12.0 COST OF SERVICE ANALYSIS AND RATE MODELING

12.1 Residential Exchange Costing Model

Issue

Whether BPA properly implemented the REP costing model.

Parties' Positions

The DSIs argue that BPA committed errors in its ASC estimates. DSI Brief, WP-02-B-DS-01, at 66; DSI Ex. Brief, WP-02-R-DS-01, at 2-66.

BPA's Position

BPA has properly implemented the REP costing model. Doubleday *et al.*, WP-02-E-BPA-44, at 2-4.

Evaluation of Positions

The Joint DSIs argued that BPA's REP costing model multiplies non-exchanging utility loads by a very small number to prevent divide by zero errors, but if BPA modified the model to add a very small number rather than multiply, the divide by zero problem would be solved and the model would treat the utilities properly as ASC and PF rates change. Schoenbeck *et al.*, WP-02-E-DS/AL/VN-04(E1), at 3. BPA believes it treats non-exchanging utility loads properly. Doubleday *et al.*, WP-02-E-BPA-44, at 2. However, the REP costing model has been modified as the Joint DSIs suggest. Currently, operators of the model use inspection of the data to determine which of the potential exchangers will actually be exchanging during the rate period and which will be in deemer status for the rate test period. *Id.* When the expected PF Exchange Program rate is greater than the ASC of a given utility, that utility is assumed to be in deemer status for the rate test period, and its exchangeable load is zeroed out manually. *Id.* A very small number is now added to this zeroed-out exchangeable load to avoid divide by zero problems. It should be noted that the REP costing model incorporating the DSIs' suggestion yields the same results as the model used before the change, all else being equal. *Id.*

The Joint DSIs argued that BPA's Residential Exchange model does not factor the in-lieu cost into the determination of gross and net exchange costs. Schoenbeck *et al.*, WP-02-E-DS/AL/VN-04(E1), at 3. BPA disagrees. The "Gross Cost" and "Net Cost" tables in the "Summary" tab of the Residential Exchange model use the in-lieu cost in the calculation of gross and net exchange costs. Doubleday *et al.*, WP-02-E-BPA-44, at 3. However, when the in-lieu cost is below the expected PF Exchange Program rate, BPA assumes that the exchanging utility will terminate the in-lieu portion of its exchangeable load. *Id.* *See* Boling and Doubleday, WP-02-E-BPA-30, at 15-16. In this circumstance, the in-lieu cost is multiplied by the zero load to yield a zero in-lieu contribution to the gross and net exchange costs. Doubleday *et al.*, WP-02-E-BPA-44, at 3. The forecasted cost of in-lieu resources is less than the PF Exchange

Program rate in BPA's initial proposal. *Id.* Therefore, the zero in-lieu contribution to exchange costs that the Residential Exchange model calculated for the initial proposal is correct. *Id.*

The Joint DSIs argued that to properly implement the in-lieu price into the determination of gross and net exchange costs, BPA should ratio the utility's ASC and the in-lieu cost in proportion to the amount in-lieued for the comparison to the PF Exchange rate. Schoenbeck *et al.*, WP-02-E-DS/AL/VN-04(E1), at 3. BPA disagrees. The Residential Exchange model separates the monetary exchange portion of a utility's exchange load from the portion subject to an in-lieu transaction. Doubleday *et al.*, WP-02-E-BPA-44, at 3. The costs associated with these two parts are then determined separately. In the "Summary" tab of the model, the monetary exchange costs and in-lieu costs are added together, resulting in load-weighted totals for both the gross and net costs. *Id.* As discussed above, there are circumstances when it is appropriate to zero out the portion of an exchanging utility's load that is subject to an in-lieu transaction. *Id.* The DSIs' proposed method would yield erroneous results where, because the in-lieu resource cost was below the PF Exchange Program rate, the load subject to an in-lieu transaction was eliminated. *Id.*

The Joint DSIs argued that BPA's model does not use a utility's deemer balance when determining whether a utility is exchanging through the rate period. Schoenbeck *et al.*, WP-02-E-DS/AL/VN-04(E1), at 3. BPA has made only preliminary estimates of deemer balances for three exchanging utilities. Doubleday *et al.*, WP-02-E-BPA-44, at 4. These balances have not been reviewed by the exchanging utilities. *Id.* In fact, the issue of deemer balances is currently in dispute. *Id.* The existence of deemer balances and the amount of such balances, if any, must be resolved by BPA and the utilities in the negotiation and development of subsequent RPSAs. *Id.* Deemer balances are not determined in a section 7(i) hearing. Because of the preliminary and uncertain nature of the deemer balance estimates, it would be inappropriate to reflect any deemer balances in determining eligibility of the exchanging utilities during the rate period. *Id.* In addition, the three utilities with possible deemer balances (Avista, IPC, and MPC) are not forecasted to participate in the Residential Exchange during the rate period regardless of deemer balances. *Id.*

Decision

BPA properly implemented the REP costing model.

12.2 Implementation of the Rate Analysis Models (RAM)

In order to establish rates that reflect BPA's Subscription Strategy, changes and additions were made to the RAM. Doubleday *et al.*, WP-02-E-BPA-18, at 14. Care was taken to ensure that these changes and additions comport with BPA's governing statutes. *Id.* at 14-15. The RAM calculates posted rates for the five-year rate period in a two-step process. *Id.* at 15. The first step, the Rate Design Step, uses the same ratemaking methodology used in previous rate cases. Tr. 2149. The second step, the Subscription Step, takes the results of the Rate Design Step and applies Subscription Strategy-based logic to produce rates for Subscription sales. Doubleday *et al.*, WP-02-E-BPA-18, at 16.

The Rate Design Step in the RAM follows BPA's rate directives by determining the costs associated with the three resource pools (FBS resources, REP resources, and new resources) used to serve firm load, and then allocating those costs to the rate pools (PF, IP, and NR). *Id.* at 14. This cost allocation to rate pools takes place in the COSA section of the RAM. *Id.* After the initial allocation of costs, the Northwest Power Act requires that some rate adjustments be made, such as those described in sections 7(b) and 7(c) of the Northwest Power Act. *Id.* The RAM performs these rate adjustments in its Rate Design Study section. *Id.* The Rate Design Study section of the RAM concludes with the calculation of Rate Design Step rates. *Id.*

A new spreadsheet-based model (RESEXRAM) is now used to calculate the gross cost of REP resources. *Id.* This model iterates with the RAM model twice. *Id.* In the first iteration, the gross cost of REP resources is established, and adjustments are made to the values already in the COSA tables. *Id.* An unbifurcated PF rate with PF Preference and PF Exchange loads is then calculated, and the 7(b)(2) rate test is conducted. *Id.* A second iteration between the RAM-Prog model and RESEXRAM is conducted using the 7(b)(2) trigger amount from the 7(b)(2) rate test. *Id.* This iteration determines the level of the PF Exchange Program rate and the amount of net REP costs to be recovered by non-PF Exchange Program rate pools. *Id.* at 15-16.

BPA's Subscription Strategy contains alternative ways in which BPA may sell power to its customers. *Id.* at 16. For example, the Subscription Strategy proposes to offer a settlement of the REP, comprised of power sales and monetary payments, to the region's IOUs. *Id.* BPA must establish rates for such sales. *Id.* If, however, a settlement is not reached, the IOUs would continue participation in the REP, and BPA must have a rate to apply to that Program. *Id.* That rate is the PF Exchange Program rate. *Id.* The NR-02 rate and the PF Exchange Program rate are established in the Rate Design Step of the RAM. *Id.* The NR-02 rate and the PF Exchange Program rate are discussed in greater detail in the testimony of Leathley *et al.*, WP-02-E-BPA-19.

The RAM includes a Subscription Step section to calculate posted rates for the power sales envisioned in BPA's Subscription Strategy. Doubleday *et al.*, WP-02-E-BPA-18, at 16. The Subscription Step section takes the results of the Rate Design Step and adjusts them by the added credits and costs associated with BPA's Subscription Strategy policies. *Id.* The PF Preference rate, the PF Exchange Subscription rate, the RL-02 rate, and the IP-02 rate are established in the Subscription Step. *Id.* The PF Exchange Subscription rate and the RL-02 rate are discussed in greater detail in the testimony of Leathley *et al.*, WP-02-E-BPA-19. The IP-02 rate is discussed in greater detail in the testimony of Ebberts *et al.*, WP-02-E-BPA-22, and Berwager *et al.*, WP-02-E-BPA-09.

The Subscription Strategy-related cost is the cost of the monetary benefits to the IOUs associated with the proposed settlement of the REP. Doubleday *et al.*, WP-02-E-BPA-18, at 17. The Subscription Strategy-related credit is the cost savings associated with the settlement of the REP. *Id.* The Subscription Strategy assumes that regional IOUs will choose to settle the REP through the receipt of power and monetary benefits rather than continue their participation in the Program. *Id.* Under Subscription, the IOUs would be offered the equivalent of 1,800 [1,900] aMW of benefits priced at the RL-02 or PF Exchange Subscription rate. *Id.* Given BPA's decision to increase the amount of settlement benefits from 1,800 to 1,900 aMW in its

Power Subscription Strategy Administrator's Supplemental ROD, references to the 1,800 aMW amount and 800 aMW amount shall hereafter reflect the increase in such amounts in brackets, *e.g.*, [1,900]; [900]. BPA would offer a minimum of 1,000 aMW in actual power sold at the RL-02 rate or the PF Exchange Subscription rate. *Id.* The remainder, 800 [900] aMW, would be either a power sale or a cash payment depending on which is more cost-effective for BPA. *Id.* The monetary component of the settlement would be based on the difference between: (1) BPA's rate case forecast of the cost of a five-year flat-block product; and (2) the RL-02 rate or the PF Exchange Subscription rate. *Id.* It is this cash payment that is allocated during the development of the Subscription Strategy rates. *Id. See* Oliver *et al.*, WP-02-E-BPA-20.

The RAM equitably allocates to the PF Preference class and the RL-02 class the cost, a cost not otherwise allocated under section 7 of the Northwest Power Act, of the cash payment associated with the 800 or 900 aMW portion of the proposed settlement. Doubleday *et al.*, WP-02-E-BPA-18, at 17-18. The effect of this allocation is to equate the two rates. *Id.* at 18. This initial allocation of costs is consistent with the Subscription Strategy's expectation that PF Preference class customers and RL-02 class customers would pay similar rates for similar products. *Id. See* Wholesale Power Rate Development Study Documentation, WP-02-E-BPA-05A, section 2.4, tables SUBSCR 01, SUBSCR 02, SUBSCR 03, SUBSCR 04.

The Subscription Strategy Step assumes that the IOUs will not choose to continue their participation in the REP. *Id.* The rates in the Rate Design Step are set at a level sufficient to recover the net cost of the REP. *Id.* The Rate Design Step rates are the starting point for the Subscription Strategy Step rates. *Id.* Therefore, a credit in the amount of the net cost of the REP in the Rate Design Step must be allocated to the Subscription Strategy Step rates in order to avoid over-collecting the Subscription Step revenue requirement. *Id.* at 19. It is this credit that is allocated during the development of Subscription Strategy Step rates. *Id.*

The RAM equitably allocates the net cost of the REP credit, a benefit not otherwise allocated under section 7 of the Northwest Power Act, to the PF Preference class, the IP-02 class, and the RL-02 class. *Id.* This allocation takes into account the IP-PF link, as well as the DSI floor rate test. *Id.* At this point in the model, when a portion of the REP credit is allocated to the IP-02 rate so that the IP-02 rate is set equal to the flat PF rate (minus the C&R Discount costs) plus the net industrial margin, the Subscription Step IP rate is less than the DSI Floor rate. *Id.* Therefore, the IP rate is set at the DSI Floor, and the remaining REP credit is allocated to the PF Preference and RL-02 rates, reducing them to their final Subscription Strategy Step levels. *Id.* This allocation of credits achieves the Subscription Strategy expectation that PF Preference class customers, IP-02 class customers, and RL-02 class customers would pay similar rates for similar products, while maintaining the PF-IP relationship in section 7(c) of the Northwest Power Act. *Id. See* Wholesale Power Rate Development Study Documentation, WP-02-E-BPA-05A, section 2.4, tables SUBSCR 01, SUBSCR 02, SUBSCR 03, SUBSCR 04.

The IP rate class sales forecast in the Rate Design Step up to this point in the Subscription Strategy Step modeling has been 990 aMW. *Id.* After discussions with the DSIs, BPA decided to purchase 450 aMW specifically for the DSIs, with the understanding that the total of 1,440 aMW would be sold at rates high enough to cover the allocated costs of the 990 aMW in the Subscription Strategy Step plus the costs of the additional 450 aMW purchases. *Id.* at 19-20;

see Berwager *et al.*, WP-02-E-BPA-09. In BPA's initial proposal, BPA forecasted sales of 1,210 aMW at 23.5 mills/kWh and 230 aMW at 25.0 mills/kWh. Doubleday *et al.*, WP-02-E-BPA-18, at 20. Both rates include the costs of the C&R Discount. *Id.* BPA has determined that the above mix of sales and rates (1,210 aMW at 23.5 mills and 230 aMW at 25.0 mills) will recover the costs of serving the new higher DSI sales. *Id.*

Issue

Whether BPA properly implemented the Rate Design Step and the Subscription Step in the RAM.

Parties' Positions

Alcoa/Vanalco and the DSIs argue that BPA improperly implemented the Rate Design Step in the RAM by including a 1,000 aMW sale of power they characterize as an RL sale. Alcoa/Vanalco Brief, WP-02-B-AL/VN-01, at 94-96; DSI Brief, WP-02-B-DS-01, at 61-65; DSI Ex. Brief, WP-02-R-DS-01, at 2-63 to 2-65.

BPA's Position

BPA has properly implemented the Rate Design Step and the Subscription Step of the RAM and has properly included in the Rate Design Step a 1,000 aMW sale under the FPS-96 rate schedule to regional customers. Leathley *et al.*, WP-02-E-BPA-19, at 8-14; Doubleday *et al.*, WP-02-E-BPA-18, at 14-15; Doubleday *et al.*, WP-02-E-BPA-44, at 5-9.

Evaluation of Positions

Alcoa/Vanalco and the DSIs argue that BPA has included in the Rate Design Step a proposed sale of 1,000 aMW of firm power to IOUs under the RL rate. Alcoa/Vanalco Brief, WP-02-B-AL/VN-01, at 95-96; DSI Brief, WP-02-B-DS-01, at 64-65. The DSIs argue that BPA has failed to calculate appropriate rates in its Rate Design Step by, among other things, including a proposed 1,000 aMW sale at the PF-96 Exchange rate [sic] in its modeling, which represents a Subscription sale to the IOUs at the RL rate. DSI Ex. Brief, WP-02-R-DS-01, at 25. The DSIs' argument is clearly incorrect. First, BPA's proposed sale in the Rate Design Step is at the FPS-6 rate, not the PF-96 Exchange rate. More importantly, BPA's testimony expressly states that BPA did *not* include a proposed sale of 1,000 aMW of firm power to IOUs under the RL rate in the Rate Design Step. Doubleday *et al.*, WP-02-E-BPA-44, at 5. As described in Leathley *et al.*, WP-02-E-BPA-19, the Rate Design Step assumes an FPS sale of 1,000 aMW flat priced at a PF-96 equivalent rate level to be sold in the PNW. *Id.* This testimony expressly notes:

> *On the other hand, if the IOUs forego the Subscription settlement proposal, BPA would likely market the 1,000 aMW of power to other purchasers under the FPS-96 rate.* Consistent with BPA's Subscription Strategy, BPA expects that the rates for sales to the IOUs would be approximately equal to the level of the PF Preference rate. Therefore, the assumption of a FPS sale at a rate level equal

> to the PF Preference rate is a proper placeholder to reflect the possible sale of the 1,000 aMW.

Leathley *et al.*, WP-02-E-BPA-19, at 12 (emphasis added). From the inception of the rate case, BPA has clearly stated that the 1,000 aMW in the Rate Design Step is an FPS sale to regional customers, *not* a sale to IOUs at the RL rate. *Id.*

In the Rate Design Step, BPA assumes the traditional implementation of the REP. Doubleday *et al.*, WP-02-E-BPA-44, at 6. After meeting preference loads and an amount of DSI loads in the Rate Design Step, BPA may choose to serve additional regional loads. *Id.* As noted in BPA's Subscription Strategy, which contemplates the traditional REP as well as proposed settlements of that program, BPA's goals include spreading the benefits of Federal power and avoiding increases in BPA's PF Preference rate. *Id.* *See* Burns and Elizalde, WP-02-E-BPA-08, at 7. In the past, BPA's general business goals have also been to provide rate stability in the region while serving BPA's loads. Doubleday *et al.*, WP-02-E-BPA-44, at 6. The Subscription Strategy goals mentioned above are the latest expression of these long-held business goals. *Id.* BPA has determined that it can provide 1,000 aMW of additional power to its customers and not increase the PF Preference rate. *Id.* This is what BPA proposed to do. *Id.* Because BPA has not determined the precise manner in which it would provide this additional Federal power to its regional customers, BPA has assumed that it would make sales of power under the FPS rate schedule to meet regional loads. *Id.* BPA has assumed an FPS rate equal to the 1996 PF Preference rate as a reasonable price for such sales. *Id.* In summary, BPA's proposed sale of 1,000 aMW in the Rate Design Step is consistent with the Subscription Strategy and is also consistent with BPA's long-held business goals. *Id.*

Alcoa/Vanalco continue to mischaracterize BPA's 1,000 aMW FPS sale and argue that it is a part of a proposed REP settlement. Alcoa/Vanalco Brief, WP-02-B-AL/VN-01, at 95. Alcoa/Vanalco argue that in BPA's Loads and Resources Study, BPA included a sale referred to as "IOU sales post-2001." *Id.* Alcoa/Vanalco argue that under cross-examination, the Load Forecast panel admitted to this as "our proposed settlement of the Residential Exchange Program." *Id.* The DSIs note the same items and add that BPA's witness stated that the forecasted sale was "part of the package in the Subscription Strategy and that the amount of the sale reflected the policy of BPA's Subscription Strategy," citing Tr. 903-04. DSI Brief, WP-02-B-DS-01, at 63. Thus, they argue, although the Load Forecast panel identified this as the proposed RL sale pursuant to the settlement, and thus properly part of the Subscription Step, BPA included this in the Rate Design Step that preceded the Subscription Step. *Id.* Alcoa/Vanalco Brief, WP-02-B-AL/VN-01, at 95. The DSIs' conclusions are mistaken. First, as noted above, from the inception of the rate case BPA clearly stated that the 1,000 aMW in the Rate Design Step is not a sale to IOUs at the RL rate. Leathley *et al.*, WP-02-E-BPA-19, at 12. This was reconfirmed in BPA's rebuttal testimony. Doubleday *et al.*, WP-02-E-BPA-44, at 5. Indeed, it is *impossible* for the 1,000 aMW in the Rate Design Step to be a settlement sale to the IOUs, because the Rate Design Step is a step in which only the REP exists, not the IOU Subscription settlements, which exist only in the Subscription Step.

With regard to the argument that the Loads and Resources Study panel referred to a 1,000 aMW sale as a sale related to the IOU Subscription settlements, there is a logical explanation for this

description. In developing its initial rates, BPA knew that BPA's total costs in the Subscription Step would likely be greater than BPA's total costs in the Rate Design Step. This is demonstrated by a comparison of revenues and costs for each step. Wholesale Power Rate Development Study Documentation, WP-02-E-BPA-05A. However, BPA is required to recover its total costs. 16 U.S.C. §839e(a)(1). It was therefore appropriate to use the Subscription Step as a base step that would ensure BPA's total cost recovery. Because BPA knew that it would offer 1,000 aMW of power to Northwest customers at the FPS-96 rate, consistent with its overall business goals, in the Rate Design Step, and also that the Subscription Step had a 1,000 aMW settlement sale to the IOUs, it did not matter, from the perspective of the Loads and Resources panel, how the 1,000 aMW was characterized. Regardless of what the 1,000 MW was called, BPA already knew that there would be a 1,000 aMW sale in each design step. Because, as noted above, the Subscription Step is the final step used in developing rates, the Loads and Resources panel logically referred to the terminology of the step that was used to determine BPA's final proposed rates: the Subscription Step.

Alcoa/Vanalco argue that because the sales they mischaracterize as RL sales were included in the Rate Design Step, the sales had to be accounted for in the load/resource balance. Alcoa/Vanalco Brief, WP-02-B-AL/VN-01, at 95. Alcoa/Vanalco argue that this is why the Load Forecast panel identified the 1,000 aMW as power purchased to sell to the IOUs at the RL rate. *Id.* Alcoa/Vanalco argue that rather than distinguishing between sales that would take place in the Rate Design Step and the Subscription Step, the Rate Design [sic] panel used the same load/resource study for both the Rate Design Step and Subscription Step. *Id.* Tr. 1133-34. Again, the DSIs have mischaracterized BPA's actions. As noted above, no RL sales were included in the Rate Design Step. The RL sale alone did not have to be accounted for in the load/resource balance; rather, the 1,000 aMW FPS sale to regional customers in the Rate Design Step had to be reflected in the load/resource balance, just as the 1,000 aMW of IOU settlement sales in the Subscription Step had to be reflected in the load/resource balance. This was not a problem, because there was a forecasted 1,000 aMW sale in both the Rate Design Step and the Subscription Step. Therefore, a 1,000 aMW sale in the load/resource balance accommodates both design steps. Because there was no need to distinguish between sales that would take place in the Rate Design Step and the Subscription Step, and because the amount was the same in both steps, the COSA panel properly used the same load/resource study for both the Rate Design Step and Subscription Step.

Alcoa/Vanalco argue that the foregoing decision resulted in a sizeable shift in resource acquisition costs from customers eligible to purchase under the PF Exchange rate and the NR rate, the only rates that are not subject to adjustment in the Subscription Step. Alcoa/Vanalco Brief, WP-02-B-AL/VN-01, at 96. Alcoa/Vanalco argue that BPA was buying power at 28.1 mill/kWh but proposing to sell power to the IOUs at approximately 20 mills/kWh. *Id.* Alcoa/Vanalco argue that rates calculated under the Rate Design Step were forced to allocate a revenue deficiency of approximately 8 mills/kWh, or $350 million over the rate period. *Id.* The DSIs make similar arguments and argue that this resulted in costs solely attributable to the Subscription Strategy migrating into those rates set solely in the Rate Design Step, the PF Exchange rate and the NR rate. DSI Brief, WP-02-B-DS-01, at 64; DSI Ex. Brief, WP-02-R-DS-01, at 25. The DSIs argue that including 1,000 aMW of FPS sales that they mischaracterize as sales under the RL rate is an error, as it is axiomatic that an agency cannot

make contradictory findings: the 1,000 aMW will be served along with a traditional REP (in the Rate Design Step), and the 1,000 aMW will be served instead of the REP (in the Subscription Step). DSI Ex. Brief, WP-02-R-DS-01, at 25. As noted above, BPA assumed in the RAM's Rate Design Step a sale of FPS power to regional customers, not a proposed sale of power at the RL rate to the IOUs under a settlement of the REP. Leathley *et al.*, WP-02-E-BPA-19, at 12; Doubleday *et al.*, WP-02-E-BPA-44, at 7. Settlement of the REP is assumed in the RAM's Subscription Step. *Id.* The Rate Design Step assumes a traditional REP. *Id.* Also, as noted above, BPA determined that it could sell an additional 1,000 aMW to regional customers at an FPS price equivalent to PF-96 and still provide rate stability for BPA's preference customers. *Id.* In determining its load/resource balance and the associated revenue requirement, BPA does not assume that costs of individual resources will be allocated to particular individual power sales. *Id.* BPA has the authority to replace reductions in the capability of the FBS. *Id.* These reductions include the shutdown of the Trojan and Hanford nuclear plants (BPA's shares are 230 and 309 aMW, respectively); failure to complete Washington Nuclear Projects Nos. 1 and 3 (BPA's shares are 958 and 651 aMW, respectively); and hydroelectric capability losses (521 aMW). *Id.* System augmentation purchases replace some of these reductions in capability, and the costs of such augmentation purchases are melded with all other FBS resource costs before cost allocation to rate pools is performed. *Id.* The DSIs' assumption, in their calculation of a $350 million revenue deficiency, that the cost of system augmentation purchases should be allocated to specific FPS sales does not comport with BPA's established ratemaking methods. *Id*. Thus, BPA's findings are not contradictory at all. In the Rate Design Step, where the traditional implementation of the REP occurs, it is reasonable to forecast 1,000 aMW of sales to BPA's regional customers, not just the IOUs, in order to spread the benefits of the Federal system widely in the region while providing rate stability and avoiding rate increases to BPA's preference customers. BPA is not providing the IOUs both the REP and 1,000 aMW of regional sales in the Rate Design Step. These sales would be provided to regional customers generally. *Id*. Indeed, given that the IOUs would be participating in the REP, it is likely they would receive less of the 1,000 aMW of FPS-96 regional sales. This is perfectly consistent with the Subscription Step, where the REP does not exist and only settlements of the REP exist, and the 1,000 aMW of sales to the IOUs is for the purpose of settling the REP, just as proposed in BPA's Subscription Strategy. *Id*.

As stated above, BPA's policy goals include spreading the benefits of the Federal hydrosystem widely in the region and avoiding an increase in the PF Preference rate. Doubleday *et al.*, WP-02-E-BPA-44, at 9. BPA believes that making available to the region an additional 1,000 aMW priced at an FPS rate equivalent to PF-96 is one way it can accomplish these very important objectives. *Id.* *See* Burns and Elizalde, WP-02-E-BPA-08, at 7. In addition, as noted above, system augmentation purchases replace reductions in the capability of the FBS and, as such, augmentation costs are melded with all other FBS resource costs before cost allocation to rate pools is performed. Doubleday *et al.*, WP-02-E-BPA-44, at 9. Therefore, the $28.1/MWh for system augmentation cannot be linked to the cost of serving any particular individual PF, IP, or FPS sale and cannot, as the DSIs argue, be used as a price floor for FPS sales. *Id.*

Alcoa/Vanalco argue that, if their mischaracterization of BPA's FPS sales were true, then, as a result of this alleged error, the PF Exchange rate and the NR rate are unattractive to the IOUs, and the IOUs are virtually forced to take the proposed settlement. Alcoa/Vanalco Brief,

WP-02-B-AL/VN-01, at 96. Alcoa/Vanalco argue that the implementation of RAM may result in the IOUs having to settle the REP for less than if BPA had properly implemented the Rate Design Step. *Id.* Alcoa/Vanalco argue that this is arbitrary and capricious and violates sections 5(c) and 7(b) of the Northwest Power Act. *Id.* The DSIs similarly argue that, given the level of the PF Exchange rate, the IOUs must choose BPA's proposed settlement or forego large benefits that a properly calculated REP would produce. DSI Brief, WP-02-B-DS-01, at 62. The DSIs argue that BPA cannot lawfully forecast fictitious loads to produce excessive rates in order to compel IOU acceptance of an alternative to the statutory REP, nor does BPA's obligation to recover its total system costs justify the creation of loads that distort rates and shift costs between rate classes. DSI Ex. Brief, WP-02-R-DS-01, at 26. BPA disagrees with these arguments. First, as explained repeatedly above, BPA did not make an error as suggested by the DSIs. Therefore, the PF Exchange and NR rates are properly established. Whether they are attractive to the IOUs is a judgment that the IOUs will have to make. BPA does not know which option the IOUs will select. Leathley *et al*., WP-02-E-BPA-19, at 11-12. There are many factors that have to be considered in such a selection. For example, in staying with the REP, the IOUs will be subject to in-lieu transactions. Similarly, there are other factors that must be considered in taking the settlement option. For example, the IOUs would have to continue to ensure the existence of their net requirements. Because BPA has properly developed its rates, the Rate Design Step will not result in the IOUs having to settle the REP for less than is appropriate under BPA's proposal. Because BPA's rate development is well-reasoned and supported by the record, it is consistent with applicable standards of judicial review. While Alcoa/Vanalco claim that BPA's approach violates sections 5(c) and 7(b) of the Northwest Power Act, they do not explain which particular parts of such provisions have been violated or in what way such provisions have been violated. BPA's review concludes that BPA's approach is consistent with both sections 5(c) and 7(b) of the Northwest Power Act. BPA also has not forecasted fictitious loads to produce excessive rates. BPA's loads in the Rate Design Step are loads that BPA intends to serve in the event that the IOUs continue participation in the traditional REP and forego the Residential Exchange settlements. Doubleday *et al*., WP-02-E-BPA-44, at 6-7. BPA's load assumptions in the Subscription Step reflect the loads BPA intends to serve if the IOUs adopt the proposed settlements. BPA is also not using its requirement to recover total system costs to justify the creation of loads. BPA has simply noted that in the Subscription Step, BPA incurs costs that BPA does not incur in the Rate Design Step due to the different assumptions regarding the implementation of the REP and the settlements. *See* section 3.4, Wholesale Power Rate Development Study, WP-02-E-BPA-05. As noted throughout this chapter, there are no fictitious loads, but rather the appropriate assumption of 1,000 aMW of sales to regional customers in the Rate Design Step.

The DSIs acknowledge that BPA established that BPA did not include "a proposed sale of 1,000 aMW of firm power to IOUs under the RL rate prior to the Subscription Step," and also acknowledge that BPA characterized the load as "an FPS sale of 1,000 aMW flat priced at the PF-96 rate level." DSI Brief, WP-02-B-DS-01, at 64, quoting Doubleday *et al.*, WP-02-E-BPA-44, at 5. The DSIs acknowledge that BPA established that the 1,000 aMW was the result of a policy decision to "provide 1,000 aMW of additional power to its customers and not increase the PF Preference rate" and that "because BPA has not determined the precise manner in which it would provide this additional Federal power to its regional customers, BPA has assumed that it would make sales of power under the FPS rate schedule to meet regional

loads." DSI Brief, WP-02-B-DS-01, at 64, quoting Doubleday *et al.*, WP-02-E-BPA-44, at 6. The DSIs argue that this explanation was not persuasive after cross-examination. DSI Brief, WP-02-B-DS-01, at 64. The DSIs argue that the same panel that proffered these explanations admitted they simply took the data from the Loads and Resources Study, WP-02-E-BPA-01, for what it was (including the 1,000 aMW sale to the IOUs that the load forecasting panel identified as the proposed Subscription Exchange settlement, Tr. 901) and ran it through both the Rate Design and Subscription Steps. *Id.* The DSIs argue that BPA's claim that the 1,000 aMW sale in the Rate Design Step is not a sale to the IOUs at the RL rate is just semantics, and that BPA's own witnesses admitted that the 1,000 aMW sale is not a sale to unspecified customers, but "our proposed settlement of the Residential Exchange Program." DSI Ex. Brief, WP-02-R-DS-01, at 26, citing the Draft ROD, WP-02-A-01, at 12-6.

BPA disagrees that BPA's statement that it used the same overall loads and resources balance in the Rate Design and Subscription Steps invalidates BPA's position on the 1,000 aMW FPS sale in the Rate Design Step. To the contrary, since, as discussed above, the loads in the Subscription Step (absent those loads served with the 450 aMW of DSI-specific augmentation) are the same as the loads in the Rate Design Step; to use different loads and resources balances in each step would have been a modeling error. BPA's witnesses did not blindly use the data from the Loads and Resources Study; rather, they were simply stating the obvious, that since the loads were the same in both steps, separate load/resource balances did not need to be conducted for each step. They knew there was a 1,000 aMW FPS sale in the Rate Design Step and a 1,000 aMW RL sale in the Subscription Step. The fact that the data in the Loads and Resources Study, WP-02-E-BPA-01, refer only to the 1,000 aMW of settlement sales in the Subscription Step does not invalidate the wealth of BPA testimony concerning the 1,000 aMW of FPS sales in the Rate Design Step. The assumption of a 1,000 aMW FPS sale in the Rate Design Step is well-supported by BPA's testimony and policy, as discussed above, and is also a financially conservative assumption. BPA has shown that in the Subscription Step, 1,000 aMW of settlement power, over and above the power sold under the PF and IP rates, could be sold to the IOUs while still maintaining rate stability for the PF Preference customers. BPA also showed that the total revenue requirement in the Subscription Step is greater than the total revenue requirement in the Rate Design Step. *See* Wholesale Power Rate Development Study Documentation, WP-02-E-BPA-05A, at 91, lines 19 and 24. Therefore, it follows that in the Rate Design Step, with a lower revenue requirement, BPA could sell an additional 1,000 aMW of power, over and above the power sold under the PF and IP rates, and also maintain rate stability for the PF Preference customers.

The DSIs argue that it does not matter how BPA chooses to characterize the 1000 aMW sale, it cannot lawfully be included in the Rate Design Step if BPA does not expect to make the sale other than as a settlement of the REP claims. DSI Ex. Brief, WP-02-R-DS-01, at 26. This argument makes little sense. Since the inception of the rate case, BPA has identified a proposed 1,000 aMW sale to regional customers at the FPS-96 rate in the Rate Design Step in order to widely spread the benefits of Federal power among BPA's customers while continuing the traditional REP. As noted above, BPA did *not* assume a proposed sale of power at the RL rate to the IOUs under a settlement of the REP in the Rate Design Step. Leathley *et al.*, WP-02-E-BPA-19, at 12; Doubleday *et al.*, WP-02-E-BPA-44, at 7. Further, BPA indeed can lawfully include the 1,000 aMW sale in the Rate Design Step, because BPA has the authority and

intent to make such sales in the Rate Design Step environment where the traditional REP continues. It must be recalled that the IOUs may forego the proposed settlements and BPA would make its actual sales as described in the Rate Design Step. In simple terms, settlement of the REP is assumed in the RAM's Subscription Step. *Id.* The Rate Design Step assumes a traditional REP. *Id.* As noted above, BPA determined that in the Rate Design Step it could sell an additional 1,000 aMW to regional customers at a price equivalent to the PF-96 rate and still provide rate stability for BPA's preference customers. *Id.* BPA expects to make the 1,000 aMW sale to regional customers in the Rate Design Step environment where IOUs forego the proposed settlements.

The DSIs argue that it must have been obvious to staff that if what the DSIs mischaracterized as a 1,000 aMW sale to the IOUs resulting from the Subscription Strategy were removed from the Rate Design Step, the PF Exchange, IP, and NR rates calculated therein would decrease, because BPA would have additional augmentation costs related to achieving load/resource balance in the Rate Design Step. DSI Brief, WP-02-B-DS-01, at 64-65. This *ad hominem* argument is speculative, and its implications are premised on a misstatement of fact. First, as explained above, BPA properly included a 1,000 aMW FPS sale to regional customers in the Rate Design Step. Because this was proper, BPA did not have to speculate about the rate effects of removing something that was properly included. Obviously, however, if one makes a large change in any design step there will likely be consequences of that change, regardless of whether it is the Rate Design Step or the Subscription Step. As noted previously, however, from the inception of the rate case BPA clearly stated that the 1,000 aMW in the Rate Design Step is not a sale to IOUs at the RL rate. Leathley *et al.*, WP-02-E-BPA-19, at 12. This was reconfirmed in BPA's rebuttal testimony. Doubleday *et al.*, WP-02-E-BPA-44, at 5. Indeed, it is impossible for the 1,000 aMW in the Rate Design Step to be a settlement sale to the IOUs, because the Rate Design Step is a step in which only the REP exists, not the IOU Subscription settlements, which exist only in the Subscription Step. Because BPA knew that it would offer 1,000 aMW of power to Northwest customers at the FPS-96 rate in the Rate Design Step and also that the Subscription Step had a 1,000 aMW settlement sale to the IOUs, it did not matter how the 1,000 aMW was characterized. Regardless of what the 1,000 MW was called, BPA already knew that there would be a 1,000 aMW sale in each design step.

The DSIs note that BPA staff suggested that the DSI proposal to remove the 1,000 aMW sale from the Rate Design Step does not comport with BPA's policy goals for this rate case and would require a different load/resource balance and a differently sized FBS in the Rate Design Step than in the Subscription Step of the RAM. DSI Brief, WP-02-B-DS-01, at 65. The DSIs argue that BPA's rate directives do not permit staff to mischaracterize loads. *Id.* The DSIs argue that staff offers no rationale why it is necessary or even desirable to maintain the same load/resource balance and FBS size between the Rate Design Step and the Subscription Step. *Id.* The DSIs argue that the two steps have distinct purposes, and there is no analytical or policy reason for maintaining the same loads and resources for the two steps. *Id.* The DSIs argue that the only purpose is to raise the level of the PF Exchange, IP, and NR rates in the Rate Design Step above their proper level. *Id.*

While the DSIs argue that the Northwest Power Act does not permit staff to mischaracterize loads, this did not occur in BPA's rate development, and staff has characterized loads correctly.

As repeatedly noted above, from the inception of the rate case BPA clearly stated that the 1,000 aMW in the Rate Design Step is a sale to regional customers at the FPS rate and not a sale to IOUs at the RL rate. Leathley *et al.*, WP-02-E-BPA-19, at 12. This was reconfirmed in BPA's rebuttal testimony. Doubleday *et al.*, WP-02-E-BPA-44, at 5. The DSIs argue that staff offers no rationale why it is necessary or even desirable to maintain the same load/resource balance and FBS size between the Rate Design Step and the Subscription Step. DSI Brief, WP-02-B-DS-01, at 65. The DSIs, however, have mischaracterized BPA's testimony. The statement made by staff regarding the load/resource balance and FBS did not have to do with the issue of whether or not 1,000 aMW should be included in the Rate Design Step. *See* Doubleday *et al.*, WP-02-E-BPA-44, at 8-9. Instead, it addressed the issue of whether the 1,000 aMW of the FPS sale in the Rate Design Step (which the DSIs incorrectly characterize as an RL sale) should be treated in the same manner as BPA treated the cost of the other 800 [900] aMW of benefits (monetary benefits) offered to the IOUs as part of the Subscription settlements. *Id.*

While the DSIs argue that staff have offered no reason for why it is necessary or desirable to maintain the same loads and resources for the two steps, the explanation of this issue, based on the actual issue addressed by staff, is clearly stated in staff's testimony. The 1,000 aMW FPS sale in the Rate Design Step is in support of BPA's commitment to broadly spread the benefits of the Federal hydro system in the region while providing rate stability. Doubleday *et al.*, WP-02-E-BPA-44, at 8. In the Rate Design Step, BPA is uncertain to whom the 1,000 aMW of FPS power will be sold. *Id.* In the Subscription Step, BPA assumes that the IOUs accept the Subscription settlement proposal and that 1,000 aMW is made available to the IOUs in power and 800 [900] aMW in monetary benefits. *Id.* *See* Leathley *et al.*, WP-02-E-BPA-19, at 12. The 1,000 aMW of power in the Rate Design Step should not be treated in the same manner as the 800 [900] aMW of monetary settlement benefits provided in the Subscription Step, because to do so would not comport with BPA's Loads and Resources Study, WP-02-E-BPA-01. Doubleday *et al.*, WP-02-E-BPA-44, at 8. The 1,000 aMW is included in the load/resource balances of both the Rate Design Step and the Subscription Step in the RAM. *Id.* In addition, BPA has assumed that the size of the FBS is the same in both the Rate Design Step and the Subscription Step in the RAM. *Id.* The 800 [900] aMW of IOU settlement benefits is assumed not to be actual power, is not included in the loads/resources balance, and does not affect the size of the FBS. *Id.* In summary, the DSI proposal does not comport with BPA's policy goals for this rate case and would require a different loads/resources balance and a differently sized FBS in the Rate Design Step than in the Subscription Step of the RAM. *Id.* at 8-9.

On the DSI issue raised above that was based on a mischaracterization of BPA's testimony and is not related to the treatment of the 800 [900] aMW of monetary settlement benefits, the DSIs argue that the two design steps have distinct purposes, and there is no analytical or policy reason for maintaining the same loads and resources for the two steps. This argument is misplaced. BPA has not stated that there is a requirement that the loads and resources must be identical in both design steps. Instead, BPA has established the load and resource elements of each step and reflected those in each step. For the reasons repeatedly stated above, the proper loads and resources are reflected in the Rate Design Step, and the proper loads and resources are reflected in the Subscription Step. Because these steps have been properly established, it would be inappropriate to adopt a proposal that would change the loads or resources of either step.

The DSIs argue that treatment of the 1,000 aMW serves two purposes. DSI Brief, WP-02-B-DS-01, at 65. First, this treatment hides a significant amount of costs of the Subscription Step by shifting them to the Rate Design Step, which makes the settlement of the REP appear less costly than it really is. *Id.* Second, the shifting of costs increases the PF Exchange rate and reduces the potential benefits that would be available to exchanging utilities, thereby forcing them to elect the proposed settlement. *Id.* The DSIs argue that BPA cannot violate the rate directives in furtherance of these purposes and should remove the 1,000 aMW from the Rate Design Step. *Id.* To the extent that the DSIs are stating that there were inappropriate "purposes" attempted to be achieved by BPA, such *ad hominem* arguments are false and unfounded. The DSIs attribute nonexistent motives to BPA. While elements in the conduct of BPA's design steps have impacts on the levels of rates, this is simply a truism. Regardless of how a particular element affects particular rates, the question is whether BPA has properly developed and conducted the elements. In this case, as repeatedly explained above, BPA has properly conducted the elements in the Rate Design Step and the Subscription Step. BPA's rate development in these areas does not violate, but rather properly implements, the rate directives of the Northwest Power Act. The 1,000 aMW FPS sale to regional customers must be retained in the Rate Design Step.

Alcoa/Vanalco argue that there is no basis in the Northwest Power Act for the Subscription Step, and the rate directives do not allow this adjustment in the development of rates. Alcoa/Vanalco Brief, WP-02-B-AL/VN-01, at 97. The DSIs argue that even assuming the lawfulness of the Subscription Strategy, BPA's discretion does not extend to inventing fictional loads for calculating rates pursuant to the rate directives of the Northwest Power Act to support the Strategy. DSI Ex. Brief, WP-02-R-DS-01, at 26. BPA must support the Subscription Strategy in compliance with the Northwest Power Act. *Id.* BPA's rate directives in section 7 of the Northwest Power Act provide significant direction to BPA in the development of rates. 16 U.S.C. §839e. The rate directives, however, are not so detailed as to cover every circumstance that arises in ratemaking. There a number of examples of steps BPA takes in the development of rates that are not expressly stated in the rate directives. For example, in ratemaking, BPA functionalizes costs between generation and transmission. In ratemaking, BPA classifies generation costs between energy, demand, and load variance. In ratemaking, BPA uses the MCA results to distribute energy costs between monthly diurnal periods. The Northwest Power Act does not explicitly require the functionalization and classification of costs, nor does it explicitly require the use of marginal cost pricing. Thus, the fact that a particular step might not be expressly mentioned in the rate directives does not mean that it is not permitted by the Northwest Power Act. In addition, when the statute does not provide BPA with express direction regarding a particular issue, it is the agency's responsibility to interpret the statute. In the current rate case, BPA is faced with a number of circumstances that it has not previously encountered. For example, as noted above, under BPA's Subscription Strategy, an IOU may choose to continue with traditional participation in the REP, or it may choose to participate in a proposed settlement of that program. BPA does not know which option will be chosen by the IOUs. BPA therefore must develop rates that can accommodate either circumstance. This is a very difficult problem to address in ratemaking, yet it must be addressed. The Northwest Power Act recognizes the need for broad discretion in the development of rate design. Section 7(e) of the Northwest Power Act provides:

> Nothing in this Northwest Power Act prohibits the Administrator from establishing, in rate schedules of general application, a uniform rate or rates for sale of peaking capacity or from establishing time-of-day, seasonal rates, or other rate forms.

16 U.S.C. §839e(e).

As noted in greater detail above, BPA has not invented fictional loads for calculating rates pursuant to the rate directives of the Northwest Power Act to support BPA's Subscription Strategy. The loads BPA has forecasted in the Rate Design Step are the loads that BPA will serve if the traditional REP continues and the IOUs do not agree to the proposed REP settlements. BPA's proposals comply with the Northwest Power Act and also support BPA's Subscription Strategy. *Id.* In summary, the manner in which BPA has developed rates in this proceeding is premised on the reasonable construction and implementation of the rate directives of the Northwest Power Act. Reflecting a Subscription Step in BPA's rates to accommodate the special circumstances faced in this case is consistent with the Northwest Power Act.

Decision

BPA properly implemented the Rate Design Step and the Subscription Step in the RAM.

12.3 Development of the Residential Load (RL) Rate and Federal Base System (FBS) Replacements

Issue

Whether BPA properly developed the RL rate and whether BPA should acquire approximately 1,282 aMW as FBS replacement resources.

Parties' Positions

WPAG argues that the RL rate must be established under section 7(f) of the Northwest Power Act, which requires that power acquired to serve the IOUs' loads must be allocated to the rates under which they take service. WPAG Brief, WP-02-B-WA-01, at 2. WPAG also argues that BPA will be unduly discriminatory if BPA does not offer service under the RL rate to public agency customers that participate in the REP, as well as IOUs. *Id.* at 3. WPAG reiterates these arguments in its brief on exceptions. WPAG Ex. Brief, WP-02-R-WA-01, at 2-8. The PPC notes that the exchange settlements are proposed to be offered to regional IOUs but have not been proposed to be offered to other regional utilities participating in the REP. PPC Brief, WP-02-B-PP-01, at 64.

MAC argues that the net cost of system augmentation for the Slice product should not include 990 aMW of purchases for the DSIs. MAC Brief, WP-02-B-MA-01, at 8. Similar arguments are made by PPC and SPG regarding BPA's PF Preference rate. PPC Brief, WP-02-B-PP-01, at 52; SPG Brief, WP-02-B-SG-01, at 13-15. SPG also argues that non-Federal resources should not be acquired to replace reductions in FBS capability. SPG Brief, WP-02-B-SG-01, at 14-15.

BPA's Position

BPA has properly developed the RL rate. Leathley *et al.*, WP-02-E-BPA-19, at 8-14; Doubleday *et al.*, WP-02-E-BPA-44, at 10-12. BPA has properly allocated purchased power costs. Doubleday *et al.*, WP-02-E-BPA-44, at 10-12. BPA is properly acquiring 1,282 aMW as FBS replacement resources. Loads and Resources Study Documentation, WP-02-FS-BPA-01A. BPA is required by law to provide RL service only to IOUs, and offering RL service only to the IOUs as part of a settlement of the REP is not unduly discriminatory.

Evaluation of Positions

WPAG argues that sections 7(b)(1) and 7(f) of the Northwest Power Act were intended to produce a PF rate that was lower than the rate under which BPA is authorized to offer requirements service to the loads of IOUs under the Northwest Power Act. WPAG Brief, WP-02-B-WA-01, at 5-6. WPAG argues that this is contrary to BPA providing requirements service to preference customers and IOUs at approximately the same rate. *Id.* at 6. BPA acknowledges that the implementation of those statutory provisions has generally resulted in a PF Preference rate lower than the NR rate. This is also true in this rate case. As discussed in greater detail below, however, section 7(f) of the Northwest Power Act permits the development of more than one rate for requirements service to IOUs. This permits the development of the RL rate, which applies to the special circumstances of the settlement of the REP with regional IOUs.

WPAG argues that a number of ratemaking actions BPA has taken are contrary to the Northwest Power Act. *Id.* The first action WPAG describes was that BPA acquired power that is not needed during the rate period to meet preference customer loads but is used instead to serve IOU loads. *Id*. at 7. WPAG also objects to the designation of purchased power as FBS replacement power. *Id.* WPAG argues that designating power as FBS replacements for the sole purpose of reducing the rate for requirements loads of IOUs is contrary to Northwest Power Act sections 7(b)(1) and 7(f). *Id.* Without citation to authority, WPAG argues that BPA should not have acquired power not needed to meet preference customer loads to replace the FBS. The Northwest Power Act, however, expressly grants BPA the authority to acquire resources to replace reductions in the capability of the FBS.

Section 3(10) of the Northwest Power Act defines FBS resources as: (1) the FCRPS hydroelectric projects; (2) resources acquired by the Administrator under long-term contracts in force on the effective date of this Northwest Power Act; and (3) resources acquired by the Administrator *in an amount necessary to replace reductions in the capability of the resources referred to in subparagraphs (1) and (2) of this paragraph*. 16 U.S.C. §839a(10) (emphasis added).

The Northwest Power Act expressly recognizes that the Administrator may acquire resources as needed to replace the reduced capability of the FBS. As noted in BPA's testimony, these reductions include the shutdown of the Trojan and Hanford nuclear plants (BPA's shares are 230 and 309 aMW, respectively); failure to complete Washington Nuclear Projects Nos. 1 and 3 (BPA's shares are 958 and 651 aMW, respectively); and hydroelectric capability losses

(521 aMW). Doubleday *et al.*, WP-02-E-BPA-44, at 7. These reductions total 2,669 aMW, which is far more than the amount of power BPA is acquiring for the coming rate period. In addition, the Northwest Power Act does not limit resource acquisitions to the amounts needed to meet preference loads. Section 6(a)(2) of the Northwest Power Act provides that:

> In addition to acquiring electric power pursuant to section 5(c), or on a short-term basis pursuant to section 11(b)(6)(i) of the Transmission System Act, *the Administrator shall acquire*, in accordance with this section, *sufficient resources to meet his contractual obligations* that remain after taking into account planned savings from measures provided in paragraph 1 of this subsection, and to assist in meeting the requirements of section 4(h) of this Northwest Power Act.

16 U.S.C. §839d(a)(2) (emphasis added).

In BPA's current rate case, because current power sales contracts will expire before the beginning of the next rate period, BPA must forecast its contractual obligations for the coming rate period. BPA's purchases are acquired to meet BPA's forecasted loads to BPA's preference customers, IOU customers, and the relevant portion of DSI customers and other contractual obligations. As noted in BPA's testimony, "BPA does not assume that costs of individual resources will be allocated to particular individual power sales." Doubleday *et al.*, WP-02-E-B-A-44, at 7. Also, as noted in the Northwest Power Act's rate directives, FBS resources are not allocated solely to BPA's preference customers, but also to exchanging utility customers and, depending on the size of the FBS, to other customers. In fact, the Northwest Power Act expressly recognizes that FBS resources, in the proper circumstances, may be allocated to the rates BPA establishes under section 7(f) of the Northwest Power Act, *e.g.*, the NR and RL rates. Section 7(f) of the Act states that "[r]ates for all other firm power sold by the Administrator for use in the Pacific Northwest shall be based upon the cost of the portions of FBS resources, [exchange resources] . . .and additional resources which, in the determination of the Administrator, are applicable to such sales." 16 U.S.C. §839e(f).

In a similar vein, MAC argues that the net cost of system augmentation for the Slice product should not include 990 aMW of power purchases for the DSIs. MAC Brief, WP-02-B-MA-01, at 8. The PPC argues that the DSIs should pay their own augmentation costs, because preference customers are exposed to market-based charges such as the TAC, TACUL, and SUMY. PPC Brief, WP-02-B-PP-01, at 52. SPG also argues that BPA should assign to the DSIs the cost of augmentation for the DSIs. SPG Brief, WP-02-B-SG-01, at 13-15. First, as noted above, BPA must forecast its contractual obligations for the coming rate period. BPA's purchases are acquired to meet BPA's forecasted loads to BPA's preference customers, IOU customers, and the relevant portion of DSI customers and other contractual obligations. BPA has the authority to replace reductions in the capability of the FBS. This increases the size of the FBS. Costs of the FBS are then allocated in accordance with BPA's rate directives. As noted in BPA's testimony, "BPA does not assume that costs of individual resources will be allocated to particular individual power sales." Doubleday *et al.*, WP-02-E-B-A-44, at 7. SPG argues that BPA proposes to sell DSI customers power from the FBS melded with power purchases specifically for service to the DSIs. SPG Brief, WP-02-B-SG-01, at 14. SPG has mischaracterized BPA's testimony. BPA's testimony states that "BPA will be purchasing

approximately 1,562 aMW [of which 450 aMW are not FBS replacements, *see* WPRDS, WP-02-E-BPA-05, at 69] in order to have sufficient FBS resources to meet BPA's total Subscription load obligation during the FY 2002-2006 period. BPA, however, does not plan FBS replacement purchases on a customer class-by-customer class basis." Berwager *et al.*, WP-02-E-BPA-09, at 7.

SPG argues that BPA also stated that "the service to the DSI customers will be from the FBS, and because of that, all customers, both Slice and non-Slice customers will share in the costs of extending the Inventory Solution to include these sales to the DSI customers." SPG Brief, WP-02-B-SG-01, at 14, quoting Mesa *et al.*, WP-02-E-BPA-54, at 10. Both the SPG Brief and the Mesa testimony it quotes reference the testimony of Berwager *et al.*, WP-02-E-BPA-09. *Id.* As noted above, BPA does not plan FBS replacement purchases on a customer class by customer class basis. Berwager *et al.*, WP-02-E-BPA-09, at 7. Furthermore, the testimony cited by SPG concerns the actual "service" to the DSIs, as opposed to the ratemaking treatment of the IP rate class costs. The BPA witness is just stating the obvious, that all of BPA's actual load obligations, including preference customer load, IOU customer load, and DSI customer load, must be served with real power available to BPA. That power comes from the FBS. SPG notes that BPA testified during cross-examination that the proposed sale to the DSIs is not necessarily for replacement of the FBS. SPG Brief, WP-02-B-SG-01, at 14-15 SPG has mischaracterized BPA's cross-examination testimony. The BPA witness was asked if system augmentation was an FBS replacement. Tr. 218-19. The BPA witness answered that due to his imperfect knowledge of the statutory and legal connotations concerning replacements for the FBS, he did not feel competent to answer. *Id*. Nowhere in the testimony did the witness mention the DSIs. *Id.* In summary, BPA may purchase power to replace reductions in the capability of the FBS and may acquire power to meet its forecasted contractual obligations to its customers. The costs of such power are properly allocated under BPA's rate directives and may be incurred by BPA's customers. That some of BPA's power may be used to serve a portion of DSI loads is appropriate.

SPG also argues that BPA must acquire any non-Federal resources to replace the reductions in FBS capability in accordance with the requirements of section 6(b)(4) of the Northwest Power Act. SPG Brief, WP-02-B-SG-01, at 14-15. SPG argues that BPA's testimony indicates that BPA has not conducted the steps necessary if power purchases for the DSI customers are FBS replacements. *Id.;* Tr. 220, lines 2-15. This argument mischaracterizes BPA's testimony. BPA's witness correctly notes that "these are purchases that we believe are necessary in order to meet forecasted load commitments from the total customer classes that we expect to place load on us." Tr. 220, lines 9-12. BPA's witness noted earlier that he was unfamiliar with the concept of FBS replacements. BPA's witness stated that "I do not believe that I have a perfect understanding of what an FBS replacement, versus an FBS decision, versus general augmentation is. So I guess I will have to say that I believe that that has specific statutory and legal connotation that I do not feel competent to answer perfectly at this point, as to whether they are FBS replacement purchases, *per se*." Tr. 218-19. Simply because this particular witness did not understand the legal implications of FBS replacements does not mean that BPA has not conducted the steps necessary to purchase power for FBS replacements. The record is quite clear regarding BPA's proposal in this rate case to replace reductions in the capability of the FBS with power purchases.

BPA clearly proposed to replace reductions in the capability of the FBS with purchases in BPA's initial proposal. For example, "BPA will be purchasing approximately 1,562 aMW [of which 450 aMW are not FBS replacements, *see* WPRDS, WP-02-E-BPA-05, at 69] in order to have sufficient FBS resources to meet BPA's total Subscription load obligation during the FY 2002-2006 period." Berwager *et al.*, WP-02-E-BPA-09, at 7. Similarly, BPA noted that "BPA has assumed that it will need to increase its power inventory to meet its customers' Subscription purchases. The power added to the inventory is defined as FBS replacements and enables BPA to achieve load/resource balance on an annual basis. The cost of the purchased power is treated as part of the total cost of FBS resources for ratemaking purposes." Doubleday *et al.*, WP-02-E-BPA-18, at 7. Furthermore, "BPA is acquiring a substantial amount of system augmentation to meet its forecasted firm loads during the rate period. Some of these firm loads include sales to the DSIs and IOUs. BPA's power purchases replace reductions in the capability of the FBS. The costs of the FBS, including FBS replacements, are allocated to all rate classes served by the FBS." Doubleday *et al.*, WP-02-E-BPA-44, at 10. As noted previously, BPA has the authority to acquire power "in an amount necessary to replace reductions in the capability of the [FBS] resources." 16 U.S.C. §839a(10). BPA's testimony established that these reductions total 2,669 aMW, which is far more than the amount of power BPA is acquiring for the coming rate period. Doubleday *et al*., WP-02-E-BPA-44, at 7. In addition, the Northwest Power Act authorizes the BPA Administrator to acquire "sufficient resources to meet [her] contractual obligations." 16 U.S.C. §839d(a)(2). BPA also clearly identified the proposed price for the purchases in BPA's initial proposal. Oliver *et al.*, WP-02-E-BPA-20. These purchases are clearly economically prudent acquisitions. *Id*.

With regard to an additional claim that BPA has not complied with the Northwest Power Act, such an issue must begin with review of the Northwest Power Act itself. Section 6(b)(4) of the Northwest Power Act provides:

> The Administrator shall acquire any non-Federal resources to replace FBS resources only in accordance with the provisions of this section. The Administrator shall include in the contracts for the acquisition of any such non-Federal replacement resources provisions which will enable [her] to ensure that such non-Federal replacement resources are developed and operated in a manner inconsistent with the considerations specified in section 4(e)(2) of this Northwest Power Act.

16 U.S.C. §839d(b)(4). Section 4(e)(2) of the Northwest Power Act provides:

> The plan shall set forth a general scheme for implementing conservation measures and developing resources pursuant to section 6 of this Northwest Power Act to reduce or meet the Administrator's obligations with due consideration by the NWPPC for: (1) environmental quality; (2) compatibility with the existing regional power system; (3) protection, mitigation, and enhancement of fish and wildlife and related spawning grounds and habitat, including sufficient quantities and qualities of flows for successful migration, survival, and propagation of anadromous fish; and (4) other criteria which may be set forth in the plan.

16 U.S.C. §839b(e)(2).

The FBS replacements, comprised of power purchases, are being acquired in accordance with section 6(b)(4) and meet the criteria of section 4(e)(2). BPA analyzed the use of power purchases in its 1995 BPA Business Plan (DOE/BP-2664). The Administrator notes this previous administrative decision. The Business Plan specified that BPA would rely on power purchases and nonfirm energy to meet load.

> BPA must be careful not to make long-term commitments to acquire power resources for loads it may not have; *i.e.*, loads that move away from BPA service and obtain their power from BPA's competitors. In addition, because the operation of the hydrosystem has changed to provide additional flows for migrating salmon, there is a vast amount of very low-cost hydropower in the spring that makes almost any other type of generation unnecessary during the flow periods. If a new resource cannot shutdown during spring flow period, BPA will be unable to take advantage of the required spring flows to reduce costs to its customers. These conditions demand resource flexibility, as well as low cost…The type of resource that fits best with the existing system under present conditions is a resource that can operate economically during periods of low hydro generation, but which can be shutoff without incurring large costs when flows are high, whether the high flows are the result of good water years or fish flow requirements . . . only one type of resource fully meets these conditions: spot market power purchases. Power purchases are particularly attractive because they do not require capital investment or long-term financial obligations for BPA as a purchaser.

1995 BPA Business Plan, at 34.

This decision was confirmed in the BPA Business Plan Final Environmental Impact Statement (BP FEIS) that accompanied the Business Plan. Specifically, section 2.4.3.2 reviews BPA's resource priorities under the Northwest Power Act. BP FEIS at 2-26. Furthermore, BPA's Subscription Strategy NEPA ROD states that BPA does not intend to rely on the long-term acquisition of the output of new generation resources to meet any increases in its loads. Instead, BPA plans to use cost-effective power purchases. Subscription Strategy NEPA ROD at 18. For these reasons, power purchases are consistent with the criteria of section 4(e)(2), because power purchases meet the considerations for environmental quality, compatibility with the existing regional power system, fish and wildlife concerns, and other considerations related to cost effectiveness. Moreover, consistent with section 6(a)(1) of the Northwest Power Act, BPA has taken into account planned savings from conservation and renewable resources. As BPA has proceeded with augmentation of the Federal system to meet loads forecast to be served under Subscription, BPA has reviewed the role conservation should play in augmentation. Oliver *et al.*, WP-02-E-BPA-45, at 8. BPA proposed that 12 aMW of conservation resources, on an annual basis, will be targeted for acquisition. *Id.* BPA set this target based on the current 1998 Northwest Conservation and Electric Power Plan. *Id. See also* NWPPC Issue Paper 99-18, *Bonneville Conservation Acquisition 2002-2006*, which estimates the amount of cost-effective conservation available consistent with the NWPPC's 1998 Plan at 150 aMW over the rate period.

Issue Paper 99-18 at 14. Over the rate period, BPA plans to implement a total of 150 aMW from all BPA-sponsored conservation activities. *Id.*

WPAG argues that BPA has misapprehended its authority to replace lost FBS capability. WPAG Ex. Brief, WP-02-R-WA-01, at 4-5. WPAG argues that BPA's authority under section 6(a)(2) of the Northwest Power Act to acquire replacements for lost FBS capability is limited to resources, which means actual or planned electric power capability of generating resources. *Id*. WPAG argues that this definition does not denominate as an FBS replacement a short-term market purchase made pursuant to section 11(b)(6)(i) of the Transmission System Act. *Id*. First, WPAG cites no record evidence that BPA is relying on section 11(b)(6)(i) of the Transmission System Act to make its short-term (five-year) power purchases. In fact, BPA is relying on its authority to make five-year purchases under section 6 of the Northwest Power Act. Regardless, however, WPAG has misinterpreted the Northwest Power Act. WPAG failed to include the full relevant text of the Act's definition of "resource." The Northwest Power Act defines "resource," in part, as "*electric power*, *including* the actual or planned electric power capability of generating facilities." 16 U.S.C. §839a(19)(A). The Northwest Power Act's definition thus references *electric power* from whatever source, which would include market purchases, and merely notes that included as two examples of this electric power are the actual or planned electric power capability of generating facilities. Supporting this construction is the fact that the Northwest Power Act defines "electric power" as "electric peaking capacity, or electric energy, or both." 16 U.S.C. §839a(9). BPA's power purchases from the market are therefore clearly consistent with the definition of "resource" in the Northwest Power Act. WPAG argues that its conclusion is supported by section 6(b)(4) of the Northwest Power Act, which requires that the acquisition of any non-Federal resources by BPA to replace lost FBS capability must be in accordance with section 6 of the Northwest Power Act. *Id*. This argument is difficult to understand. Section 6 of the Northwest Power Act is a lengthy section of the statute. WPAG does not identify which provisions of section 6 are alleged to be inconsistent with BPA's proposal. Without knowing these provisions, BPA is unsure of WPAG's arguments. WPAG also argues that short-term market purchases cannot be FBS replacements under sections 6(a)(2) and 6(b)(4) of the Northwest Power Act. *Id*. BPA, however, has discussed its compliance with sections 6(a)(2) and 6(b)(4) of the Northwest Power Act in section 12.3 of this chapter. WPAG argues that since the short-term market purchases that BPA proposes to make cannot be denominated FBS replacements, their costs cannot, consistent with section 7(b)(1) of the Northwest Power Act, be included in the costs allocated to the PF rate. WPAG Ex. Brief, WP-02-R-WA-01, at 5. As noted in the foregoing discussion, BPA's market purchases are clearly resources under the Northwest Power Act and are also FBS replacement resources. The costs of these resources are properly allocated to the PF Preference rate. Doubleday *et al*., WP-02-E-BPA-44, at 10. In summary, BPA intends to acquire the amount and type of resources noted above as FBS replacement resources.

WPAG argues that the record makes it abundantly clear that augmentation power purchases that BPA intends to make during the rate period are solely for the purpose of making power sales to the IOUs under the RL rate. WPAG Ex. Brief, WP-02-R-WA-01, at 3, citing Doubleday *et al.*, WP-02-E-BPA-44, at 10-11. WPAG has misrepresented BPA's rebuttal testimony. The cited testimony does not indicate that system augmentation purchases are made solely to support RL rate sales. The testimony states: "BPA is acquiring a substantial amount of system

augmentation to meet its forecasted firm loads during the rate period. *Some of these firm loads include sales to the DSIs and IOUs*." Doubleday *et al.*, WP-02-E-BPA-44, at 10, lines 20-22 (emphasis added). Clearly, system augmentation amounts are associated with BPA's total firm load obligation. WPAG argues that the power needed to effectuate the REP settlement will be purchased in the market and denominated as FBS replacement power, permitting BPA to allocate a large portion of the costs of this power to preference customers. WPAG Ex. Brief, WP-02-R-WA-01, at 3. As noted above, BPA's purchases are acquired to meet BPA's forecasted loads to BPA's preference customers, IOU customers, and the relevant portion of DSI customers and other contractual obligations. As noted in BPA's testimony, "BPA does not assume that costs of individual resources will be allocated to particular individual power sales." Doubleday *et al.*, WP-02-E-BPA-44, at 7.

SPG argues that BPA proposes to spread the costs of power purchases for the DSIs over other rate classes. SPG Brief, WP-02-B-SG-01, at 14-15. SPG argues that BPA's rates for preference and Federal agency customers must be based on only the costs of those FBS resources and power purchases necessary to meet the loads of these customer classes, citing section 7(b)(1) of the Northwest Power Act, 16 U.S.C. §839e(b)(1). *Id*. SPG has misapplied section 7(b)(1) of the Northwest Power Act. Section 7(b)(1) provides:

> The Administrator shall establish a rate or rates of general application for electric power sold to meet the general requirements of public body, cooperative, and Federal agency customers within the PNW, and loads of electric utilities under section 5(c). Such rate or rates shall recover the costs of that portion of the FBS resources needed to supply such loads until such sales exceed the FBS resources. Thereafter, such rate or rates shall recover the cost of additional electric power as needed to supply such loads, first from the electric power acquired by the Administrator under section 5(c) and then from other resources.

16 U.S.C. §839e(b)(1).

BPA is expressly complying with this provision. The FBS is a single resource pool and is not divided into separately priced portions that serve any particular customer class. As noted earlier, BPA has the authority to replace reductions in the capability of the FBS resources. BPA also has authority to purchase power to meet its forecasted contractual obligations to its customers. The amount of BPA's proposed augmentation purchases is well below the amount of the reductions in the capability of the FBS that BPA is authorized to replace. BPA's purchases, as FBS replacements, increase the size of the FBS. However, BPA's rates for preference customers and Federal agency customers are still recovering the costs of only that portion of the FBS resources needed to supply such loads. Remaining FBS resources are allocated in accordance with the rate directives. The Northwest Power Act expressly recognizes that the FBS may exceed the requirements of its preference customers. For example, section 7(f) of the Northwest Power Act notes that "all other firm power sold by the Administrator for use in the PNW shall be based upon the cost of the portions of *FBS resources*, purchases of power under section 5(c) of this Northwest Power Act and additional resources which, in the determination of the Administrator, are applicable to such sales." 16 U.S.C. §839e(f) (emphasis added). It is therefore, clear that section 7(b)(1) does not prohibit purchases to replace reductions in the capability of the FBS.

Once the FBS was determined, BPA properly allocated to the PF Preference rate "the costs of that portion of the FBS resources needed to supply such loads." 16 U.S.C. §839e(b)(1).

WPAG notes that BPA is proposing an RL rate to provide requirements service to IOUs. WPAG Brief, WP-02-B-WA-01, at 7. Without citation to evidence, WPAG argues that the fact that the RL rate is a requirements rate is to avoid recall provisions to which BPA's surplus power sales are subject. *Id.* BPA did not propose requirements sales to IOUs simply to avoid recall provisions for sales of surplus power. BPA is authorized to make sales to IOUs under a number of statutory provisions. BPA may sell requirements power to the IOUs under section 5(b) of the Northwest Power Act. 16 U.S.C. §839c(b). BPA may sell in-lieu power to the IOUs under section 5(c)(5) of the Northwest Power Act. 16 U.S.C. §839c(c)(5). BPA may also sell power to the IOUs pursuant to section 5(f) of the Northwest Power Act. 16 U.S.C. §839c(f). BPA determined that it is appropriate to offer requirements power to the IOUs, because the IOUs have a right to such power purchases, and such power sales were an appropriate part of the consideration for the proposed Residential Exchange settlements. Doubleday *et al.*, WP-02-E-BPA-44, at 13. In addition, in the Subscription Strategy, BPA concluded that net requirements power sales could be a component of a settlement of the REP with the IOUs. Leathley *et al.*, WP-02-E-BPA-19, at 9. There is no requirement that BPA must sell the IOUs only surplus power for Residential Exchange settlements. *See* 16 U.S.C. §832a(f).

WPAG argues that augmentation costs must be allocated to the RL rate. WPAG Ex. Brief, WP-02-R-WA-01, at 2. WPAG also argues that the RL rate is inconsistent with the resource cost allocations of section 7(f) of the Northwest Power Act, because it does not include all of the costs of power that BPA will acquire for serving the IOU loads. WPAG Brief, WP-02-B-WA-01, at 7. These arguments are not persuasive. As noted above, the Northwest Power Act does not prohibit BPA from acquiring power to replace the FBS and to meet its forecasted contractual load obligations. Furthermore, the costs of system augmentation purchases that replace some of these reductions in capability of the FBS are melded with all other FBS resource costs before cost allocation to rate pools is performed. Doubleday *et al.*, WP-02-E-BPA-44, at 7. BPA, therefore has not, as alleged by WPAG, acquired power for the purpose of serving particular IOU loads or any other particular load. The costs of the FBS, including FBS replacements, are allocated to all rate classes served by the FBS. *Id.* Because BPA's preference customers are served with FBS resources, they bear some of these costs. *Id.* This treatment is consistent with BPA's Subscription Strategy goals of spreading the benefits of Federal power widely in the region while avoiding a PF Preference rate increase. *Id.* at 10-11. *See* Burns and Elizalde, WP-02-E-BPA-08, at 7.

Furthermore, in the Subscription Step, BPA assumes that the 1,000 aMW sale to as-yet unidentified Northwest customers under the FPS-96 rate schedule in the Rate Design Step no longer occurs, and is replaced by a sale to the IOUs at either the RL-02 or the PF Exchange Subscription rate. Leathley *et al.*, WP-02-E-BPA-19, at 13. The costs recovered by the FPS sale in the Rate Design Step are the same basic costs recovered by the RL/PF Exchange Subscription sale. *Id.* This provides the foundation for establishment of the RL-02 rate. *Id.* The FPS-96 rate is a section 7(f) rate, and costs are allocated to FPS loads following the 7(f) rate directives. The RL rate cost basis in the Subscription Step, as discussed above, is based on an FPS-96 cost basis in the Rate Design Step. Therefore, the RL rate cost basis is supported by the 7(f) rate directives.

In addition, section 7(f) of the Northwest Power Act supports the development of the RL rate. Section 7(f) provides:

> Rates for all other firm power sold by the Administrator for use in the PNW shall be based upon the cost of the portions of FBS resources, purchases of power under section 5(c) of this Northwest Power Act and additional resources which, in the determination of the Administrator, are applicable to such sales.

16 U.S.C. §839e(f).

These "other firm power" sales include requirements sales to regional IOUs. The legislative history of the Northwest Power Act establishes that BPA may establish more than one rate under section 7(f). The report of the House Committee on Interstate and Foreign Commerce states:

> Section 7(f) establishes the rate or rates for sales to IOUs other than sales pursuant to the section 5(c) exchange, preference customers for power needed to meet the requirements of new large single "loads" and all other miscellaneous sales. This rate has sometimes been called a new resource rate and *does not preclude the establishment of more than one rate under this provision if circumstances make a separate rate for a separate load or demand necessary or appropriate*.

H.R. Rep. No. 976, 96th Cong. 2d Sess. 69 (1980) (emphasis added).

As established in BPA's testimony, current circumstances make the establishment of a separate rate for a separate IOU load or demand both necessary and appropriate. Leathley *et al.*, WP-02-E-BPA-19, at 9. IOUs have the right to make net requirements power purchases from BPA. 16 U.S.C. §839c(b)(1). IOUs have the right to participate in the REP. 16 U.S.C. §839c(c). In its Subscription Strategy, as noted above, BPA concluded that net requirements power sales could be a component of a settlement of the REP with the IOUs. Leathley *et al.*, WP-02-E-BPA-19, at 9.

As noted above, current circumstances make the establishment of a separate rate for a specified separate IOU load or demand both necessary and appropriate. *Id.* These circumstances involve, in part, the REP. *Id.* The REP has been in existence since shortly after enactment of the Northwest Power Act. *Id.* BPA has implemented the program for approximately 18 years. *Id.* During that time, BPA has learned what is required to implement the program and the costs and benefits of implementing the program. *Id.* For example, BPA must negotiate RPSAs with exchanging utilities. *Id.* These negotiations are contentious, lengthy, and demanding of the agency's and customers' resources. *Id.* at 9-10. Disputes regarding implementation of the RPSAs and the litigation of such disputes require additional resources to resolve. *Id.* at 10.

In addition, BPA establishes an ASC Methodology, which is used to calculate the ASCs of exchanging utilities. *Id.* The administrative establishment or revision of the ASC Methodology is extremely contentious. *Id.* Revision of the ASC Methodology in 1984 led to extensive disagreements and litigation among BPA customers and other interested parties in the region. *Id.* This process and litigation proved expensive and taxing for all parties. *Id.*

In implementing the REP, BPA must also review ASC filings made by the exchanging utilities. *Id.* The utilities' ASC filings can be great in number and extremely technical. *Id.* BPA's review of the ASC filings demands the dedication of numerous BPA employees or contract employees, or both. *Id.* BPA's ASC reports are then filed by the IOUs with FERC for review. *Id.* These reviews are also contentious and demand the expenditure of BPA's, the utilities' and interested parties' resources. *Id.* The exchanging utilities can also appeal FERC's decisions to the United States Court of Appeals for the Ninth Circuit. *Id.* These reviews are also contentious and demand the expenditure of BPA's, the utilities' and interested parties' resources. *Id.*

Furthermore, the determination of exchange benefits, as noted previously, is based in part on the level of the applicable PF Exchange rate. *Id.* If the PF Exchange rate is low, benefits are increased. *Id.* If the PF Exchange rate is high, benefits are reduced. *Id.* This leads to additional contentiousness in BPA's rate hearings. *Id.* BPA's rates are reviewed by FERC for confirmation and approval and may be appealed to the United States Court of Appeals for the Ninth Circuit. *Id.* These reviews are also contentious and demand the expenditure of BPA's, the utilities' and interested parties' resources. *Id.*

In light of these difficulties, beginning in 1981, BPA and exchanging utilities executed RPSAs for 20 year terms. *Id.* Between 1981 and today, all of these RPSAs have been settled except for one, which is between BPA and a utility in deemer status. *Id.* at 10-11. (Deemer status is where a utility sets its ASC equal to BPA's PF Exchange rate and does not receive positive benefits, but accrues a negative balance that must be eliminated before resuming the receipt of positive benefits.) *Id.* at 11. *See* Boling and Doubleday, WP-02-E-BPA-30. This extremely large number of Residential Exchange settlements reflects the nature and benefits of such settlements. Leathley *et al.*, WP-02-E-BPA-19, at 11. Parties are able to avoid the contentiousness of the myriad Residential Exchange issues, thereby saving significant administrative and legal expenses. *Id.* Parties receive known benefits instead of guessing future benefits due to changes in the ASC Methodology, the determination of ASC reports, and the development of wholesale power rates. *Id.* This enables parties to engage in better financial planning. *Id.*

The foregoing circumstances support the development of the RL rate. *Id.* The RL-02 rate applies only to net requirements sales to IOUs where the IOUs agree to a settlement of the REP. *Id.* As noted in BPA's Subscription Strategy:

> In Subscription, BPA proposes a settlement in which residential and small farm loads of the IOUs will be assured access to the equivalent of 1,800 aMW of Federal power for the 2002-2006 period. Of this amount, at least 1,000 aMW will be met with actual power deliveries, depending on which approach is most cost-effective for BPA.

Id.

While BPA proposed to offer a settlement based on the equivalent of 1,800 or 1,900 aMW of Federal power, the residential and small farm loads of the IOUs that will be eligible for participation in the Residential Exchange after 2001 total approximately 4,500 aMW. *Id.* Thus, under the proposed settlement, the IOUs are foregoing their rights to exchange their total

residential and small farm loads for the receipt of the equivalent of 1,800 [1,900] aMW of Federal power, a much smaller amount than their total exchangeable loads. *Id.*

In addition, BPA does not know whether the IOUs will continue the traditional REP or will choose to participate in a settlement of the REP through Subscription. *Id.* at 11-12. BPA has therefore developed rates that will apply under each scenario. *Id.* at 12.

Additional support for the RL-02 rate is found in the manner in which Federal power is made available to BPA's customers. *Id.* at 13. As noted previously, the REP provides a monetary form of access to Federal power for regional utilities. *Id.* In recent years, however, the benefits available to the residential consumers of IOUs from the REP have decreased substantially from the benefits provided in earlier years. *Id.* Because of the decline in these benefits, certain parties have argued that the residential consumers of the region's IOUs are being denied proper access to Federal power. *Id.* Under Subscription, BPA proposed a settlement of the REP in which IOUs could purchase Federal power for a portion of their net requirements loads at competitive rates. *Id.* BPA believes that providing the IOUs the ability to purchase a specified amount of power at competitive rates contributes to the widespread use of Federal power. *Id.*

The establishment of the RL-02 rate is also consistent with regional discussions in the Comprehensive Review and in the development of BPA's Subscription Strategy. *Id.* In the Comprehensive Review, the Steering Committee encouraged parties to continue settlement discussions and to explore other paths to ensure that residential and small farm loads receive an equitable share of the benefits of the Federal system. *Id.;* Comprehensive Review, Final Report, at 14. The Comprehensive Review also noted the desire to make power sales to BPA's customers at cost. Leathley *et al.*, WP-02-E-BPA-19, at 13. While the Final Report did not expressly state that all BPA rates would be equal, some customer groups suggested that this was the basic intent. *Id.* at 13-14. These positions were reflected in comments made during the Subscription process by certain customer groups, including the IOUs and the DSIs, regarding their respective rates. *Id.* at 14. In the Subscription Strategy, BPA acknowledged these parties' understandings, stating BPA's expectation that "[t]hese sales [to IOUs] will be at a rate approximately equal to the PF Preference rate, subject to establishment in BPA's rate case and consistent with BPA's rate directives." *Id.;* Subscription Strategy at 16.

WPAG argues that the RL rate is arbitrarily set at a level equal to the PF Preference rate. WPAG Brief, WP-02-B-WA-01, at 8. This argument is refuted by the record. As noted in BPA's Subscription Strategy, which contemplates the traditional REP as well as proposed settlements of that program, BPA's goals include spreading the benefits of Federal power and avoiding increases in BPA's PF Preference rate. *See* Burns and Elizalde, WP-02-E-BPA-08, at 7. In the past, BPA's general business goals have also been to provide rate stability in the region while serving BPA's loads. Doubleday *et al.*, WP-02-E-BPA-44, at 6. The Subscription Strategy goals mentioned above are the latest expression of these long-held business goals. *Id.* BPA has determined that it can provide 1,000 aMW of additional power to its customers and not increase the PF Preference rate. *Id.* BPA has assumed an FPS rate equal to the 1996 PF Preference rate as a reasonable price for such sales. *Id.* BPA's proposed sale of 1,000 aMW in the Rate Design Step is consistent with the Subscription Strategy and is also consistent with BPA's long-held business goals. *Id.* In the Subscription Step, BPA assumes that the IOUs accept the Subscription settlement proposal and that 1,000 aMW is made available to the IOUs in

power and 800 [900] aMW in monetary benefits. *Id.* *See* Leathley *et al.*, WP-02-E-BPA-19, at 12. The costs recovered by the FPS sale in the Rate Design Step are the same basic costs recovered by the RL/PF Exchange Subscription sale. This provides the foundation for establishment of the RL-02 rate. Leathley *et al.*, WP-02-E-BPA-19, at 13. Therefore, at the beginning of the Subscription Step, the RL rate is set at a PF-96 equivalent level. This level is similar to the PF-02 level. The Subscription Step section takes the results of the Rate Design Step and adjusts them by the added credits and costs associated with BPA's Subscription Strategy policies. Doubleday *et al.*, WP-02-E-BPA-18, at 17. In the Subscription Step, the RAM equitably allocates the net cost of the REP credit, a benefit not otherwise allocated under section 7 of the Northwest Power Act, to the PF Preference class, the IP-02 class, and the RL-02 class. *Id.* at 19. This allocation of credits achieves the Subscription Strategy expectation that PF Preference class customers, IP-02 class customers, and RL-02 class customers would pay similar rates for similar products, while maintaining the PF-IP relationship in section 7(c) of the Northwest Power Act. *Id.* *See* Wholesale Power Rate Development Study Documentation, WP-02-E-BPA-05A, section 2.4, Tables SUBSCR 01, SUBSCR 02, SUBSCR 03, SUBSCR 04. As shown by the well-documented and logical steps above, BPA was not arbitrary in setting the RL rate at a level equal to the PF Preference rate.

WPAG argues that in BPA's initial proposal, BPA proposed that up to 800 [900] aMW of the proposed settlement would be provided to the IOUs as a cash payment. WPAG Ex. Brief, WP-02-R-WA-01, at 5, citing Leathley *et al.*, WP-02-E-BPA-19, at 12, 19. The cited testimony, however, does not contain the statements alleged by WPAG. There is no mention of the 800 [900] aMW portion of the IOU settlements on page 12 of the cited testimony, and there is no page 19 of the cited testimony. WPAG argues that BPA now takes the position that the cash payment portion of the settlement is not part of the rate case, but will be decided in a separate process. *Id.*, citing Draft ROD, WP-02-A-01, at 12-21. BPA does not understand this assertion. First, WPAG's citation relates only to a reiteration of BPA's Subscription Strategy regarding the proposed IOU settlements. It simply notes that BPA proposes a minimum of 1,000 aMW of power and 800 [900] aMW of monetary benefits. Leathley *et al.*, WP-02-E-BPA-19, at 12-13, 16. Ever since the issuance of BPA's Subscription Strategy, BPA's IOU settlement proposal has always been to provide 1,000 aMW of power and 800 [900] aMW of monetary benefits. *Id.* The monetary benefits will be calculated on the basis of the difference between BPA's five-year flat-block market price forecast and the rate that the IOUs pay for their Subscription power purchases. *Id.* Both BPA's five-year flat-block market price forecast and the rate that the IOUs pay for their Subscription power purchases are issues that are resolved in the rate case. In addition, the IOU settlement agreements must be negotiated between the parties. In the case of the proposed IOU settlement agreements, BPA has established that BPA will be conducting a 30-day public comment process on the proposed settlements in which parties may comment on issues regarding the propriety of the proposed settlements. WPAG argues that this contradicts BPA's argument that in order to perform the Subscription Step, BPA assumes that the IOUs accept the proposed settlement, with 1,000 aMW delivered as actual power and 800 [900] aMW provided as monetary benefits. WPAG Ex. Brief, WP-02-R-WA-01, at 5, citing Draft ROD, WP-02-A-01, at 12-10. WPAG argues that if the amount and costs of monetary benefits to be provided to the IOUs under the proposed settlement were used as an integral part of the case to calculate the RL rate in the Subscription Step, they cannot be treated as a separate matter to be dealt with outside of the rate case when the legality of the cash

payments under the Northwest Power Act rate directives is called into question. *Id*. at 5-6. BPA believes that WPAG misunderstands BPA's proposal. BPA has been consistently clear that its IOU settlement proposal is for 1,800 aMW (now 1,900 aMW), which is comprised of forecasted minimum power sales of 1,000 aMW and 800 [900] aMW of monetary benefits. Leathley *et al*., WP-02-E-BPA-19, at 12-13, 16. With this information, BPA can develop the costs that are used to develop the RL rate in the Subscription Step. The actual negotiation and development of the settlement agreements are not conducted in the rate case but will reflect this structure. *Id*. Cash payments are not being made under the Northwest Power Act's rate directives. Rather, under the settlement authority granted BPA under section 2(f) of the Bonneville Project Act and as affirmed in section 9(a) of the Northwest Power Act, BPA is using endpoints established in BPA's rate case as the basis for calculating the monetary settlement benefits. It is appropriate to reflect the proposed power and monetary elements of the settlement, because BPA must forecast its loads and resources for the coming rate period and, given that BPA has proposed to offer REP settlements to the IOUs, the best information available must be used to reflect those proposed offers in BPA's rates. BPA believes that its settlement proposal is lawful and BPA is using the best information available to forecast the costs of the proposed settlements.

WPAG argues that including a monetary payment obligation in conjunction with a rate that is providing requirements service is beyond BPA's authority under section 7(f) of the Northwest Power Act. WPAG Ex. Brief, WP-02-R-WA-01, at 6. Again, section 7(f) of the Northwest Power Act is the statutory provision that provides for the establishment of rates for net requirements sales to IOUs. 16 U.S.C. §839e(f). BPA is using section 7(f) to establish the RL rate. The use of the RL rate as one endpoint in the calculation of monetary settlement payments is perfectly consistent with section 7(f). The difference between BPA's five year flat-block price forecast and the rate paid by the IOUs for the settlement power sales has long been the basis of the proposed settlement that provides the IOUs appropriate consideration for the termination of their participation in the REP. Leathley *et al*., WP-02-E-BPA-19, at 12-13, 16. These endpoints could have been other items, such as a fixed numerical point or an index. The RL rate is used as an endpoint in calculating the monetary payment portion of the settlement to establish appropriate consideration for the settlement. This is perfectly consistent with the Northwest Power Act.

WPAG argues that while section 2(f) of the Bonneville Project Act grants BPA the authority to settle claims, it is a prerequisite that a claim actually be asserted. WPAG Ex. Brief, WP-02-R-WA-01, at 6. WPAG argues that the record is bereft of any claim by the IOUs cognizable under section 2(f) of the Bonneville Project Act. *Id*. WPAG argues that the Draft ROD attempts to remedy this absence by listing a number of future problems that may be asserted by a party under the REP to be implemented in 2001. *Id*., citing Draft ROD, WP-02-A-01, at 12-24. WPAG argues that this attempt to manufacture a claim is of no avail, since mere assertions in a brief do not constitute evidence in the record. *Id*. WPAG has mischaracterized BPA's Draft ROD and the record in this proceeding. BPA expressly noted the obvious, that the IOUs' outstanding claim is the prospective implementation of the REP under RPSAs during the coming rate and contract periods. Draft ROD, WP-02-A-01, at 12-24; Leathley *et al*., WP-02-E-BPA-19, at 11. BPA also noted that the IOUs' claim is their statutory *right* to participate in the REP. 16 U.S.C. 839c(c)(1). As the record shows, this is a substantial claim, involving some $183 million in BPA's initial proposal, Wholesale Power Rate

Development Study Documentation, WP-02-E-BPA-05A, at 91, and $240 million during the coming rate period, Wholesale Power Rate Development Study Documentation, WP-02-FS-BPA-05A. BPA also explained the many reasons supporting previous settlements of the REP, which also apply to settlements of the implementation of the program in the next rate period. Leathley, *et al*., WP-02-E-BPA-19, at 8-14. *Id*. There can be no dispute that this extensive information is in the record. This record evidence clearly establishes the IOUs' claim that is the basis for the settlement.

WPAG argues that BPA's interpretation of its settlement authority under section 2(f) would render the Northwest Power Act's rate directives meaningless. WPAG Ex. Brief, WP-02-R-WA-01, at 7. WPAG argues that BPA's interpretation would have made it unnecessary to include sections 5(c) and 7(b) in the Northwest Power Act in order to implement the REP, because BPA already had the authority to make cash payments to the IOUs as part of a sale of requirements power in order to settle claims that had not yet been asserted. *Id*. This argument is based on faulty logic. Sections 5(c) and 7(b) of the Northwest Power Act are necessary elements for the existence of the REP. The REP is based on the determination of a utility's ASC, the determination of the PF Exchange rate, the determination of the utility's residential load, and many other factors. 16 U.S.C. §839c(c); Boling *et al*., WP-02-E-BPA-30. Sales of power and money do not create an REP. The REP is a statutory right of regional utilities for which participation can be terminated through a settlement. WPAG's argument is also based on faulty presumptions. First, as explained above and in greater detail in BPA's testimony cited above, the IOUs have a claim that has been asserted. The IOUs have a statutory *right* to participate in the REP. 16 U.S.C. §839c(c)(1). As noted in BPA's Letter Request for Comment on Prototype RPSA and IOU Settlement Agreements, IOUs must request participation under section 5(c) of the Northwest Power Act in order to have an RPSA or settlement agreement. Because BPA does not know its load obligations at this time, BPA must forecast the IOUs' participation in the proposed settlements. BPA is therefore not making cash payments as part of requirements sales for claims that have not been asserted. While any settlement agreements will not be effective until such agreements are executed by the parties, BPA must forecast the IOUs' settlement of their rights to participation in the REP and develop rates that apply to the proposed settlements.

WPAG argues that section 2(f) of the Bonneville Project Act does not grant BPA authority to set requirements rates in a manner that is not authorized by section 7 of the Northwest Power Act. WPAG Ex. Brief, WP-02-R-WA-01, at 7. WPAG argues that the only rate under which BPA is authorized by the Northwest Power Act to make cash payments is section 7(b) in conjunction with the REP established in section 5(c). *Id*. WPAG argues that BPA cannot use section 2(f) to create ratemaking authority it lacks under section 7(f) of the Northwest Power Act. *Id*. WPAG misunderstands BPA's proposed settlements. BPA is not relying on section 2(f) to set any requirements rates. BPA is relying on section 7(f) of the Northwest Power Act, 16 U.S.C. §839e(f), its legislative history, and testimony to develop the RL rate. *See* Leathley *et al*., WP-02-E-BPA-19, at 8-14; 16 U.S.C. §839e(f). Section 7(f) power sales include requirements sales to regional IOUs. The legislative history of the Northwest Power Act establishes that BPA may establish more than one rate under section 7(f). The report of the House Committee on Interstate and Foreign Commerce states:

> Section 7(f) establishes the rate or rates for sales to IOUs other than sales pursuant to the section 5(c) exchange, preference customers for power needed to meet the requirements of new large single "loads" and all other miscellaneous sales. This rate has sometimes been called a new resource rate and *does not preclude the establishment of more than one rate under this provision if circumstances make a separate rate for a separate load or demand necessary or appropriate*.

H.R. Rep. No. 976, 96th Cong. 2d Sess. 69 (1980) (emphasis added).

As established in BPA's testimony, current circumstances make the establishment of a separate rate for a separate IOU load or demand both necessary and appropriate. Leathley *et al.*, WP-02-E-BPA-19, at 9. IOUs have the right to make net requirements power purchases from BPA. 16 U.S.C. §839c(b)(1). IOUs have the right to participate in the REP. 16 U.S.C. §839c(c). In its Subscription Strategy, as noted above, BPA concluded that net requirements power sales could be a component of a settlement of the REP with the IOUs. Leathley *et al.*, WP-02-E-BPA-19, at 9. BPA has therefore not used section 2(f) of the Bonneville Project Act to establish the RL rate.

As noted above, WPAG argues that the only rate under which BPA is authorized by the Northwest Power Act to make cash payments is section 7(b) in conjunction with the REP established in section 5(c). WPAG Ex. Brief, WP-02-R-WA-01, at 7. The implementation of the traditional REP, however, uses a section 7(b) rate, the PF Exchange rate, which is compared with the utility's ASC and then multiplied by the utility's eligible residential load to produce REP benefits, which have traditionally been monetary, but which can be comprised of actual power sales. 16 U.S.C. §839c(c); 16 U.S.C. §839c(c)(5). WPAG is incorrect in its underlying assumption that the section 7(b) rate itself authorizes cash payments. It does not. The *REP* authorizes cash payments based on the comparison ASC and the PF Exchange rate. WPAG ignores another manner in which BPA can make monetary payments under the Bonneville Project Act and the Northwest Power Act. Section 2(f) of the Bonneville Project Act provides:

> Subject only to the provisions of this chapter, the Administrator is authorized to enter into such contracts, agreements, and arrangements, including the amendment, modification, adjustment, or cancellation thereof and the compromise or final settlement of any claim arising thereunder, *and to make such expenditures, upon such terms and conditions and in such manner as [she] may deem necessary*.

16 U.S.C. §832a(f) (emphasis added). This authority was reaffirmed in section 9(a) of the Northwest Power Act. 16 U.S.C. §839f(a). It is clear that the Administrator can make expenditures for settlements in such manner as she deems necessary, including the comparison of two endpoints--the five-year flat-block market forecast of power and the RL rate--to calculate monetary benefits for the IOU settlements.

WPAG argues that the RL rate contains a provision under which the purchaser receives a cash payment equal to the difference between the market price of power and the rate under which it is buying power from BPA. WPAG Brief, WP-02-B-WA-01, at 8. WPAG argues that the rate

directives in section 7 do not grant BPA the authority to establish a cash payment program for customers as part of a requirements power rate. *Id.* WPAG argues that designating the Residential Exchange settlements as settlements does not permit institution of a cash payment program under the auspices of a requirements rate. *Id.* WPAG misunderstands the RL rate. The RL rate does not contain a provision under which the purchaser receives a cash payment equal to the difference between the market price of power and the rate under which it is buying power from BPA. *See* Wholesale Power Rate Schedules, WP-02-E-BPA-07, at 30-34. While WPAG argues that the rate directives in section 7 do not grant BPA the authority to establish a cash payment program for customers as part of a requirements power rate, BPA has not established a cash payment program for customers in the RL rate. BPA's Subscription Strategy proposes a settlement of the REP with regional IOUs in which residential and small farm loads of the IOUs will be assured access to the equivalent of 1,800 [1,900] aMW of Federal power for the FY 2002-2006 period (and 2,200 aMW for the FY 2007-2011 period). Leathley *et al.*, WP-02-E-BPA-19, at 16. Of this amount, at least 1,000 aMW will be met with actual power deliveries. *Id.* The remaining 800 [900] aMW will be provided in the form of either power or monetary benefits, depending on which approach is most cost-effective for BPA. *Id.* This determination, as well as the amount of power and monetary benefits offered to each IOU, will be made in a separate process. *Id.* The monetary benefits will be based on the difference between the five-year flat-block market price of power forecasted in the rate case and the rate used to make Subscription sales to the IOUs (the RL-02 or the PF Exchange Subscription rate). *Id.*

Therefore, BPA's proposed settlements, if executed, will establish the monetary payment program as an element of that settlement, not the RL rate. BPA is not permitting institution of a cash payment program under the auspices of a requirements rate. The calculation of monetary benefits for a settlement must be based on some standard. Using the difference between the five-year flat-block market price of power forecasted in the rate case and the rate used to make Subscription sales to the IOUs, as provided in the Subscription Strategy, is a reasonable method for determining the monetary element of the settlement. The fact that the RL rate is a reference point in calculating such benefits does not mean that the RL rate establishes such a program.

WPAG admits that section 2(f) of the Bonneville Project Act provides BPA the authority to settle claims. WPAG Brief, WP-02-B-WA-01, at 8. WPAG argues that this authority does not establish authority to create rates for requirements service that contravene the rate directives of section 7(f) of the Northwest Power Act. *Id.* WPAG argues that this is particularly the case when the record is devoid of any outstanding claim between BPA and the customers to whom it is offering the RL rate. *Id.* Section 2(f) of the Bonneville Project Act provides:

> Subject only to the provisions of this chapter, the Administrator is authorized to enter into such contracts, agreements, and arrangements, including the amendment, modification, adjustment, or cancellation thereof and the compromise or final settlement of any claim arising thereunder, and to make such expenditures, upon such terms and conditions and in such manner as [she] may deem necessary.

16 U.S.C. §832a(f).

This provision grants broad discretion to the Administrator in the settlement of claims. This authority was affirmed in section 9(a) of the Northwest Power Act. 16 U.S.C. §839f(a). *See Utility Reform Project v. Bonneville Power Admin.*, 869 F.2d 437, 442-443 (9th Cir. 1989). This authority supports BPA's proposed Subscription settlements with the IOUs. However, BPA is not simply relying on this authority for the establishment of the RL rate or to establish any rate, much less a rate that would contravene the rate directives of section 7 of the Northwest Power Act. The RL rate, as discussed above, is consistent with the rate directives and legislative history of the Northwest Power Act. While WPAG argues that the record is devoid of any outstanding claim between BPA and the customers to whom it is offering the RL rate, this is incorrect. The outstanding claim is the prospective implementation of the REP under RPSAs during the coming rate and contract periods. Regional utilities have a right to participate in the REP. 16 U.S.C. §839c(c)(1). BPA previously explained the reasons supporting previous settlements of the REP, which also apply to settlements of the implementation of the program in the next rate period. *See* Leathley *et al.*, WP-02-E-BPA-19.

WPAG argues that assuming, *arguendo*, that BPA has the authority to establish the RL rate, BPA is offering the rate in an arbitrary and discriminatory fashion because it is being offered only to IOUs and not to preference customers that participate in the REP. WPAG Brief, WP-02-B-WA-01, at 9. As noted in the extensive preceding discussion in this ROD regarding the development of the RL rate, it clearly has not been developed in an arbitrary fashion. *See* Leathley *et al*., WP-02-E-BPA-19, at 8-14; Doubleday *et al*., WP-02-E-BPA-18, at 14-18; Doubleday *et al*., WP-02-E-BPA-44, at 5-9. With regard to the argument that the rate is being offered in an arbitrary fashion, BPA also disagrees. BPA's reasons for developing and offering IOU settlement power at the RL rate date back to BPA's Subscription Strategy. *See* Subscription Strategy, at 8-10, 16-17. One of the goals of the Subscription Strategy was to "spread the benefits of the FCRPS as broadly as possible with special attention given to residential and rural customers of the region." Subscription Strategy, at 3. One manner in which this was achieved was BPA's proposed settlement of the REP with the IOUs. *Id*. at 8-10. Additional support for offering power at the RL rate to the IOUs is presented in this ROD at great length. *See, e.g.*, Leathley *et al*., WP-02-E-BPA-19, at 8-14. In summary, the RL rate is not being offered in an arbitrary fashion. With regard to the argument that the RL rate is discriminatory, BPA disagrees. Reasons supporting the offer of the REP settlement to regional IOUs are discussed elsewhere. *See, e.g.*, Leathley *et al*., WP-02-E-BPA-19, at 8-14. In any event, however, the courts have recognized that BPA's rate directives do not establish a non-discrimination requirement. *Southern California Edison Co. v. Jura*, 909 F.2d 339, 343-344 (9th Cir. 1990) (challenging BPA's nonfirm energy rates under section 7(k) of the Northwest Power Act). With regard to the argument that the RL rate is being offered in a discriminatory manner, BPA disagrees. The RL rate is a rate developed under section 7(f) of the Northwest Power Act. 16 U.S.C. §839e(f). The rates for requirements service for IOUs are different than the rates for requirements service for BPA's preference customers. Compare 16 U.S.C. §839e(b)(1) with 16 U.S.C. §839e(f). BPA is not offering the RL rate in a discriminatory manner: BPA, under law, can only offer requirements power to the IOUs at a rate established under section 7(f) of the Northwest Power Act, the RL rate, and not to preference customers, who must, under section 7(b)(1) of the Northwest Power Act, pay the PF rate for requirements service. Indeed, preference customers do

not need to purchase power at the RL rate, because they can purchase the exact same product at the exact same price (although under a different rate) by making such purchases at the PF rate.

The PPC notes that the exchange settlements are proposed to be offered to regional IOUs, but have not been proposed to be offered to other regional utilities participating in the REP. PPC Brief, WP-02-B-PP-01, at 64. WPAG argues that this is troublesome, because some IOUs eligible for the RL rate have sold or may sell all of their non-Federal generating resources that were previously used to serve their retail load. WPAG Brief, WP-02-B-WA-01, at 9. (A discussion of this issue is contained in ROD section 14.3.) As noted elsewhere in this ROD, BPA spent years with its customers and other interested parties developing BPA's Subscription Strategy. One element of this Strategy was the proposal of a settlement of the REP with regional IOUs. The Subscription Strategy did not address a proposed settlement of the REP with regional preference customers. The fact that BPA is proposing to offer a particular exchange settlement to the IOUs, however, does not mean that BPA will not offer an exchange settlement to BPA's exchanging preference customers. BPA has not yet completed discussions of potential exchange settlements with its exchanging preference customers, but BPA has not precluded doing so. Because those discussions have not yet concluded, it is not known whether the form of such settlements would be similar to that proposed for the IOUs or an approach that might better reflect the particular characteristics of preference utilities. Furthermore, BPA's rate case is to establish rates, not to determine whether BPA should offer a new exchange settlement to a particular customer class.

In any event, however, BPA is not required to offer the same settlement to all of BPA's customers. As noted above, section 2(f) of the Bonneville Project Act provides that the Administrator may enter into settlements "upon such terms and in such manner as [she] may deem necessary." 16 U.S.C. §832a(f). *See Utility Reform Project v. Bonneville Power Admin.*, 869 F.2d 437, 442-443 (9th Cir. 1989). It is appropriate to consider settlement proposals for different classes of BPA's customers. BPA's IOU customers differ from BPA's preference customers in many ways. For example, IOUs are for-profit companies, while preference customers are generally non-profit. IOUs are regulated by state utility commissions, while preference customers generally make decisions through their boards. IOUs do not have preference and priority to Federal power, while preference customers have such priority. IOUs have been the primary recipients of benefits under the REP, while preference customer benefits have been much smaller. In addition, numerous preference customers have already settled the REP through 2011 and do not require a settlement at this time. For many reasons, it is appropriate to offer the proposed settlement only to regional IOUs at this time.

WPAG argues that while BPA stated that it is proper to limit the RL rate to IOUs since settlement discussions with preference customers participating in the REP have not been completed, in fact no such discussions have been initiated and there is no evidence in the record that BPA intends to initiate settlement discussions with preference customers. WPAG Ex. Brief, WP-02-R-WA-01, at 8-9. WPAG argues that BPA's failure to initiate settlement discussions with preference customers is not a legal justification for excluding preference customers from the settlement proposed for the IOUs. *Id*. In response to these arguments, as noted previously, it is proper to limit the RL rate to IOUs because, under law, only IOUs may purchase requirements power from BPA under section 7(f) of the Northwest Power Act. In addition, the fact that BPA

is proposing to offer a particular exchange settlement to the IOUs does not mean that BPA will not offer an exchange settlement to BPA's exchanging preference customers. BPA noted that it had not completed discussions of potential exchange settlements with exchanging preference customers but has not precluded doing so. BPA did not mean to imply that such negotiations were currently underway with preference customers, but rather that BPA expected to have such discussions and such discussions have not yet occurred, or been completed. The issue, therefore, is not an issue of discrimination. It is simply an issue of timing. It should be noted, however, that while WPAG states that BPA has not initiated settlement discussions with its preference customers, BPA does not recall a request from WPAG to initiate settlement discussions with BPA. Settlement discussions can be initiated by either party. While WPAG claims that there is no evidence in the record that BPA intends to initiate discussions with preference customers, BPA did discuss some of the standards for the REP and the REP settlements in the context of both IOU and preference customers during the hearing. Tr. 1556-68. Settlements of the REP, however, do not have to be done at the same time or in the same manner for all exchanging utilities. Indeed, BPA's testimony noted that BPA had negotiated settlements of the REP with all but one utility. Leathley *et al*., WP-02-E-BPA-19, at 10-11. This includes IOUs and preference customers. BPA issued records of decision for REP settlements. Each settlement occurred with an individual utility or a group of utilities represented by an organization, such as the settlement agreement BPA executed with PNGC and nine PNGC members. The fact that BPA offered a settlement agreement to one utility or a group of utilities did not require BPA, in over 30 settlement agreements that BPA executed, to offer the same settlement to all other exchanging utilities. There are two classes of exchanging utilities--exchanging IOUs and exchanging preference customers. The settlements for such utilities need not be the same as offered to members of the other class. Therefore, contrary to WPAG's claim, BPA's settlement proposal to regional IOUs is not discriminatory, and certainly not unduly discriminatory, even though it is not currently offered to BPA's preference customers.

Decision

BPA properly developed the RL rate. BPA intends to acquire approximately 1,282 aMW of power purchases as FBS replacements.

12.4 Allocation of 7(b)(2) Amount

Issue

Whether BPA properly allocated the 7(b)(2) rate test trigger amount.

Parties' Positions

WPAG argues that BPA did not follow the statutory directive that requires that the trigger amount be allocated to all other rates under which power is sold by BPA. WPAG Brief, WP-02-B-WA-01, at 10-11; WPAG Ex. Brief, WP-02-R-WA-01, at 10-15. The PPC and OURCA argue that BPA should assign the costs identified through the section 7(b)(2) rate test to the forecasted load of the RL class. PPC Ex. Brief, WP-02-R-PP-01, at 16; OURCA Ex. Brief, WP-02-R-OU-01, at 8.

BPA's Position

BPA properly allocated the section 7(b)(2) trigger amount. Wholesale Power Rate Development Study, WP-02-E-BPA-05, at 63-65.

Evaluation of Positions

WPAG argues that section 7(b)(3) of the Northwest Power Act requires that the 7(b)(2) trigger amount be "recovered through supplemental rate charges for all other power sold by the Administrator to all other customers." WPAG Brief, WP-02-B-WA-01, at 10, WPAG Ex. Brief, WP-02-R-WA-01, at 10-11. WPAG argues that the trigger amount was allocated only to the PF Exchange, NR, and IP rates, and since BPA is forecasting that there will be no loads served under these rates during the rate period, the trigger amount ends up back in the PF rate. *Id.* WPAG argues that this deprives preference customers of the cost protection that the rate test was intended to provide them. *Id.* WPAG argues that proper allocation of the trigger amount would increase the RL rate. *Id.* WPAG argues that the trigger amount should be allocated to all power rates under which BPA intends to sell power to the IOUs and DSIs. *Id.*

First, WPAG and OURCA argue that the trigger amount was allocated only to the PF Exchange, NR, and IP rates, and BPA is forecasting that there will be no loads served under these rates during the rate period. WPAG Brief, WP-02-B-WA-01, at 10; OURCA Ex. Brief, WP-02-R-OU-01, at 8. This argument is incorrect. In this rate case, BPA does not know the manner in which IOUs will purchase power or receive Federal benefits from BPA. Leathley *et al*., WP-02-E-BPA-19, at 12. IOUs may continue the REP or participate in settlements of that program. The Rate Design Step reflects the circumstance where the IOUs participate in the REP. In this case, the Rate Design Step properly allocated the trigger amount to all other rates in that Step. *See* Wholesale Power Rate Development Study Documentation, WP-02-E-BPA-05A, at 72. This includes about 1,300 aMW of Residential Exchange load and 990 aMW of DSI load, and also NR load. BPA is not stating that no sales are forecasted for these loads. Instead, in the Rate Design Step, where the 7(b)(2) rate test is calculated, those loads are forecasted to occur. In addition, however, BPA must recognize the possibility that IOUs would execute the proposed settlement agreements. The record shows that the forecasted cost of the proposed settlements exceeds the forecasted net cost of the REP in the Rate Design Step. *See* Wholesale Power Rate Development Study Documentation, WP-02-E-BPA-05A, Table SUBSCR.01, lines 19 and 24. BPA must establish rates to recover its costs. Because BPA does not know which option the IOUs will pick, however, BPA must assume the highest-cost possibility in setting rates in order to ensure the recovery of its costs. Therefore, the development of rates based on costs in the Subscription Step does not mean that BPA is not forecasting loads to occur in the Rate Design Step. Further, costs are allocated to the other loads in the Rate Design Step.

WPAG argues that the trigger amount should be allocated to all power rates under which BPA intends to sell power to the IOUs and DSIs. WPAG Brief, WP-02-B-WA-01, at 10. The PPC and OURCA argue that BPA should assign the cost identified through the section 7(b)(2) rate test to the forecasted load of the RL class. PPC Ex. Brief, WP-02-R-PP-01, at 16; OURCA Ex. Brief, WP-02-R-OU-01, at 8. WPAG, OURCA and the PPC argue that the practical effect of

shielding the Subscription Step rates from their appropriate share of the rate test trigger amount is to shift such costs back to the PF rate, thereby depriving the preference customers of the cost protection that the rate test was intended to provide. WPAG Ex. Brief, WP-02-R-WA-01, at 11; OURCA Ex. Brief, WP-02-R-OU-01, at 8; PPC Ex. Brief, WP-02-R-PP-01, at 15. Given that BPA must develop rates to reflect two mutually exclusive scenarios in which IOUs may receive benefits from the Federal system, it is inappropriate that such amount be allocated to the RL and PF Exchange Subscription rates. As noted above, in the Rate Design Step of the RAM, the modeling assumes the full implementation of the traditional REP. Doubleday *et al.*, WP-02-E-BPA-18, at 15-16. The rate that is applicable to the traditional REP is the PF Exchange Program rate. Tr. 2277-78. Before the 7(b)(2) rate test is performed in the Rate Design Step, the PF Exchange Program rate and the PF Preference rate are equal, and are, in fact, one unbifurcated PF rate. *Id.* If the 7(b)(2) rate test triggers, an amount of PF Preference rate protection is calculated and allocated to all other rates, resulting in the bifurcation of the PF rate into the PF Exchange Program rate and the PF Preference rate. *Id.* The traditional REP is assumed in only the Rate Design Step. The PF Exchange Program rate is applicable in only the Rate Design Step. Therefore, the 7(b)(2) rate test used to determine the PF Exchange Program rate used in the implementation of the traditional REP is applicable to only the Rate Design Step. It also follows that rates not associated with the Rate Design Step, such as the RL and PF Exchange Subscription rates, would not be involved in the allocation of PF rate protection amounts calculated in the Rate Design Step. The PF rate protection amount is already fully allocated in the Rate Design Step before implementation of the Subscription Step in the RAM, where the RL, PF Exchange Subscription, and IP/IPTAC rates are calculated. *See* Wholesale Power Rate Development Study Documentation, WP-02-E-BPA-05A, at 72. In addition, the IP Indexed rate is not modeled in the RAM, with the assumption that the IP Indexed rate will recover the same revenues as the IP/IPTAC rate over the rate period. Miller *et al.*, WP-02-E-BPA-21, at 3.

It is inappropriate to allocate the trigger amount to the RL and PF Exchange Subscription rates for additional reasons. This requires a review of section 7(b)(3) of the Northwest Power Act. 16 U.S.C. §839e(b)(3). Section 7(b)(3) of the Northwest Power Act provides:

> Any amounts not charged to public body, cooperative, and Federal agency customers by reason of paragraph (2) of this subsection *shall be recovered through supplemental rate charges for all other power sold by the Administrator to all customers*. Rates charged public body, cooperative, or Federal agency customers pursuant to this subsection shall not include any costs or benefits of a net revenue surplus or deficiency occurring for the period ending June 30, 1985, to the extent such surplus or deficiency is caused by a difference between actual power deliveries and power deliveries projected for the purpose of establishing rates to direct service industrial customers under subsection (c)(1) of this subsection, and an overrecovery or underrecovery of the net costs incurred by the Administrator under section 5(c) as a result of such difference.
>
> Any such revenue surplus or deficiency incurred *shall be recovered from, or repaid to, customers over a reasonable period of time after July 1, 1985, through a supplemental rate charge or credit applied proportionately for all other power*

> *sold by the Administrator* at rates established under other subsections of this section prior to July 1, 1985.

16 U.S.C. §839e(b)(3) (emphasis added).

It is important to recognize the distinction drawn by Congress regarding the allocation of the costs under section 7(b)(3). For allocations of a net revenue surplus or deficiency under section 7(b)(3), such amounts are "recovered from, or repaid to, customers over a reasonable period of time after July 1, 1985, through a supplemental rate charge or credit applied proportionately for all other power sold by the Administrator." In other words, Congress knew how to provide for proportional allocations of the referenced costs and expressly did so. For general allocations of the 7(b)(2) trigger amount, however, Congress did not require a proportional allocation, but rather provided that such amounts are recovered through "supplemental rate charges for all other power sold by the Administrator to all customers." This means that BPA is not required to proportionally allocate the trigger amount to all other power sold by the Administrator to all customers. Nevertheless, BPA generally believes that such a proportional allocation is the appropriate means to allocate the trigger amount to BPA's power sales to non-preference customers.

As noted previously, BPA is facing special circumstances in the current rate case. BPA does not know the manner in which IOUs will purchase power or receive benefits from the Federal system, whether through the REP or through the proposed exchange settlements with IOUs. The principles for the proposed exchange settlements were developed in BPA's Subscription Strategy in order to establish an appropriate value to be provided by BPA (a minimum of 1,000 aMW of power at a rate expected to be approximately equivalent to the PF Preference rate and 800 [900] aMW in financial benefits) for the value provided by the IOUs (settlement of the REP). These settlements have not yet been offered or executed, and BPA must use the information available at this time in developing rates. The RL and PF Exchange Subscription rates are special rates used solely for the purpose of implementing proposed settlements of the REP. As noted above, it is inappropriate to allocate the trigger amount to these rates, because of the special circumstances and manner in which BPA had to develop rates in this proceeding (*see* previous discussion of Rate Design Step and Subscription Step). In addition, however, as noted above, BPA is not required to allocate the trigger amount on a proportional basis. This means that the amounts allocated to particular settlement sales may vary among the power sales to BPA's non-preference customers. Given the special nature of the RL and PF Exchange Subscription rates and that their use is strictly limited to proposed settlement sales, and that their proposed level is the appropriate level to establish the proper consideration for the settlement of the REP, it is appropriate that additional costs not be allocated to those rates. BPA emphasizes that this is a special circumstance and an exception to BPA's usual allocation of such amounts.

WPAG argues that the use of the word "proportionately" in the last sentence of section 7(b)(3) in conjunction with an unrelated credit or charge does not alter the language establishing the duty of the Administrator to spread to all other power sold to all customers the costs that must be excluded from the PF rate due to the rate test. WPAG Ex. Brief, WP-02-R-WA-01, at 14. WPAG goes on to argue that even assuming, *arguendo*, that BPA may not be statutorily required to allocate the rate test trigger proportionately to all non-preference rates, and may have the

freedom to choose how much is allocated to each of the rates other than the PF rate, this does not free BPA to make such allocation decisions in a manner that results in the preference customers paying any portion of the rate test trigger amount. *Id.* BPA disagrees with WPAG's allegation that the preference customers pay a portion of the rate test trigger amount. The current rate case is unique in that BPA must establish appropriate rates to be used in the traditional REP, as well as rates to be used in the event of a settlement of the REP. Doubleday *et al*., WP-02-E-BPA-18, at 16. To accommodate this unique situation, BPA's ratemaking process includes two rate modeling steps, a Rate Design Step and a Subscription Step. *Id*. at 14-20. The Rate Design Step produces rates that are appropriate for a world that includes the traditional REP. *Id*.

BPA conducts the section 7(b)(2) rate test in the Rate Design Step of the rates models. This is appropriate for a number of reasons. First, section 7(b)(2) of the Northwest Power Act provides that the absence of the traditional REP is one of the five section 7(b)(2) assumptions. 16 U.S.C. §839e(b)(2). Therefore, the section 7(b)(2) rate test must be performed in the Rate Design Step that includes the traditional REP, because, under law, rates must be compared between the Program Case, where the program exists, and the 7(b)(2) Case, where the program does not exist. The Rate Design Step is the only step that models the traditional REP. Doubleday *et al*., WP-02-E-BPA-18, at 16. In addition, if the section 7(b)(2) rate test triggers, the PF Preference rate protection costs are allocated to other firm loads in the Rate Design Step, including the IP rate and PF Exchange Program rate loads. 16 U.S.C. §839e(b)(3). This results in a bifurcation of the PF rate into a PF Preference rate and a PF Exchange Program rate, which occurs only in the Rate Design Step. *Id.* Therefore, in the Rate Design Step, the amount of preference customer rate protection is both calculated and allocated to all other loads. In this case, the Rate Design Step has properly allocated the rate test trigger amount from the PF Preference customers to all other rates in that Step. *See* Wholesale Power Rate Development Study Documentation, WP-02-E-BPA-05A, at 72. While BPA must calculate the 7(b)(2) rate test in the Rate Design Step, where the amount of the 7(b)(2) trigger is indeed allocated to other power sales, BPA must also comply with the statutory requirement to recover its total costs. 16 U.S.C. 839e(a)(1). In the Subscription Step, BPA assumes that regional IOUs execute proposed settlements of the REP. BPA must therefore calculate Subscription Step rates that recover the costs of such settlements. Where such settlements would impose higher costs on BPA, BPA must allocate such costs to rates. Doubleday *et al*., WP-02-E-BPA-18, at 17-18; Doubleday *et al*., WP-02-E-BPA-44, at 13. It would be inappropriate, however, to conduct the 7(b)(2) rate test in the Subscription Step, because one of the five section 7(b)(2) assumptions, the traditional REP, does not exist in the Subscription Step.

WPAG argues that the structure of the settlement proposed for the IOUs requires BPA to elect whether to allocate the rate test trigger amount to either the NR and PF Exchange Program rates, or the RL, PF Exchange Subscription and IP/IPTAC rates. WPAG Ex. Brief, WP-02-R-WA-02, at 11-12. BPA disagrees with WPAG's argument that BPA has a choice as to which set of rates the rate test trigger amount can be allocated. As stated above, the section 7(b)(2) rate test must be performed in the Rate Design Step, which includes the traditional REP, because, under law, rates must be compared between the Program Case, where the program exists, and the 7(b)(2) Case, where the program does not exist. The Rate Design Step is the only step that models the traditional REP. In addition, if the section 7(b)(2) rate test triggers, the PF Preference rate protection costs are allocated to other firm loads in the Rate Design Step, including the IP rate

and PF Exchange Program rate loads. 16 U.S.C. §839e(b)(3). This results in a bifurcation of the PF rate into a PF Preference rate and a PF Exchange Program rate, which occurs only in the Rate Design Step. Therefore, in the Rate Design Step, the amount of preference customer rate protection is both calculated and allocated to all other loads. In this case, the Rate Design Step has properly allocated the rate test trigger amount from the PF Preference customers to all other rates in that Step. Those Rate Design Step rates are the IP, NR, and PF Exchange Program rates. *See* Wholesale Power Rate Development Study Documentation, WP-02-E-BPA-05A, at 72.

WPAG argues that the fact that BPA has placed itself in an untenable position in its negotiations with the IOUs over the REP and the purported settlement does not absolve BPA of its responsibility to adhere to the requirements of sections 7(b)(2) and (3) of the Northwest Power Act, nor to provide its preference customers with the rate protection guaranteed to them by these statutory provisions. WPAG Ex. Brief, WP-02-R-WA-02, at 12. First, BPA has not placed itself in an untenable position in its negotiations with the IOUs. The principles of BPA's proposed IOU settlements were developed in the extensive public process used to develop BPA's Subscription Strategy. BPA's settlement proposal provides appropriate consideration, developed in a logical, consistent and lawful manner, in exchange for the rights of the IOUs to participate in the REP. Furthermore, BPA disagrees with WPAG's argument that BPA is not adhering to the requirements of sections 7(b)(2) and (3) of the Northwest Power Act. The section 7(b)(2) rate test is a statutorily required component of BPA's ratemaking process. The rate test involves the projection and comparison of two sets of wholesale power rates for the general requirements loads of BPA's public body, cooperative, and Federal agency customers (7(b)(2) or preference customers). The two sets of rates are: (1) a set for the rate filing test period (FY 2002-2006) and the ensuing four years (FY 2007-2010) assuming that section 7(b)(2) is not in effect (Program Case rates); and (2) a set for the same period taking into account the five assumptions listed in section 7(b)(2) Case rates). The 7(b)(2) Case rates are modeled exactly the same as the Program Case rates except for the five assumptions listed in section 7(b)(2). The five assumptions prescribed by section 7(b)(2) of the Northwest Power Act and used to model the 7(b)(2) Case are:

(1) Within or adjacent DSI loads are transferred to public utilities at the start of the 7(b)(2) rate test period; the remaining DSI loads are transferred to IOUs as BPA/DSI pre-Northwest Power Act contracts expire.

(2) *No section 5(c) REP takes place.*

(3) Additional resources of three specified types serve the loads of 7(b)(2) customers when FBS resources are exhausted.

(4) The DSI reserve benefits under provisions of the Northwest Power Act are not available in the 7(b)(2) Case. The 7(b)(2) Case rates will reflect this increased cost to the 7(b)(2) customers.

(5) Financing benefits under provisions of the Northwest Power Act are not available in the 7(b)(2) Case. The 7(b)(2) Case rates will reflect this increased resource

cost due to the absence of BPA financial backing if additional resources are required to serve 7(b)(2) customers.

See 16 U.S.C. §839e(b)(2) (emphasis added). For a discussion of the development of the Program and 7(b)(2) Case rates, *see* Section 7(b)(2) Rate Test Study, WP-02-FS-BPA-06, and Section 7(b)(2) Rate Test Study Documentation, WP-02-FS-BPA-06A.

The current rate case is unique in that BPA must establish appropriate rates to be used in the traditional REP, as well as rates to be used in the event of a settlement of the REP. Doubleday *et al*., WP-02-E-BPA-18, at 16. To accommodate this unique situation, BPA's ratemaking process includes two rate modeling steps, a Rate Design Step and a Subscription Step. *Id*. at 14-20. The Rate Design Step produces rates that are appropriate for a world that includes the traditional REP. *Id*. The Subscription Step produces rates that are appropriate for a world where the traditional REP does not exist, and has been replaced with a settlement agreement. *Id*.

BPA conducts the section 7(b)(2) rate test in the Rate Design Step of the rates models. As noted previously, this is appropriate for a number of reasons. First, section 7(b)(2) of the Northwest Power Act provides that the absence of the traditional REP is one of the five section 7(b)(2) assumptions. Therefore, the section 7(b)(2) rate test must be performed in the rate design step that includes the traditional REP, because, under law, rates must be compared between the Program Case, where the program exists, and the 7(b)(2) Case, where the program does not exist. The Rate Design Step is the only step that models the traditional REP. In addition, if the section 7(b)(2) rate test triggers, the PF Preference rate protection costs are allocated to other firm loads in the Rate Design Step, including the IP rate and PF Exchange Program rate. 16 U.S.C. §839e(b)(3). This results in a bifurcation of the PF rate into a PF Preference rate and a PF Exchange Program rate, which occurs only in the Rate Design Step. While BPA must calculate the 7(b)(2) rate test in the Rate Design Step, where the amount of the 7(b)(2) trigger is allocated to other power sales, BPA must also comply with the statutory requirement to recover its total costs. 16 U.S.C. §839e(a)(1). In the Subscription Step, BPA assumes that regional IOUs execute proposed settlements of the REP. BPA must therefore calculate Subscription Step rates that recover the costs of such settlements. Where such settlements would impose higher costs on BPA, BPA must allocate such costs to rates. Doubleday *et al*., WP-02-E-BPA-18, at 17-18; Doubleday *et al*., WP-02-E-BPA-44, at 13. It would be inappropriate, however, to conduct the 7(b)(2) rate test in the Subscription Step, because one of the five section 7(b)(2) assumptions, the traditional REP, does not exist in the Subscription Step.

WPAG argues that the proposed DSI Compromise demonstrates that BPA has the ability to require customers being offered a settlement to choose between two mutually exclusive options before the start of this proceeding. WPAG Ex. Brief, WP-02-R-WA-02, at 12. BPA disagrees with the WPAG argument that the DSI Compromise approach is analogous to the IOU REP settlement. While both the DSI Compromise and the REP settlements require that a choice be made between two mutually exclusive options, the timing of when the choices must be made is quite different. BPA's power sales to the DSIs for the coming rate period were unclear and had to be addressed in some manner before BPA could forecast DSI loads and conduct the power rate case. The DSI Compromise Approach is a way of determining how much BPA power DSIs will be qualified to purchase, and at what proposed price. BPA proposed that the total amount of

power would be allocated according to the relative amounts of IP-96 purchases of each eligible DSI. Berwager *et al.*, WP-02-E-BPA-09, at 7-8. In other words, those DSIs that purchased larger amounts of power from BPA during the current rate period would be entitled to a larger proportional share of the available power than DSIs that placed less load on BPA at the IP-96 rate during this period. *Id.* Further, only those DSIs that were willing to support the Compromise Approach proposal in the rate case and in other forums would be eligible to purchase power at the proposed Compromise Approach rate of 23.5 mills/kWh. *Id.* The slightly higher rate of 25.0 mills/kWh under the Targeted Augmentation Approach would be available to DSIs that were unwilling to commit to supporting the Compromise Approach as proposed in BPA's initial proposal. *Id.* Therefore, individual DSIs had to choose whether to support the Compromise Approach or not before the rate case proceeding.

In contrast to the Compromise Approach, the proposed IOU REP settlements require the IOUs to choose between the benefits offered under the traditional REP and the benefits offered under the settlement. BPA's Subscription Strategy proposes a settlement of the REP with regional IOUs in which residential and small farm loads of the IOUs will be assured access to the equivalent of 1,800 [1,900] aMW of Federal power for the FY 2002-2006 period (and 2,200 aMW for the FY 2007-2011 period). Leathley *et al.*, WP-02-E-BPA-19, at 16. Of this amount, at least 1,000 aMW will be met with actual power deliveries. *Id.* The remaining 800 [900] aMW will be provided in the form of either power or monetary benefits depending on which approach is most cost-effective for BPA. *Id.* This determination, as well as the amount of power and monetary benefits offered to each IOU, will be made in a separate process. *Id.* The monetary benefits will be based on the difference between the five-year flat-block market price of power forecasted in the rate case and the rate used to make Subscription sales to the IOUs (the RL-02 or the PF Exchange Subscription rate). *Id.* The benefits of the traditional REP are determined, in part, by the level of the PF Exchange Program rate. The PF Exchange Program rate is calculated in the rate case and will not be known until the final rate case documents are published. Clearly, the IOUs cannot make an informed decision between the traditional REP, to which they have a statutory right, and the settlement before the value of the benefits associated with the traditional REP has been forecasted at the conclusion of the rate case.

WPAG argues that the fact that BPA did not require the IOUs to make an election between the traditional REP and a settlement prior to the start of this proceeding does not in any manner free BPA of its duty to implement the provisions of the rate test. WPAG Ex. Brief, WP-02-R-WA-01, at 12. As noted above, it would have been inappropriate for BPA to require the IOUs to make an election between the traditional REP and a settlement prior to the start of this proceeding. In addition, however, BPA must address the circumstances that it could face in the coming rate period in order to ensure that it recovers its total costs. These include the continuation of the traditional REP, on one hand, and the proposed settlements of the REP, on the other hand. BPA cannot simply ignore circumstances that may affect BPA's total costs. Furthermore, BPA has implemented the provisions of the rate test properly and allocated the rate test trigger amount to the appropriate non-preference rates. As noted above, the section 7(b)(2) rate test must be performed in the Rate Design Step, which includes the traditional REP, because, under law, rates must be compared between the Program Case, where the program exists, and the 7(b)(2) Case, where the program does not exist. The Rate Design Step is the only step that models the traditional REP. In addition, if the section 7(b)(2) rate test triggers, the PF Preference

rate protection costs are allocated to other firm loads in the Rate Design Step, including the IP rate and PF Exchange Program rate. 16 U.S.C. §839e(b)(3).

WPAG argues that BPA should allocate to the rates formulated in the Rate Design Step (the PF Exchange Program and NR rates) and those formulated at the Subscription Step (the RL, PF Exchange Subscription, and the IP/IPTAC rates) the full portion of the rate test trigger amount. WPAG Ex. Brief, WP-02-R-WA-01, at 12. WPAG also argues that since each IOU must choose whether to participate in the REP or in the settlement proposal, and cannot do both, such an allocation would not result in an over-collection of BPA's costs. *Id.* at 13. WPAG argues that such an allocation scheme would result in BPA complying with the requirements of the rate test by allocating the rate test trigger amount to all other power purchased by all other customers, and proving that preference customers receive the full cost protection to which they are entitled under sections 7(b)(2) and (3) of the Northwest Power Act. *Id.* at 13. WPAG's new allocation proposal was not raised during the hearing, and BPA and the rate case parties have not had an opportunity to review this proposal. Based on WPAG's argument, however, this proposal is inappropriate and an insufficient substitute for BPA's proposal. As noted above, BPA conducts the section 7(b)(2) rate test in the Rate Design Step of the rates models. This is appropriate for a number of reasons. First, section 7(b)(2) of the Northwest Power Act provides that the absence of the traditional REP is one of the five section 7(b)(2) assumptions. Therefore, the section 7(b)(2) rate test must be performed in the Rate Design Step, which includes the traditional REP, because, under law, rates must be compared between the Program Case, where the program exists, and the 7(b)(2) Case, where the program does not exist. The Rate Design Step is the only step that models the traditional REP. In addition, if the section 7(b)(2) rate test triggers, the PF Preference rate protection costs are allocated only to other firm loads in the Rate Design Step, including the IP rate and PF Exchange Program rate. 16 U.S.C. §839e(b)(3). BPA's ratemaking process allocates costs to customer loads in sequential steps starting with the initial COSA allocations and continuing through the various statutory rate design adjustments, including the 7(c)(2) and 7(b)(2) rate design adjustments. In each step of the ratemaking process, specific cost amounts are allocated to specific customer loads, and a balancing credit amount is allocated to other customer loads. *See* Wholesale Power Rate Development Study Documentation, WP-02-FS-BPA-05A, Table RDS40. Each adjustment of costs between rate classes merely redistributes the original revenue requirement amount among the customer classes. A ratemaking adjustment cannot, as WPAG suggests, allocate twice the amount of costs to some loads as it credits to other loads. Allocating the entire rate test trigger amount twice to two different customer loads, one in the Rate Design Step and the other in the Subscription Step, does not comport with BPA's ratemaking methods. In addition, as stated above, the 7(b)(2) rate test is appropriate only for the Rate Design Step, and the allocation of the 7(b)(2) rate test trigger amount should be to only those loads used in the calculation of the 7(b)(2) rate test trigger.

WPAG argues that the fact that BPA has added a new and heretofore unheard of "Subscription Step" to its rate process does not relieve BPA of the statutory duty to allocate to all other power sold to all other customers, including customers purchasing power under the RL, PF Exchange Subscription, and IP/IPTAC rates, the costs that must be excluded from the PF rate under the terms of the rate test. WPAG Ex. Brief, WP-02-R-WA-01, at 13. BPA has not argued that adding the Subscription Step relieves BPA from its statutory duties. Instead, it is a means of implementing BPA's statutory duties. As BPA explained previously in section 12.2 regarding

BPA's implementation of the Rate Design Step and the Subscription Step, the fact that the Subscription Step is new does not mean that it is inappropriate or inconsistent with statute. WPAG argues that the statute does not exempt a rate from bearing its share of the rate test trigger amount based on when in the rate process it is formulated. *Id.* WPAG argues that the fact that the RL, PF Exchange Subscription, and IP/IPTAC rates were formulated in the Subscription Step, instead of the Rate Design Step, does not shield them from the statutory directive that they be allocated a portion of the rate test trigger amount. *Id.* at 13-14. As discussed at length above, the 7(b)(2) rate test is properly performed in the Rate Design Step of the RAM. Also as discussed above, the entire amount of the section 7(b)(2) rate test trigger rate protection amount is credited to the PF Preference rate, and those costs are allocated to other rates in the Rate Design Step of the RAM. Having afforded the PF Preference class rate protection in the Rate Design Step, it would be redundant to repeat that step again. Since the entire amount of the section 7(b)(2) rate test trigger PF Preference rate protection has been allocated to other rate classes before the calculation of the Subscription Step rates, it would be inappropriate to reallocate that very same PF Preference rate protection amount to those rates. This argument is discussed in additional detail below.

WPAG argues that by shielding the RL, PF Subscription, and IP/IPTAC rates from paying the rate test trigger amount, BPA has failed to fulfill its statutory duty, and has constructed a PF rate that includes costs that the rate test requires BPA to collect from all other power sold to all other customers. WPAG Ex. Brief, WP-02-R-WA-01, at 15. As discussed at length above, the 7(b)(2) rate test is properly performed in the Rate Design Step of the RAM. Also as discussed above, the entire amount of the section 7(b)(2) rate test trigger rate protection amount is credited to the PF Preference rate, and those costs are allocated to other rates in the Rate Design Step of the RAM. Having afforded the PF Preference class the section 7(b)(2) rate test trigger rate protection in the Rate Design Step, it would be redundant to repeat that step again. Since the entire amount of the section 7(b)(2) rate test trigger PF Preference rate protection has been allocated to other rate classes before the calculation of the Subscription Step rates, it would be inappropriate to reallocate that very same PF Preference rate protection amount to those rates. This issue has been addressed at great length in this section.

WPAG argues that while BPA may feel that implementation of its Subscription proposal presents special circumstances that warrant an abrogation of the statutory duty to allocate the rate test trigger amount to all other power sold to all other customers, neither the statute, nor the case law recognize such an exception. WPAG Ex. Brief, WP-02-R-WA-01, at 15. Contrary to WPAG's argument, BPA does not feel that special circumstances warrant an abrogation of the statutory duty to allocate the rate test trigger amount to all other power sold to all other customers. Instead, these special circumstances have been accommodated consistent with existing law, as explained in greater detail in this chapter. As explained previously at great length, BPA added a Subscription Step to its ratemaking process to accommodate the special circumstances it faces in the current rate case. However, BPA is abiding by sections 7(b)(2) and (3) of the Northwest Power Act. BPA conducts the section 7(b)(2) rate test in the Rate Design Step of the rates models. This is appropriate for a number of reasons. First, section 7(b)(2) of the Northwest Power Act provides that the absence of the traditional REP is one of the five section 7(b)(2) assumptions. Therefore, the section 7(b)(2) rate test must be performed in the Rate Design Step, which includes the traditional REP, because, under law, rates

must be compared between the Program Case, where the program exists, and the 7(b)(2) Case, where the program does not exist. The Rate Design Step is the only step that models the traditional REP. In addition, if the section 7(b)(2) rate test triggers, the PF Preference rate protection costs are allocated to other firm loads in the Rate Design Step, including the IP rate and PF Exchange Program rate. 16 U.S.C. §839e(b)(3). In addition to these reasons, assuming, *arguendo*, that BPA must allocate the trigger amount to the RL, PF Exchange Subscription, and IP/IPTAC rates despite the inappropriateness of doing so, as noted previously, section 7(b)(3) of the Northwest Power Act provides BPA with discretion in the allocation of the trigger amount to non-preference sales. 16 U.S.C. §839e(b)(3). Because such allocation does not have to be proportional, BPA's allocations to particular rates may range from very little, including nothing, to very great. In the development of current rates, for example, BPA can allocate $1,000 to the rates that WPAG has alleged have escaped the allocation of the trigger amount: the RL, PF Exchange Subscription, and the IP/IPTAC rates. Such an allocation, however, does not change BPA's rates to preference customers or any other customer class and complies with WPAG's argument that such rates must be allocated some of the trigger amount. BPA has previously noted that, given the extraordinary circumstances BPA faces in developing rates in this proceeding and the fact that the RL and PF Exchange Subscription rates are *settlement* rates for a single limited purpose--to provide power sales at a rate that provides appropriate consideration for the settlement of the REP--BPA's cost allocations are properly conducted in order to establish rates that provide the proper consideration for the REP settlements. WPAG argues that BPA's desire to strike a political bargain with the IOUs to provide them with power at the same rate paid by preference customers, based on the dubious proposition that doing so will gain BPA political allies, simply does not override its duty to abide by sections 7(b)(2) and (3) of the Northwest Power Act. *Id.* First, there is no evidence in the record that BPA has struck a political bargain with the IOUs based on the proposition that doing so will gain BPA political allies. As evidenced by the record, some IOUs have been extremely critical of the proposed settlements and settlement rates, among other things. BPA is not concerned with whether BPA's proposal will gain BPA political allies. Instead, BPA is concerned with ensuring that it is developing its rates in a manner that complies with the rate directives of sections 7(b)(2) and 7(b)(3).

Decision

BPA properly allocated the 7(b)(2) amount.