Power Administration

SUBJECT: POLICY OVERVIEW

Section 1: Introduction and Purpose of Testimony

Q. Please state your names and qualifications.
A. My name is Diane Cherry, and my qualifications are contained in TRM-12-Q-BPA-04.
A. My name is Raymond D. Bliven, and my qualifications are contained in TRM-12-Q-BPA-01.
A. My name is Scott K. Wilson, and my qualifications are contained in TRM-12-Q-BPA-19.

Q. What is the purpose of your testimony?
A. The purpose of this testimony is to sponsor the Tiered Rate Methodology (TRM), TRM-12-E-BPA-01. We provide an overview of the TRM and discuss the background policy and context underlying the TRM; describe the relationship between the TRM and the Regional Dialogue Contracts; and discuss criteria, conditions, and processes for TRM change or re-opening. This testimony makes use of defined terms in the Tiered Rate Methodology (TRM); see TRM pages v-xvii.

Q. How is your testimony organized?
A. Our testimony is organized in 9 sections. Section 1 is this introduction. Section 2 discusses background and context for the TRM. Section 3 discusses the concept of tiered rates. Section 4 discusses the relationship between the TRM and power sales contracts. Section 5 discusses the relationship between the TRM and relevant rate cases. Section 6 discusses the evolution of the rate design presented in the TRM. Section 7 discusses the rate design principles on which the TRM is based. Section 8 discusses other rate design
issues, such as those related to the Slice product, service to BPA’s DSI customers, and
the section 7(b)(2) rate test. Section 9 discusses TRM sections 12 and 13.

Section 2: Background

Q. What is the purpose of the TRM?
A. The purpose of the proposed TRM is to establish the rate design and cost of service
allocations necessary to implement the Long-Term Regional Dialogue Final Policy
(Policy), issued in July 2007. The rate design and cost allocations would be applied in
each Northwest Power Act section 7(i) rate proceeding over the term of the Regional
Dialogue contracts. The rate design aspects of the Policy, as implemented in the TRM,
are subject to final determination in this section 7(i) rate proceeding. The TRM gives
direction on how to determine rates. The proposed TRM is designed to provide
assurance about how BPA’s costs would be allocated in a manner that would preserve
the value of the existing Federal system and protect that benefit from the costs of
additional service for customers’ load growth. As proposed, the TRM is intended to
provide a predictable and durable means by which to tier BPA’s Priority Firm Power
(PF) rate, beginning in FY 2012.

Q. What do you mean by predictable and durable?
A. The TRM would establish a rate design where the costs of the existing Federal system
resources would be allocated to particular Cost Pools and recovered in total. The TRM
also describes how the costs in each Cost Pool can change over time.

BPA intends to seek Federal Energy Regulatory Commission (FERC or the
Commission) approval of the TRM for a term concurrent with the new Regional
Dialogue power sales contracts. See TRM section 11.

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Q. What specific goals of the Policy would be achieved through the TRM?
A. The Policy at 5-7 identified a number of goals to be achieved through the contracts and rates. Those applicable to this TRM are:

Promotion of Regional Electric Infrastructure: Promotion of regional electric infrastructure in order to ensure a reliable future power supply and to avoid excessive market price volatility. As stated in the Policy,

“[d]efining the amount of power each customer is eligible to purchase from BPA at the lowest-cost Tier 1 rate (the HWM [High Water Mark]) will allow utilities to move forward with plans to meet their additional or new load by developing their own resources or purchasing additional power from BPA at a potentially higher Tier 2 rate.”

Low and Stable BPA Tier 1 Power Rates: Low power rates are one of BPA’s most important contributions to the regional economy. The Policy will help maintain low and stable Tier 1 power rates by minimizing to the extent possible the amount of resource Augmentation costs included as part of the Tier 1 rate.

Enhanced BPA Financial Stability and Assurance of Treasury Payments: A low and stable Tier 1 rate created by changing BPA’s past practice of acquiring new power and melding its costs with those of the existing system would greatly reduce the financial uncertainty that occurred when BPA power rates rose due to the inclusion of incremental resource costs. This rate stability should significantly reduce future risks to BPA’s ability to make its Treasury payments.

Accomplishment of Conservation and Renewable Resources: Tiered rates and HWMs would create “powerful economic incentives” for customers to develop conservation and renewable resources. The TRM describes the pricing construct that would be used for support services that customers will need to
integrate intermittent renewable resources, such as wind, to serve their retail loads.

Q. What is accomplished by tiering the PF rates?
A. We believe that by tiering the PF rates BPA would be able to preserve the value of the existing Federal Base System. The costs of new resource acquisitions (except for specific, limited Augmentation as set forth in the section II of the Policy and described in TRM section 3) would be allocated to Tier 2 Cost Pools, not to Tier 1 Cost Pools. Tiering the rates would create cost transparency by reflecting the cost of incremental resources incurred by BPA to serve customers’ above-HWM load placed on BPA. Allowing customers to transparently see the costs of BPA’s future resource acquisitions to meet their load would allow customers compare the economics of both BPA’s and their own resource acquisition choices. In addition, customers who choose to use their own resources to meet above-HWM load would avoid paying the costs of BPA acquisitions to meet the above-HWM load of other customers who purchase such power from BPA. Section 3 of this testimony further describes the tiered rates construct.

Q. When would the proposed TRM rate design take effect?
A. The first rates established pursuant to the TRM would take effect in the FY 2012-2013 Rate Period.

Q. If the first rate case that would apply the rate designs established in the TRM is three years away, why are you conducting this section 7(i) proceeding now?
A. BPA’s Subscription power sales contracts expire on September 30, 2011. We expect to offer new 20-year CHWM Contracts to follow the Subscription contracts in August 2008. To make informed choices necessary to develop resources, BPA and customers need long-term certainty about the service provided under these CHWM Contracts. An important part of that certainty is establishing long-term rate design certainty that would be applicable to power sold by BPA under those contracts. Customers will be asked to
execute their CHWM Contracts in the fall of 2008. Because the contracts would provide service from FY 2012 through FY 2028, it is crucially important that the rate design be as stable as possible over that same period. In order to make informed decisions, customers need to understand the rate construct that will apply to their cost of service under these contracts.

Q. Are you proposing to set actual rate levels now?
A. No. We are not proposing to determine specific costs or rate levels applicable to power that will be sold under these contracts in this TRM rate proceeding. Rather, the specific rate levels would be developed, consistent with the TRM, in the respective section 7(i) rate proceedings during the term of this TRM.

Section 3: Tiering: What It Is and What It Is Not

Q. What do you mean when you use the term “tiering”?
A. When using the term “tiering,” we mean the process of segregating and allocating separately the costs associated with existing Federal resources (Tier 1 Costs) and the costs of future resources (Tier 2 Costs). This design means that BPA would no longer meld the costs of future resource acquisitions with the costs of the existing Federal system. The result is that the PF rate would have both Tier 1 Rates and Tier 2 Rates based on different Cost Pools.

Q. What future resource acquisition costs are you referring to that would be Tier 2 Costs?
A. We are referring to the cost of any additional resources and associated support services required to meet the above-HWM load on BPA. The TRM also identifies some very specific circumstances where certain future resource acquisition costs would be included in Tier 1 Costs; see TRM sections 3.2 and 3.4.
Q. Under the TRM, are you proposing to allocate the output of the Federal resources among customers?

A. No, we are not proposing to allocate the output of the Federal resources among customers. Rather, under the TRM we are proposing to allocate the costs of resources. This is a very important distinction. BPA will continue using the entire Federal system resources to meet all of its regional customers’ loads with firm power without distinction between the proposed rate tiers.

Q. What resource costs would be used in setting the Tier 1 Rates?

A. The costs of a specific set of Federal system resources, identified as Tier 1 System Resources, would be allocated to the Tier 1 Cost Pools. See Roberts et al., TRM-12-E-BPA-04 and TRM section 3 for a description of Tier 1 System Resources. These forecast costs would be the basis for Tier 1 Rates. Similarly, Tier 2 System Resources costs would be assigned to the Tier 2 Cost Pools and would serve as the basis for Tier 2 Rates.

Q. How would BPA decide the amount of power a customer could purchase at Tier 1 Rates and how much at Tier 2 Rates?

A. The Policy establishes the basic steps for the calculation of High Water Marks, which would be used to determine how much requirements power each customer can purchase at Tier 1 Rates. There would be several types of HWMs established for each customer; the most important are the Contract HWM (CHWM) and the Rate Period HWM (RHWM). The specifics of how the various HWMs are determined are discussed in TRM section 4 and in Stene et al., TRM-12-E-BPA-05.

Q. Briefly describe the CHWM and RHWM.

A. The CHWM for each customer would be based on each customer’s Measured FY 2010 Load adjusted for several factors and net of its Existing Resources. The CHWM would
establish each customer’s baseline eligibility to purchase an amount of power at Tier 1 Rates.

The RHWM, which would be calculated for each Rate Period, would adjust the amount of power a customer could purchase at a Tier 1 Rate during that particular Rate Period based upon changes to the forecast firm critical output of Tier 1 System Resources. A customer could purchase an amount of power up to its RHWM at Tier 1 Rates but would be limited to its Net Requirement if the customer’s Net Requirement was less than its RHWM. Any forecast power purchase from BPA for above-RHWM load would be charged a Tier 2 Rate(s). Id.

Q. When you talk about Tier 1 (or Tier 2), are you talking about products?
A. No. We expect BPA will offer a single requirements power sales contract—the CHWM Contract—to each customer to serve its Net Requirement with Federal system power. Each customer would have a choice of the products BPA would offer—Load Following, Block, and Slice/Block. Without respect to which product a customer chooses, the customer would be able to purchase power up to its RHWM at Tier 1 Rates. In addition, we expect BPA to offer several Tier 2 Rate Alternatives, which would have certain contractual requirements, such as notice provisions or agreements associated with the Tier 2 Rate Alternatives.

Q. Why do you believe it is important not to allow costs to shift among Cost Pools?
A. We believe that customers would benefit from not having costs shift among the various Cost Pools. Keeping Cost Pool costs separate would provide customers with rate stability and certainty. To ensure that costs would not shift between the Cost Pools requires both the specified cost allocations detailed in the proposed TRM and contractual commitments on the part of customers. Thus, it would be fundamental that BPA perform the correct cost allocations and that customers meet their contractual obligations. We also believe keeping Cost Pool costs separate would result in sending
more efficient and effective price signals, which would lead to more cost-effective resource decisions by BPA and its customers.

Q. **Would Tier 2 Rates be limited to only a customer’s load growth served by BPA?**

A. No. The Tier 2 Rate should not be equated with Federal power that would be used to serve only a customer’s load growth. Although load growth is expected to be the largest component of above-RHWM load, it would be possible for a customer without load growth to be faced with a situation of purchasing at Tier 2 Rates. The firm critical output of Tier 1 System Resources may decline output in the future. Such a decline in output would reduce customers’ RHWMs, resulting in increased exposure to Tier 2 rates. In this case, the proposed TRM rate design would allow customers to more clearly see BPA’s costs of replacing some or all of the decreased firm critical output of Tier 1 System Resources. BPA would serve some of the region’s load growth at Tier 2 Rates, but we also expect customers to develop Non-Federal Resources and apply those to their load.

Q. **Would all load growth for Load Following customers be charged Tier 2 Rates?**

A. Not necessarily, or more accurately, not immediately. The TRM would establish a process for determining above-RHWM load. Above-RHWM load would be determined by BPA in advance of a Rate Period and would not change during that Rate Period. Once established, the above-RHWM load would not include unexpected load growth during that Rate Period. Also, RHWMs would be limited to an annual energy amount. Therefore, although a customer’s load may grow in some months, if it is not growing on an annual basis, the monthly load growth would not be considered above-RHWM load. To address this type of growth in monthly load, BPA would assess the customer Load Shaping rates for the higher monthly loads and provide Load Shaping credits for the lower monthly loads. This would afford customers a measure of certainty as to their costs within the Rate Period. We believe such certainty is appropriate for within a Rate
Period when customers have less flexibility to respond to the kind of price signal that charging a Tier 2 Rate based on incremental cost would provide.

Q. *How would access to power at Tier 1 Rates change if the forecast firm critical output of Tier 1 System Resources changes?*

A. We recognize that the projected firm critical output of Tier 1 System Resources may increase or decrease during the term of the CHWM Contracts. To address these changes, prior to each relevant rate case BPA would forecast the firm critical output of Tier 1 System Resources and use that information to establish RHWMs. The RHWM calculation would start with the CHWM and adjust it up or down based on changes in the forecast firm critical output of Tier 1 System Resources.

Q. *Would a customer always be able to purchase Federal power up to its full RHWM?*

A. No. A customer could not purchase power up to its full RHWM amount if its Net Requirement is less than its RHWM. Within a Rate Period, the RHWM would set a maximum amount of energy available to the customer at Tier 1 Rates, but the total amount of power that a customer could purchase from BPA would be limited by the customer’s determined Net Requirement. The value of any unused RHWM would be credited back to all customers purchasing at Tier 1 Rates. See TRM section 4.3.

Q. *How would BPA ensure that a customer’s decision on how to serve its above-RHWM load does not shift costs to other customers?*

A. To create a basis for parity and comparison among the customer’s options on how to serve its above-RHWM load, BPA would sell all power at Tier 2 rates as if it were a flat annual block of energy. This flat annual block would create an economic benchmark to allow comparison among Tier 2 Rate Alternatives and Non-Federal Resources that a customer could choose to serve above-RHWM load. Basing the price of Tier 2 Rate Alternatives on a supply of power shaped in a flat annual block is straightforward and would also reduce BPA’s administrative burden. The flat annual block should avoid
future cost disputes and disagreements that could arise under a variably shaped Tier 2
Rate designs.

BPA’s Tier 2 Rates would include Resource Support Services, which would account for the financial costs or benefits created by converting the projected output of specific Tier 2 System Resources into a flat annual block. When a Load Following customer chooses to meet its above-RHWM load with its own resources, the same Resource Support Services would be used to convert the projected output of the customer’s resource into a flat annual block of power. However, this application of Resource Support Services would be limited to Load Following customers, because the shape or variance of their resource choices would affect the hourly amounts of power BPA sells to the customer. The Load Following customer also may choose instead a non-Federal source to supply RSS-type services. Block and Slice/Block customers’ resource choices would not affect the hourly amounts of power BPA sells to the customer, so RSS would not be a mandatory service for these customers. Block and Slice/Block customers may choose to buy stand-alone Resource Support Services for new renewable resources that they dedicate to load, however.

Q. Would BPA tier all of its rates?

A. At this time, we propose to tier only the PF power rate. The tiered PF rate would apply only to power sold under CHWM Contracts. It is not our expectation that BPA would tier the PF Exchange rate, the Industrial Firm Power (IP) rate, or the New Resources Firm Power (NR) rate at this time, but the TRM would not prohibit those rates from being tiered.

Section 4: Relationship Between the TRM and Regional Dialogue Power Sales Contracts

Q. Please describe the relationship between the TRM and the CHWM Contracts.
A. We expect BPA and customers to sign new 20-year CHWM Contracts by December 2008. Under these contracts, BPA will sell power to customers for their Net Requirement for the period FY 2012 through FY 2028. The TRM would establish the rate design approach that BPA would follow when it sets rates during the term of the CHWM Contracts. It also would establish the process that BPA would follow in FY 2011 to calculate a CHWM for each customer. Specific details of the CHWM calculation are discussed in TRM section 4 and in Stene et al., TRM-12-E-BPA-05. BPA would amend each customer’s CHWM Contract to include its CHWM in late-FY 2011.

Q. What product choices would BPA offer Publics under CHWM Contracts?
A. BPA would offer CHWM Contracts with three products choices: 1) Load Following, which would meet a customer’s hourly loads minus the amount of its firm resources declared and dedicated to be used for its load; 2) Block, which would provide a customer with predefined hourly amounts of power based on the customer’s planned Net Requirement; and 3) Slice/Block, which would be based on a planned Net Requirement and combines a Block purchase with a Slice purchase. The Slice portion provides power based on the shape of generation from Tier 1 System Resources.

Section 5: Relationship Between the TRM and Relevant Rate Cases

Q. What do you mean by “relevant” rate cases?
A. We propose that the TRM be in place for the 20-year term of the CHWM Contracts. However, as proposed in the TRM, BPA would commit to establish actual rate levels every two years beginning with FY 2012. By relevant rate case, we mean the specific rate case that BPA would hold to set the rates for each two-year rate period during the term of the CHWM Contracts.

Q. Why are you proposing to conduct rate cases every two years?
A. We believe that it makes sense for a number of reasons.

1) Load forecast risk. Above-RHWM amounts are set based on load forecasts. We believe it is reasonable to set the above-RHWM amounts frequently to correct load forecast error.

2) Market price risk. We are proposing to base certain rate components on market price forecasts (i.e., Load and Resource Shaping Charges). A longer rate period would increase the chances that the forecast price would not align with the then-current market prices.

3) Cost of risk. Because establishing rate levels based on forecast market prices for surplus sales, given the volatility of market prices, BPA’s revenue uncertainties would increase the longer any particular forecast is relied upon and the associated risk mitigation could become very expensive. Therefore, longer rate periods generally mean higher rate levels, with more-frequent rate adjustments, such as Cost Recovery Adjustment Clauses or Dividend Distribution Clauses.

4) Slice True-Up Adjustment. Any disputes over the costs included or excluded in the Slice True-Up Adjustment would be resolved in rate cases. Longer rate periods would defer the decision of the proper allocations of costs between Slice and Non-Slice Rates and between Tier 1 and Tier 2 Rates.

5) Average System Costs. We expect utility ASCs will be determined on a two-year basis. Having rate cases on a two-year basis also would keep rates and ASCs synchronized.

Q. Do you anticipate BPA establishing rates for a period other than a two-year Rate Period?

A. Yes. First, the TRM would be applied for 17 years of power deliveries, which does not divide exactly into two-year Rate Periods. BPA has not decided whether at the end of the contract period there would be a three-year Rate Period or a one-year Rate Period. Also,
it is also possible that other events might arise that would alleviate the need to make such a decision, such as having subsequent contracts start a year early. Thus, BPA will determine this Rate Period duration proposal at the end of the contract period.

Second, it is possible that over the next 20 years, the market and the load/resource balance situation may stabilize. BPA and customers may decide that BPA does not need to undergo the effort or the expense of conducting rate cases every two years. In that situation, BPA may propose to revise the TRM to allow other than a two-year Rate Period; such proposal for change of the TRM would be done consistent with the provisions as outlined in TRM sections 12.3 and 13.2.

Q. Do you expect BPA to file this TRM with FERC at the conclusion of this 7(i) process?

A. Yes, that is our current expectation. Filing for approval by the Commission now would bring finality to this process and clarify that future revisions of the TRM would be subject to the terms therein, not in the WP-12 rate case. Seeking approval now would also assure customers that CHWMs and the Transition Period method, actions that occur outside of the WP-12 rate case, would be established as proposed in the TRM. By waiting to file with the Commission, BPA could find itself having completed a WP-12 rate case assuming TRM approval, only to have to repeat the process and re-do the rates if the Commission remanded the TRM. Submitting to the Commission sooner rather than later would ensure that the proposal filed by BPA staff closest to the development of the TRM and reviewed by Commission staff who have demonstrated they are familiar with BPA ratesetting directives. Also, this Commission seems favorably disposed toward pro-market and pro-infrastructure development proposals. We believe the proposed TRM would be favorably viewed by this Commission as furthering its goals, a view that might not be held by future Commissions.

We expect BPA to consider this question and decide on when it would file with the Commission during the course of this proceeding.
Q. *What do you expect would be decided in each relevant rate case?*

A. Well, for one, the actual rate levels would be set in each rate case. Additionally, TRM section 12.4 specifically calls out actions that would not considered to be changes to the TRM. As appropriate, these would be dealt with in the relevant rate case(s). These include:

- Calculation of actual rate levels.
- Any rate issues not addressed in the TRM.
- Any rate issues specifically identified in the TRM that are specifically reserved for determination in a future 7(i). These include, but are not limited to:
  - Rate treatment for customers that execute Regional Dialogue Contracts without a Contract High Water Mark;
  - Forecast of the firm critical output of Tier 1 System Resources, forecasts of Augmentation of Tier 1 System Resources, forecasts of Balancing Power Purchases;
  - Allocation of costs consistent with the costs allocation principles, method, and table;
  - Risk mitigation;
  - Development of a System-Shaped Load for each customer;
  - Determination of cost adders to Tier 2 Cost Pools;
  - Design, pricing, and application of the Resource Support Services (RSS) rates;
  - Irrigation Rate Mitigation true-up;
  - Application of section 7(c) of the Northwest Power Act;
  - Application of section 7(b)(2) of the Northwest Power Act;
  - Rates for New Publics;
  - Rates for unanticipated above-RHWM load;
Rates for customers who choose to switch products; and
Rates for customers who choose to transfer load served at a Tier 2 rate to
being served at a Tier 2 Vintage rate.

Section 6: Evolution of Rate Design

Q. There is a very specific Tier 1 rate design in this proposal. How did this come about?
A. In the Fall of 2006, BPA staff began working collaboratively with public power
representatives to develop the Tier 1 Rate design. In the process, a number of
alternatives were considered, from the status quo rate design to ones with significant
modifications. During the ensuing months, what is now the proposed TRM rate design
began to take shape, using components of a number of different alternatives. After
about one year, the public power representatives coalesced around a general concept that
forms the core of the rate design included in the TRM.

Q. Are there parts of the public power rate design concept that BPA did not adopt as part of
this TRM proposal?
A. Yes. The demand rates in the public power proposal were constant from month to
month, whereas we are proposing that the monthly demand rates will be shaped through
the year. See Fisher et al., TRM-12-E-BPA-06. The public power proposal developed
Contract Demand Quantities (CDQs) based on FY 2008-2010 historical load levels,
whereas we are proposing to use FY 2005-2007 historical load factors applied to
Eligible Load. Id.

Q. Why do you propose a shaped demand rate?
A. We believe there are two primary reasons to shape the demand rates. First, demand
charges that more directly pass on to customers the actual cost of capacity provide the
correct price signals to customers as they consider developing new resources. We
believe these prices signals will encourage customers to undertake this infrastructure
development. Second, we believe it is important to show customers that capacity has
different value in some months compared to other months. For example, one megawatt
of capacity in January has more value (and hence is more costly to provide) than one
megawatt of capacity in June. While we could have proposed to determine the shape of
demand rates in each relevant rate case, we propose to define now how the demand rates
would be shaped so that customers would have advance knowledge of BPA’s practice
and can make better-informed long-term resource decisions.

Q. Why do you propose a set of years to calculate CDQs different from those in the public
power proposal?

A. We are proposing to use FY 2005-2007 historical load factors to calculate CDQs rather
than FY 2008-2010 load levels proposed by public power. We prefer to use a historical
time period during which peak demands were able to be met from the existing Federal
system rather than a future period when BPA’s system capability to meet peak demand
loads could require additional future resources. Using historical period load factors
applied to Eligible Load would also allow more load growth to be reflected in CDQs
than the public power proposal. Also, using the earlier period would allow more time to
determine the historical loads, any necessary adjustments, and more customer review
than waiting until FY 2011 when development of CHWMs would compete for BPA and
customer staff time and attention. We believe that our proposal appropriately accounts
for customers’ load growth between the period used for historical load factors and the
year used to determine CHWMs by applying the historical load factors to Eligible Load.
Section 7: Rate Design Principles

Q. During the discussions with customers, did certain rate design principles become evident?

A. Yes. A primary objective of both customers and BPA was that costs be allocated to the customers who caused those costs to be incurred. In developing the proposed TRM, we followed six cost allocation principles. These principles also are proposed to be used to provide guidance for addressing circumstances that may arise during the term of the Regional Dialogue Contracts for any new costs that are not specifically addressed in this TRM.

Q. What is the first principle, and what is its intent?

A. Tiering is a ratemaking construct implemented through an allocation of costs rather than an allocation of power. See TRM section 2.1.

This principle is intended to communicate that tiering is limited to ratemaking. It does not convey rights to Federal power for a customer’s load in excess of its Net Requirement. Nor does it imply any customer ownership of the output of the Federal generating system in whole or in part. It also means that BPA will sell Federal system power to meet a customer’s Net Requirement; BPA is not selling Tier 1 power or Tier 2 power. BPA is also not establishing a separate business to sell Tier 2 power; nor are financial reserves separately established for the tiers.

Q. What is the second principle, and what is its intent?

A. Tier 1 Costs will be kept separate and distinct from Tier 2 Costs. Tier 1 Costs will be recovered through Tier 1 Rates. Tier 2 Costs are not to be recovered through the Tier 1 Rates except when necessary to ensure BPA’s cost recovery during the Rate Period or to conform to court ruling, or as otherwise provided for in sections 12 and 13 of the TRM. Id.
BPA is trying to provide certainty that the costs of BPA’s Tier 1 System Resources will be allocated to Tier 1 Rates and the costs of most future resources will be allocated to Tier 2 Rates. However, there are circumstances that might arise during the term of the Regional Dialogue Contracts that require Tier 2 Costs to be shifted to customers that purchase at Tier 1 Rates. We believe the probability of any of these circumstances occurring is very low, but their possibility cannot be ignored. We must allow for their occurrence by recognizing the exception. Should such an exception occur, BPA would identify the proposal to reallocate Tier 2 Costs in the relevant rate case, consistent with the procedures described in section 12 and 13, for changes that can be made only to ensure cost recovery or to comply with a court ruling. Parties to that rate case will be allowed to offer alternative cost recovery mechanisms.

Q. What is the third principle, and what is its intent?

A. Individual Tier 2 Cost Pools are to be kept separate from one another; customers paying the costs of one Tier 2 Cost Pool will not be responsible for paying the costs of another Tier 2 Cost Pool. Id.

Just as with Tier 1, BPA’s intent is to provide certainty that the costs of specific resources would be allocated to specific Tier 2 Rates and would continue to be allocated to the same Tier 2 Rates and to no others.

Q. Why is there no cost shift exception in the third principle as with the second principle?

A. We believe that the exception in the first principle is sufficient to address the rare circumstances that might occur that would give rise to shift costs away from their intended Cost Pool.

Q. What is the fourth principle, and what is its intent?

A. BPA will achieve the separation of costs between Tier 1 and 2 Cost Pools and among Tier 2 Cost Pools through the ratemaking process, and the separation will not affect the operation or dispatch of the FCRPS. BPA will use available
resources to serve system load in the most efficient and cost effective manner possible, without considering the ratemaking aspects of tiering. *Id.*

Similar to principle 1, this principle limits tiering to ratemaking. Tiering is not intended to change BPA’s operation or dispatch of resources. In operating the Federal system, BPA will not identify or assign resources to Tier 1 or Tier 2 and will not be limited to only using Tier 1 System Resources to serve customers purchasing at Tier 1 Rates. Similarly, resources whose costs are allocated to Tier 2 Cost Pools will not be limited to serving Tier 2 Loads.

Q. What is the fifth principle, and what is its intent?

A. The ratemaking separation of costs between the tiers and among the Tier 2 Cost Pools will not be necessarily the same as BPA’s accounting treatment of the costs because tiering is a ratemaking methodology, not an accounting practice. When differences arise between ratemaking and accounting, the ratemaking allocations determined in accordance with section 2 of the TRM shall govern BPA’s ratemaking. *Id.*

This principle allows the ratemaking principles to take precedence over BPA’s accounting conventions as they may change over time. For example, if BPA’s accounting system mixes the cost of certain Tier 2 System Resources into the same accounts, BPA will separate those costs in ratemaking to properly allocate the costs to the appropriate Tier 2 Cost Pools. Another example might be that a cost account might include costs that BPA determines that Slice customers are not responsible for paying. In this case, BPA will separate the costs in ratemaking to properly allocate the costs to the Tier 1 Cost Pools.

Q. What is the sixth principle, and what is its intent?

A. BPA’s allocation of costs between the Composite and Non-Slice Cost Pools will recognize the types of costs distinct to the type of service each group receives and
how they pay for that service. Composite costs will not include the costs of converting resource output into load service, such as Balancing Power Purchases, and the costs of risk mitigation not directly attributable to Slice purchasers.

Because Slice customers purchase surplus power directly from BPA through the Slice product, the Composite Cost Pool will not be allocated the revenues and costs of BPA’s surplus marketing, such as secondary revenue credits, costs of wheeling secondary power, and any judgments and settlements related to those transactions.

The administrative costs of surplus marketing (primarily staffing costs) will be allocated to the Composite Cost Pool. \textit{Id.}

This principle is intended to guide the allocation of costs between Slice and Non-Slice customers. Slice customers should not be responsible for paying the types of costs identified in this principle. To the extent a new cost arises that meets or closely resembles these types of costs, they would be allocated to the Non-Slice Cost Pool. If they do not match this principle, they would be allocated to the Composite Cost Pool and be paid by all Tier 1 purchasers.

\textbf{Q.} Are there other goals BPA is trying to achieve with this rate design?  
\textbf{A.} BPA and the customers analyzed how much changing the rate design would shift costs between PF customers. Looking at information used in the WP-07 Final Proposal, BPA and the customers made an assessment that using the proposed new rate design rather than what was actually used in the WP-07 rates would not generally cause rate increases of more than five percent for a particular customer.

\textbf{Q.} What is the importance of the five percent rate impact threshold for future rate cases?  
\textbf{A.} It has no bearing on quantifying rate impacts in any other context. The five percent impact threshold was used solely within the development and assessment of alternative rate designs. The threshold was based on one particular data set, including a specific
revenue requirement and load forecast. The threshold was not intended to be used in any other context.

Q. How do tiered rates affect customer rate levels?

A. We expect the impact of tiering to affect individual customers differently. This is an intended result because it would send price signals to the customers about the effects of their load growth on BPA’s costs. However, we would expect a customer that grows at the average rate of growth for BPA’s entire load would pay about the same amount under tiered rates as under melded rates. Customers that grow greater than average would see its power costs grow faster under tiered rates than under melded rates, while less than average growers would see its power costs grow slower under tiered rates.

Section 8: Other Issues

Section 8.1: Slice Rates

Q. Would the TRM change any aspect of the existing Slice Rate Methodology?

A. The TRM would replace the existing Slice Rate Methodology with the Tier 1 cost treatments and put the Slice rate and pricing on the same basis as other power products sold at Tier 1 Rates. The definition of Tier 1 System Resources in the TRM would replace the “Slice System Resources.” The Slice Product Costing and True-Up Table would be replaced by the Cost Allocation Table, TRM Table 2.1. The Cost Allocation Table identifies to which Tier 1 Cost Pool specific costs would be allocated. Another change is that there would be two rate components charged for service to Slice purchasers: the Composite Customer Rate and the Slice Customer Rate. A further change is that the TRM would allow a Slice customer, as well as other customers, to request the Composite Customer Charge to be shaped during a year rather than to be a constant flat charge each month throughout the year (see Fisher et al., TRM-12-E-
We do not believe that these changes materially alter the provisions in the Slice Rate Methodology.

Q. Are there other more material changes to the Slice Rate Methodology proposed in the TRM?

A. Yes. The existing Slice contract provides the Slice customers with a right to audit BPA’s annual Slice True-Up Adjustment, and a settlement agreement allows a form of dispute resolution if Slice customers disagree with the assignment of costs to them. The TRM would replace these contract provisions with its own provisions on verification of identified costs for the Tier 1 Rates and procedure for resolving disputes over allocation of costs. The right to audit costs would be replaced with a cost verification process. The right to dispute the allocation of costs to Slice customers would be timed differently, in that the TRM proposes that any adjustment resulting from a dispute would be reserved for the next general section 7(i) rate proceeding and would not occur after the settlement dispute resolution process.

Q. Why do you propose replacing the audit with the verification process?

A. The provisions of the verification process would provide both Slice and non-Slice customers the ability to review and challenge BPA’s cost allocation decisions. It would serve all parties best to have a single forum for discussing the proper allocation of costs and credits between Slice and non-Slice Cost Pools, and between Tier 1 and Tier 2 Cost Pools. That forum is more efficiently and logically the relevant rate case. Rate cases have not historically "looked backward" at cost allocations in the prior Rate Period, but we propose that this limited ex post review be added to future cases.

Q. Does this mean that rate cases would be the venue for review of cost allocation?

A. Yes. The relevant rate cases would be the venue for addressing issues related to cost allocation, particularly if a new cost or revenue is accrued during a Rate Period that had not been anticipated when the Cost Pools were determined.
Q. Why would the relevant rate case be the venue for addressing issues related to cost allocation?

A. Under the TRM, two fundamental differences in conditions would call for a different approach to addressing these legitimate interests of customers. First, the new rate design and contracts increase the likelihood that all customers, not just Slice customers, would have a keen interest in ensuring that such post-rate case allocations are performed properly. Currently, all customers are interested in the allocation between Slice and non-Slice rates. Under the proposed TRM, all customers would also want to be sure that new costs are correctly allocated between Tier 1 and Tier 2 Cost Pools. Many customers would also have an interest in the proper allocation of costs among different Tier 2 Cost Pools. Second, the days of five-year Rate Periods are very likely gone, and with that change, the frequency of significant new costs appearing in the Slice True-Up will decline because the time between rate cases will be shorter.

Section 8.2: Shared Rate Plan

Q. The TRM proposes a Shared Rate Plan (SRP) (TRM section 7; see also Fisher et al., TRM-12-E-BPA-06, section 4). Why is there a 500 aMW limit on the participation in this rate design?

A. We propose to limit the amount of load covered under the SRP. Without a limit, the SRP could subvert the general concept of tiered rates because the SRP melds the costs of new Federal resources with the costs of the existing Federal system and shares these costs within a customer pool. Without a participation limit, this concept could mask actual incremental costs and thus mask the important price signals that will encourage regional infrastructure, particularly conservation. Therefore, we propose the limit to restrict the SRP to BPA’s smallest customers who have committed to purchase their entire load from BPA through the term of the CHWM Contracts. We expect that the price signals from
tiered rates would have a much smaller impact on their purchasing and infrastructure
development decisions. Therefore, we believe that it is reasonable to restrict access to the
SRP to these customers.

Section 8.3: Direct Service Industry Rates

Q. Do you expect BPA to incur and recover costs through rates that result from providing
service benefits to Direct Service Industrial (DSI) customers after the year 2011?

A. Yes, if BPA determines it is appropriate. BPA is still exploring alternative approaches
for providing service benefits to the DSIs after their current contracts expire at the end of
FY 2011. These alternatives include 1) providing power through power sales contracts
with an optional financial valuation mechanism similar to the existing FY 2007-2011 DSI
contract; 2) providing some level of actual power sales to the DSIs under a Regional
Dialogue Contract; and 3) other approaches as they may arise. If BPA elects to provide
actual power sales to the DSIs and it becomes necessary to purchase Augmentation (see
TRM section 3.2.1.4), these Augmentation costs would be allocated to Tier 1 as FBS
costs (see TRM section 10.3).

Q. Does BPA intend to establish rates under the TRM that would apply to power sold by
BPA to DSIs under future power sales contracts?

A. We are not proposing so, but the TRM would not preclude such rates. TRM section 10.3
proposes that any sale to the DSIs “would be priced at the Industrial Firm Power (IP) rate
determined in accordance with section 7(c). BPA does not intend to tier the IP rate, but it
is not prohibited by this TRM.”

Section 8.4: Section 7(b)(2) Rate Test

Q. Does the TRM propose any changes be to the Northwest Power Act’s section 7(b)(2) rate
test to accommodate tiered rates?
A. No changes are proposed to the section 7(b)(2) rate test to accommodate tiered rates.

Q. *Would the TRM affect the section 7(b)(2) rate test in the future?*

A. We do not expect it to. Tiering is primarily a PF rate design matter. Generally, BPA applies rate design to the PF rate after performing the 7(b)(2) rate test. For example, the current PF rate design contains two energy rates, a demand rate, a Slice rate, and a load variance rate. These rate designs are applied after the 7(b)(2) rate test. The rate test is performed on an average annual cost basis, and the TRM does not propose to change how the rate test is conducted. The rate test would continue include all of BPA’s costs allocated to the PF rates without respect to tiered cost pools. Additionally, the TRM does not prohibit changes to how the rate test is conducted.

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Section 8.5: Capacity Acquisitions

Q. *Would BPA capacity acquisitions be limited, like the energy acquisitions (also known as Augmentation) are limited by the Policy?*

A. No. The proposal recognizes that the region’s capacity situation is changing and that the Federal system is becoming more capacity constrained. Increased uses of the system, such as integrating wind, the possibilities of our customers’ loads becoming “peakier” (*i.e.*, decreasing load factors), and losses of flexibility in the Federal system are expected to require BPA and the region to take a look at the available capacity from the system and other sources. To this end, BPA is currently focusing on its capacity needs in several forums: BPA began a resource acquisition planning program this year; BPA committed in the wind integration rate case settlement to study uses of system capacity; and BPA will actively participate in the Northwest Power and Conservation Council’s 6th Power Plan. In recognition of the growing capacity constraints, we have designed the TRM proposal so that, to the extent possible, the marginal cost of serving load growth
for both energy and capacity would be allocated to those who are creating the increased needs.

Q. How will capacity costs be allocated under the TRM?

A. As we note above, the TRM would treat all deliveries to serve customer above-RHWM loads as a flat annual block of power (see section 3 above) within Rate Periods. Consequently, any loads that are greater than the forecast purchase of power at Tier 1 and Tier 2 Rates would be recovered through the Load Shaping and Demand Charges under the Tier 1 Rate. Therefore, any capacity cost incurred by BPA to meet the variance in a customer’s load would be allocated to the Non-Slice Cost Pool to be consistent with the rate design principles and would be recovered in the rates to non-Slice customers.

Furthermore, any capacity cost incurred by BPA to meet the obligations placed on the Federal system by, for example, transmission services or resource integration, would be allocated to the Composite Cost Pool because it would be a general obligation of the Federal system. However, we also propose that BPA would price the service to these obligations at the marginal cost of the service and credit the revenues recovered from the sale of the services to the Composite Cost Pool.

Section 9: TRM Sections 12 and 13: Criteria, Conditions, and Processes for Changing or Re-Opening the TRM

Q. What is proposed in TRM sections 12 and 13?

A. Sections 12 and 13 of the TRM would set forth the procedural protections for customers covering changes to the TRM. TRM section 12 proposes the criteria and conditions for a TRM change or re-opening. TRM section 13 proposes the specific processes for changing or re-opening the TRM.

Q. What, generally speaking, is the purpose for proposing sections 12 and 13 in the TRM?
As indicated earlier in this testimony, the tiered rates proposal seeks to afford both customers and BPA long-term certainty and predictability in terms of the rate design that will govern establishment of BPA’s rates for customers with CHWM Contracts for the next 20 years. If adopted, it will be BPA’s policy to revise the TRM as little as possible. TRM sections 12 and 13 are key components of providing that long-term certainty and predictability. Section 12 proposes what in the TRM could subsequently be changed, the categories of types of change by purpose, and the predicates for various categories of change. Section 13 proposes the procedures that would apply to ensure that the TRM is changed only as provided in Section 12.

Q. If BPA intends to provide long-term certainty and predictability with the TRM, why would section 12 provide for changing the TRM?

A. BPA has the responsibility under section 7(a)(1) of the Northwest Power Act to establish, and periodically review and revise if necessary, BPA’s power rates to recover its costs. Other substantive subsections of section 7 concern rates for various customer classes, cost allocation, and rate design. Section 9(b) of the Northwest Power Act provides that the Administrator shall timely implement the Act in a sound and businesslike manner. In order to satisfy these directives, we propose that BPA must provide for the TRM to be able to be changed in the limited manner provided in TRM section 12.

Q. Under what conditions could the TRM be changed or re-opened?

A. The conditions would generally fall into four categories. First, the proposed TRM clarifies that any aspect of the TRM may be changed if necessary to ensure cost recovery or to comply with a court ruling. Second, certain specific provisions may be changed only to ensure cost recovery or to comply with a court ruling. For purposes of the TRM, the term “court ruling” includes a ruling of the Federal Energy Regulatory Commission that disapproves or remands a BPA rate based on the TRM. The third general area is...
comprised of changes that would be considered unintended consequences of the TRM.

The fourth area encompasses changes that are considered improvements or enhancements. Each of these is further described below in this section of the testimony. In addition, TRM section 12 specifies that certain actions to implement the TRM are not considered changes to the TRM. These are described and listed above in section 5 of this testimony. In any event, because the TRM is a rate construct, any changes must be made pursuant to the procedural requirements of section 7(i) of the Northwest Power Act or its successor.

Q. Please relate the categories of change in TRM section 12.1 to the statutory sections you referred to above.

A. The proposed TRM provides in section 12.1 that anything in the TRM may be changed if necessary to assure cost recovery or respond to court ruling. This assures, first, that BPA could satisfy its statutory responsibility under section 7(a)(1) to, if necessary, revise rates to recover BPA’s costs. If BPA were to determine that something in the TRM stood in the way of BPA’s cost recovery, the TRM could be changed to cure the problem. Section 12 provides that even in that instance, BPA must consult with customers and explain what steps it has taken to avoid having to make the change. We believe this is consistent with, and reflective of, sound business principles. It assures customers that BPA is continuing to honor the customers’ need for certainty and predictability, while assuring cost recovery. This section would also ensure that in the event a future court ruling necessitates BPA changing the TRM, BPA will have retained the ability to do so. We think that it is prudent to retain to BPA the ability to respond, and that this ensures BPA’s ability to timely implement the Northwest Power Act in a sound and businesslike manner, consistent with section 9(b).

Q. Please relate the categories of change in TRM section 12.2 to the statutory sections you referred to above.
A. Section 12.2 of the proposed TRM provides that certain sections of the TRM may be changed only if necessary to ensure cost recovery or respond to court ruling. The identified sections reflect the core or fundamental building blocks of tiered rates. Because these sections are fundamental, it is consistent with sound business principles to have these sections be immune from change except in the narrowest of circumstances. Therefore, these areas would not be subject to change due to unintended consequences or for enhancements or improvements.

Q. Please relate the categories of change in TRM section 12.3 to the statutory sections you referred to above.

A. Section 12.3 of the proposed TRM provides that certain sections of the TRM, other than those identified in Section 12.5, could be changed if necessary to avoid unintended consequences that would put at risk the policy goals underlying the TRM. Since the TRM deals with cost recovery and court ruling elsewhere, section 12.3 covers an unanticipated and extraordinary type of situation where something in the TRM turns out to be seriously problematic to the point of frustrating the policy goals of the TRM. We recognize that we is proposing to fundamentally change its current rate design, e.g., the development of the Customer Charges to collect the majority of costs allocated to the Tier 1 Cost Pools rather than primarily through charges for heavy load hour and light load hour energy. While we have worked with customers to develop rate designs that should work over time, it is possible that BPA may find results that were unexpected, i.e., unintended consequences that put at risk the policy goals underlying the TRM. In this specific and narrow circumstance, we believe it is prudent and in BPA’s and the customers’ best interest to preserve BPA’s ability to change the TRM if necessary to deal with these unintended consequences.

Q. Please relate the categories of change in TRM section 12.4 to the statutory sections you referred to above.
A. Section 12.4 of the proposed TRM provides that the TRM may be changed to improve or enhance the TRM. Given this purpose, and the protections provided elsewhere in section 12, section 12.4 focuses on refinements that would improve the TRM. We believe allowing for the possibility for this kind of change makes good business sense and will not disturb the certainty and predictability afforded by the TRM.

Q. Are those categories of changes the only kind of change propose by TRM section 12?

A. No. The changes identified above would be changes to the language of the TRM. Customers’ representatives raised the concern that the TRM should provide assurance against BPA ignoring the requirements of the TRM and effectively thereby changing the TRM. At the same time, we recognize that there will always be ambiguity in complex undertakings such as the TRM, and we did not want to have interpretative disputes be subject to the same rules as apply to changes. Therefore, at the beginning of section 12, the proposed TRM states that a change would mean a change to the actual language of the TRM or a patent disregard or omission of something that is unambiguously required by the TRM. It would not refer to questions of interpretation or implementation of the TRM. We think this provides ample protection against BPA ignoring the requirements of the TRM and effectively thereby changing the TRM.

Q. What assurance do customers have that BPA would not undercut all of these protections by changing or ignoring them in the future?

A. We believe the assurances are very strong. Concurrent with establishment of the TRM, BPA staff is developing CHWM Contracts. We expect those contracts to contractually commit that BPA would change the TRM only in accordance with the procedures of TRM sections 12 and 13. In other words, the Administrator is ceding his discretion to change the TRM except to the extent provided in the TRM. So, in order to change any of the protections in section 12, BPA would have to first satisfy the procedural requirements...
of section 13 as they would pertain to change for purposes of cost recovery, court ruling, unintended consequences, or improvements or enhancements.

Q. Would TRM section 13 serve any other purpose?

A. Yes. Section 13 would provide the dispute resolution procedures that BPA must follow in order to make a change to the TRM and spells out the different processes that would apply to different changes. Section 13 also would contains sections about the process for disputes about whether BPA had proposed a change to the TRM when BPA is implementing the TRM, and disputes over how BPA is interpreting the TRM outside a rate case.

Q. How, if at all, would section 13 reflect the policies you identified as informing the various categories of change identified in TRM section 12?

A. We think very well. When it comes to the changes for cost recovery or court ruling, the procedures would reflect the policy of the law that it is the Administrator’s responsibility, his or her statutory charge, to establish rates to ensure cost recovery, and do so in a lawful fashion. In recognizing the historical importance of the TRM and its goal of certainty and predictability, we have proposed for the rate case Hearing Officer to make non-binding determinations of whether BPA’s proposal to change the TRM is necessary to ensure cost recovery or respond to court ruling pursuant to section 12.1 or 12.2, and/or whether the proposed change was unreasonably disproportionate to what would be needed to comply with the court ruling or to ensure cost recovery, compared to the alternative proposal(s), if any, offered by the rate case parties. This third-party opinion would, as a political matter, expose the Administrator’s reasoning and decision to extra scrutiny, making it more likely that the Administrator would only avail himself of the right to change the TRM for cost recovery and to respond to court ruling when absolutely necessary.
This protection would be provided as well when BPA disputes whether it is changing the TRM. The Hearing Officer would be empowered to determine if BPA was changing the TRM. If, notwithstanding BPA’s disagreement, the Hearing Officer determined a change was being made, then the change could not be made and the matter would be excluded from the record, unless BPA argued the change is necessary for cost recovery.

When it comes to change for unintended consequences, section 13.2 would provide for the Hearing Officer to determine whether BPA’s proposal to change the TRM pursuant to section 12.3 was necessary to avoid significant harm due to consequences not anticipated when the TRM was put place and whether the value of the proposed change would outweigh any harm created by the change. For improvements and enhancements, section 13.3 would provide for the Hearing Officer to determine whether BPA’s proposal to change the TRM pursuant to section 12.4 was appropriate because 1) the change would improve or enhance implementation of the TRM in a way that would continue to effectuate its purposes but be more cost-effective and efficient, customer responsive, may be readily implemented, or capable of fulfilling the TRM’s purposes; and 2) the value of the proposed change would outweigh any detriment created by the change.

Finally, if there would be a dispute between rate cases whether BPA was changing the TRM, section 13.7 would provide for a binding third-party determination of the matter. This would assure changes would be made only in accordance with the requirements of Northwest Power Act section 7(i) and TRM sections 12 and 13.

Q. Do you believe that the procedures of TRM section 13 would adequately protect customers from changes by the Administrator to the TRM?

A. We believe the proposal affords customers as much protection as appropriate when it comes to changes for cost recovery and court ruling. As we indicated earlier, it is the
Administrator’s statutory responsibility to establish rates to assure cost recovery, and do so in a lawful fashion.

When it comes to changes for unintended consequences and improvements or enhancements, we sought to strike a balance between customers’ need for predictability and certainty with the recognition that there are reasons why a particular kind of change may be required.

Q. Did you consider any alternatives to TRM section 13?
A. Yes. Attachment A to this testimony presents alternative language that we considered.

Q. Why did you not propose this language?
A. We understand the customers’ desire for a durable commercial relationship. However, we believe some of the alternatives presented by customers and the alternative presented in Attachment A went too far. BPA must balance many aspects of its business relationship within the legal and policy constraints that exist. Many of the determinations that customers requested, such as arbitration for HWM, Net Requirement, and resource capability determinations are fundamentally decisions that are appropriately made by BPA, not by a third party. These tend to be fairly technical determinations. We believe it would be very difficult to find a third party who was knowledgeable and would be acceptable to all parties. This would add additional expense and time and could be very administratively burdensome. In addition, the Administrator must retain the ability to make decisions about ratesetting and cannot delegate these to a third party.

We recognize the importance of these determinations and that many of these decisions will affect other customers. That is why we have proposed a process that is more transparent than the current processes. It is also why we are willing to propose the Attachment A mini-trial process. A mini-trial would allow the Administrator to hear the concerns of all who present evidence. The requirement that a certain percentage of
customers petition regarding the issue would help limit the number of issues that come
to the Administrator through this process and thus limit its administrative burden.

Q. Why are you unwilling, in this instance, to propose referring the matter to a third-party
neutral for a binding decision?

A. The TRM is a rate construct, and we understand that all rate matters must be determined
in a section 7(i) rate proceeding.

Q. What do you have to say about the TRM and customer contracts based on existing
statutory requirements?

A. TRM section 12 would also contain language that BPA would not warrant or represent
that the TRM or contracts are immune from subsequently enacted legislation, or that the
TRM or contracts would be immune from costs imposed by court order or agency
regulations of a general and public nature. The effect of later-enacted legislation on
earlier agency actions would present complex legal questions and is an issue that the
courts are ultimately in the best position to resolve. We do not want BPA to be seen as
warranting or representing that the TRM has a legal effect that it would not have or that
BPA would not have the authority to confer. Similarly, we wish to be clear neither that
the TRM nor the CHWM Contracts should be construed as being immutable, particularly
if court order or agency regulations of a general and public nature, such as a universal
Btu tax or a requirement that all utilities achieve some specified amount of energy
efficiency, would require change. We have tried to be clear that BPA must maintain its
ability to recover all costs appropriately borne by it.

Q. Would these provisions run counter to or somehow trump the protection afforded
customers by the BPA Refinancing Act of 1996?

A. No, that specific legislation is secured by BPA’s contracts and will, as a consequence, be
binding on BPA for the term of the contracts, as Congress intended. The BPA
Refinancing Act of 1996 requires BPA to offer contract language that essentially has the
effect of precluding BPA from charging rates for old capital investments that are not cost-based. Any new contract BPA offers as long as that law is in effect will secure the cost-based value of the system for our customers by including the statutory language. The statutory language incorporated in the contract provides in part that “apart from charges necessary to repay the new principal amount of an old capital investment as established under subsection (b) of this section and to pay the interest on the principal amount under subsection (c) of this section, no amount may be charged for return to the United States Treasury as repayment for or return on an old capital investment, whether by way of rate, rent, lease payment, assessment, user charge, or any other fee.”

Q. Does this conclude your testimony?

A. Yes.
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Attachment A

Alternative TRM Section 13

13 Processes for TRM change or reopening

13.1 Process Generally Applicable to Any TRM Change or Revision

No change to the TRM may be made without complying with the procedural requirements of section 7(i) of the Northwest Power Act or its successor.

In the event that this TRM provides that an input to establishment, administration, or implementation of the TRM (e.g., CHWM determination process and results, RHWM Process and results) shall be as determined pursuant to contract or process outside a rate case, then any dispute concerning determination of that input shall not be subject to any of the procedures of this section 13, except as specifically provided for. Similarly, no billing disputes shall be subject to any of the procedures of this section 13 except as specifically provided for.

13.2 Process for Section 12.3 Change to TRM ("Unintended Consequences Change")

In the event that BPA, upon its own or a customer’s initiative, wishes to propose to make a change as provided for in section 12.3 (unintended consequences that put at risk the policy goals underlying the TRM) that affects only customers with CHWM Contracts (e.g., it does not concern programmatic responsibilities such as fish and wildlife or the Residential Exchange, and does not involve the DSIs, IOUs, or customers taking service under non-CHWM contracts), BPA may propose such change only after complying with the requirements of this section. Other section 12.3 proposed changes (i.e., those that do affect other parties and interests) may only be proposed consistent with the procedural requirements of section 7(i) of the Northwest Power Act or its successor.
Before BPA proposes such a change that affects only customers with CHWM Contracts, BPA will notify all preference customers of the change it would like to propose and why it believes 1) the change will avoid significant harm due to consequences not anticipated when the TRM was put in place; and 2) the value of the proposed change outweighs any harm created by the change. The notice will specify the date by which the customer may object to BPA making the proposal and the means for the customer registering its objection.

BPA may propose the change unless it is objected to by Tier 1 preference purchasers totaling both 1) at least 70 percent of such purchasers (utility count), and 2) Tier 1 preference purchasers representing at least 50 percent of the sum of the CHWMs of all Tier 1 preference purchasers. In determining the total, BPA shall count each abstention and absence of a vote as a vote that the customer does not object to the proposed change. In the event that the requisite number and CHWM percentage object to BPA’s proposed change, BPA shall not propose the change. In the event the requisite number and CHWM percentage do not object to BPA’s proposed change, BPA may propose the change in accordance with the procedural requirements of section 7(i) of the Northwest Power Act or its successor.

13.3 Process for Section 12.4 Improvements and Enhancements
A section 12.4 change may be proposed only in accordance with the requirements of this section. In the event BPA, or a group comprised of not less than 45 percent of the Tier 1 preference purchasers (utility count), wishes to propose in a section 7(i) hearing that the Administrator make a section 12.4 improvement or enhancement to the TRM, BPA or the group may propose such change only after complying with the requirements of this section.

Before BPA or the group proposes a change under section 12.4, BPA will notify all preference customers of the change it or the group would like to propose and why BPA or the group
believes 1) the change will improve or enhance implementation of the TRM in a way that will continue to effectuate its purposes but be more cost-effective and efficient, customer responsive, readily implementable, or capable of fulfilling the TRM’s purposes; and 2) the value of the proposed change outweighs any detriment created by the change. The notice will specify the date by which the customer may express its support for BPA’s or the group’s proposal, and the means for registering its support.

BPA or the group may propose the change only if it is approved by Tier 1 preference purchasers totaling both 1) at least 70 percent of such purchasers (utility count); and 2) Tier 1 preference purchasers representing at least 50 percent of the sum of the CHWMs of all Tier 1 preference purchasers. In determining the total, BPA shall count each abstention and absence of a vote as a vote that the customer does not approve the proposed change. In the event that the requisite number and CHWM percentage do not express support of BPA’s or the group’s proposed change, BPA or the group, as the case may be, shall not propose the change. In the event the requisite number and CHWM percentage support BPA’s proposed change, BPA shall propose the change in accordance with the procedural requirements of section 7(i) of the Northwest Power Act or its successor. In the event the requisite number and CHWM percentage support the group’s proposed change, the group shall raise the proposed change in accordance with the procedural requirements of section 7(i) of the Northwest Power Act or its successor.

13.4 Process for TRM Changes to Assure Cost Recovery or Respond to Court Ruling (pursuant to sections 12.1 and 12.2)

This section applies when BPA proposes to change the TRM to assure cost recovery or respond to court ruling pursuant to section 12.1 or 12.2 and some customers believe that BPA’s proposal to change the TRM is not necessary to assure cost recovery or respond to court ruling pursuant to section 12.1, and/or that the proposed change is unreasonably disproportionate to what is needed.
to comply with the court ruling or to ensure cost recovery, compared to the alternative proposal(s), if any, offered by the Tier 1 preference purchasers.

a. In this event, upon written petition by Tier 1 preference purchasers totaling both 1) at least 70 percent of such purchasers (utility count), and 2) at least 50 percent of the sum of the CHWMs of all Tier 1 preference purchasers filed within twenty (20) working days after submission of BPA’s initial rate proposal, the rate case Hearing Officer is empowered and required to determine, consistent with the rate case schedule, whether BPA’s proposal to change the TRM is necessary to assure cost recovery or respond to court ruling pursuant to section 12.1 or 12.2, and/or whether the proposed change is unreasonably disproportionate to what is needed to comply with the court ruling or to ensure cost recovery, compared to the alternative proposal(s), if any, offered by the Tier 1 preference purchasers.

b. If BPA disagrees with the conclusion of the Hearing Officer, BPA may within five (5) working days of the Hearing Officer’s decision petition the Hearing Officer for a mini-trial before the Administrator. If such a petition is timely made, the Hearing Officer shall expeditiously schedule, consistent with the rate case schedule, a mini-trial before the Administrator over whether BPA’s proposed TRM change is in fact required to assure cost recovery or respond to a court ruling and/or whether the proposed change is unreasonably disproportionate to what is needed to comply with the court order or to ensure cost recovery, compared to the alternative proposal(s), if any, offered by the Tier 1 preference purchasers.

13.5 Process for Disputes Over Whether BPA Has Proposed a TRM Change

This subsection applies when both of the following conditions are met: 1) a party to a BPA rate proceeding alleges that a BPA proposal constitutes or includes a change to the TRM as defined in section 12, and 2) BPA believes that its proposal is not such a change.
If Tier 1 preference purchasers totaling both 1) at least 70 percent of Tier 1 preference purchasers
(utility count), and 2) at least 50 percent of the sum of the CHWMs of all such purchasers file a
petition with the Hearing Officer within 10 working days after submission of BPA’s initial case
alleging that a BPA proposal constitutes or includes a change to the TRM that has not been
acknowledged and proposed by BPA as a change pursuant to section 12 and that the customers
oppose the change, the rate case Hearing Officer is empowered and required to determine
whether the matter proposed by BPA is a change in the TRM as defined in TRM section 12. If
the Hearing Officer concludes that the matter proposed by BPA is not a change in the TRM as
defined in section 12, that conclusion is binding on all parties.

If the Hearing Officer concludes that the matter proposed by BPA is not a change in the TRM as
defined in section 12 or that the matter has been proposed by BPA as a change pursuant to
section 12, that conclusion is binding on all parties for purposes of this section 13.5, and the
Hearing Officer shall take no further action pursuant to this section.

If the Hearing Officer concludes that the matter proposed by BPA is a change to the TRM that
has not been proposed by BPA as a change pursuant to section 12, but BPA subsequently alleges,
no later than 5 working days after the Hearing Officer announces his or her conclusion, that the
proposed change is necessary to assure cost recovery or respond to a court ruling pursuant to
section 12.1 or 12.2, then the Hearing Officer shall make the determinations called for in
paragraph a and otherwise proceed as provided pursuant to paragraph b and section 13.6.

If the Hearing Officer concludes that the matter proposed by BPA is a TRM change that has not
been proposed by BPA as a change pursuant to section 12, and BPA does not timely allege that
the proposed change is necessary to assure cost recovery or respond to a court ruling, then the
Hearing Officer shall strike all matter concerning the proposed change from the record, and that shall be conclusive on BPA and the parties for purposes of that case.

13.6 Mini-Trial Regarding Proposed TRM Change

If the Hearing Officer schedules a mini-trial before the Administrator, as described in sections 13.2, 13.3, 13.4, and 13.5, the following procedures will apply. A mini-trial to the Administrator shall be a part of the rate case, shall be presided over by the Hearing Officer, and shall consist of the following:

1) Parties shall file statements of position that summarize their arguments as to why the Hearing Officer’s decision should be upheld or reversed, whether in whole or in part. The Hearing Officer shall encourage parties with like positions to consolidate their submissions.

2) Oral presentations, not to exceed two days in total, shall be scheduled before the Administrator. The order of presentation shall be the Hearing Officer, parties in opposition to the Hearing Officer’s decision, and parties in support of the Hearing Officer’s decision. Parties’ presentations may consist of testimony, oral argument, or a combination of both. The Administrator may ask any questions, or engage in any discussion, with any of the presenters that he or she deems appropriate.

3) Within five (5) working days of the oral presentations, the Administrator shall provide the Hearing Officer a written statement that the Administrator either adopts or does not adopt the Hearing Officer’s decision. If the Administrator adopts the Hearing Officer’s decision, that shall be conclusive on BPA for remaining purposes of the rate case hearing. If the Administrator does not adopt the Hearing Officer’s decision, the Administrator shall summarize the basis for the decision, but may elect to change the decision at the conclusion of the rate case hearing in the Administrator’s Record of Decision.
The Hearing Officer is further empowered to establish and employ such procedures as deemed necessary or appropriate, consistent with the rate case schedule, to efficiently, fairly, and impartially make the determinations under this section and under section 13.2, 13.3, 13.4, or 13.5. The decision of the Hearing Officer shall be based upon a consideration of the record on the issues, and it shall include findings of fact and conclusions of law, with reasons and bases therefore, upon each material issue of fact, law, or discretion presented on the record. The Hearing Officer may at any time render an accelerated decision in favor of a party as to any or all parts of the issues, without further hearing or upon such limited additional evidence, such as affidavits, or briefing as he or she may require, if no genuine issue of material fact exists and a party is entitled to judgment as a matter of law.

13.7 Process Applicable to Alleged BPA TRM Change Outside a Rate Case

In the event a preference customer believes that a BPA action changes or constitutes an attempt to change the TRM outside a rate case held pursuant to section 7(i) of the Northwest Power Act or its successor, it shall promptly, but no later than five (5) working days after it learns of BPA’s action, notify BPA in writing of its belief and the general basis for its belief. If BPA agrees with the customer, it shall not make the change except pursuant to section 13.1. If BPA disagrees with the customer, BPA will notify customers and interested parties of the notice within five (5) working days of its receipt, and shall, if possible, provide a summary of its position why the action is not a change or attempted change, and shall promptly convene a public meeting with customers and interested third parties to discuss the notice and BPA’s action.

If, within five (5) working days after the conclusion of the public meeting held pursuant to the previous paragraph, 1) at least 70 percent of Tier 1 preference purchasers (utility count), and 2) Tier 1 preference purchasers representing at least 50 percent of the sum of the CHWMs of all
such purchasers do not indicate that BPA’s action changes or constitutes an attempt to change the TRM, then BPA shall proceed in the ordinary course. In determining the total, BPA shall count each abstention and absence of a vote as a vote that the customer does not object to the proposed change.

If, within five (5) working days after the conclusion of the public meeting held as described above in this section, 1) at least 70 percent of Tier 1 preference purchasers (utility count), and 2) Tier 1 preference purchasers representing at least 50 percent of the sum of the CHWMs of all such purchasers indicate that BPA’s action changes or constitutes an attempt to change the TRM, then BPA shall refer the matter to a third-party neutral for a binding decision on the matter.

The third-party neutral shall be selected at random from a roster of neutrals maintained by BPA, and selected by BPA in consultation with Public Power Council representatives, for the purpose of settling disputes regarding whether a BPA action is a change or attempted change in the TRM.

Within five (5) working days of announcement of the neutral’s appointment, any customer may submit a written submission to the neutral, BPA, and other customers in support of its position that BPA’s action constitutes a change or attempted change in the TRM. BPA, and any customer that so elects, shall within ten (10) working days thereafter submit a written submission to the neutral, BPA, and other customers in support of its position that BPA’s action does not constitute a change or attempted change in the TRM. No written submission shall exceed fifty (50) double-spaced pages (12 point font; 26 lines, except for single-spaced quotes), together with exhibits not in excess of one hundred (100) pages.

Within five (5) working days of receipt of the last of the written submissions made pursuant to the paragraph immediately above, the neutral shall notify the parties whether the neutral wishes
to hear argument or otherwise discuss the parties’ submissions and, if so, the date for the hearing, provided it shall occur within ten (10) working days.

In the event the neutral has not set a hearing pursuant to the paragraph immediately above, the neutral shall, within ten (10) working days of the last of the written submissions, issue a written determination as to whether BPA’s action constitutes a change or attempted change in the TRM. In so doing, the neutral shall accord substantial deference to the Administrator’s determination that the action does not constitute a change or attempted change in the TRM.

In the event the neutral has set a hearing, the neutral shall, within ten (10) working days after the hearing, issue a written determination as to whether BPA’s action constitutes a change or attempted change in the TRM. In so doing, the neutral shall accord substantial deference to the Administrator’s determination that the action does not constitute a change or attempted change in the TRM.

The decision of the neutral shall be binding on and accepted by the Administrator. If the neutral determines that BPA’s action constitutes a change or attempted change in the TRM, the change may not be made by BPA without complying with the procedural requirements of section 7(i) of the Northwest Power Act or its successor, and the procedural requirements of section 13.

If prior to or during the process set forth in this section BPA has taken the action that the neutral subsequently determined constitutes a change or attempted change in the TRM, BPA shall take all actions necessary to revoke the action. In no event shall this be construed to provide for damages or liability for loss of profits, or special, incidental, or consequential damages.

One or more third-party neutrals shall be retained by BPA, acting in consultation with major preference customer group representatives, for the purpose of monitoring and, if requested pursuant to this section, providing advisory decisions concerning disputes over factual matters determined in connection with BPA CHWM, Forecast Net Requirement, and Tier 1 System Resources capability determinations. The third-party neutral shall have a strong engineering or other technical background and experience sufficient to make an independent assessment of facts in dispute in connection with BPA CHWM, Forecast Net Requirement, and Tier 1 System Resources capability determinations.

In the case of CHWM, factual matters could involve utility Non-Federal Resource capability, actual FY 2010 load, and any adjustments to those values such as Weather Normalization, Conservation Adjustment, load and data anomalies, and bad behavior. In the case of Forecast Net Requirement, factual matters could involve load forecasts, Non-Federal Resource capability, and other factual matters. In the case of Tier 1 System Resources capability determinations, factual matters could and would concern only whether the determinations generally comport with BPA’s historical approach to making such determinations.

The third-party neutral will have access to, and be able to generally monitor, the pre-decisional internal and external processes BPA employs to make its CHWM, Forecast Net Requirement, and Tier 1 System Resources capability determinations. The neutral will be free to seek and have access to relevant information from both BPA and the customer, subject to appropriate confidentiality arrangements. Since the neutral cannot be expected to be conversant with every matter, BPA and the customers shall alert the neutral to matters that they anticipate may result in disputes.
BPA shall not make final decisions on customer CHWM, Forecast Net Requirement, and Tier 1 System Resources capability until after it has 1) posted its determinations on its website, 2) provided information concerning these matters in response to reasonable information requests, 3) held a public meeting where BPA would explain its determinations and customers and BPA would discuss and seek to resolve issues, and 4) concluded the dispute resolution process provided for below.

Following the public meeting, a customer could seek a decision by the neutral concerning his/her view on 1) a disputed CHWM factual matter if the disputed matter meets the threshold criteria established in section 4.2.1.1, 2) a Forecast Net Requirement factual matter if the disputed matter changes the relevant value or adjustment by a quantity that equals or exceeds the lesser of 5 percent or 10 aMW of the customer’s last year’s load on BPA; or 3) BPA’s initial determination of Tier 1 System Resources capability but only if the customer has the written support for the request by 70 percent of the Tier 1 preference purchasers by utility count. The decision standard on the former for values or adjustments for which the TRM provides standards is whether the BPA proposed value was determined in a manner reasonably consistent with the TRM, and where the TRM provides no standard, whether the BPA proposed value or adjustment is a reasonable one. The decision standard on the latter is whether the BPA proposed Tier 1 System Resources capability determination is a reasonable one.

The dispute process will be a single hearing open to all Tier 1 preference purchasers and shall last no longer than BPA indicates, allowing BPA to render a timely final decision. The dispute process shall be appellate in nature, with the result that the neutral’s findings and conclusions shall be based upon materials that BPA has made publicly available, materials the parties have previously provided to BPA, new or additional materials only upon request by the neutral, and arguments on the materials submitted to the neutral by BPA and the customer. Testimony or
cross examination will occur only upon request of the neutral. The neutral shall transmit his or her decision in writing to the Administrator, who shall make a final decision on the disputed issue after consideration of the neutral’s report.