



March 11, 2005

Transmitted via Electronic and U.S. Mail

Paul E. Norman  
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RE: The Public Power Council's Comments To BPA On  
The Direct Service Industries (DSIs)

Dear Paul:

We are pleased to provide BPA with these comments on service to the DSIs during FY2007-2011. Although there is considerable diversity in views within public power regarding continued DSI service, we have identified a set of core principles that should be observed in providing benefits to the DSIs.

**Any Proposal BPA Makes Regarding The DSIs Must Fit Under The 27 Mill Rate Cap**

First and most importantly, any proposal that BPA makes with regards to the DSIs needs to fit under the 27 mill rate cap that we have said that BPA should observe in the next rate period. An initial weakness in PBL's Power Function Review (PFR) process was that the PFR simply consisted of presenting cost estimates for various areas of PBL without reference to how all these various cost estimates added up an overall cost, and how that overall cost translated to a post-2006 PBL rate. PBL has commendably made changes to the PFR process to allow better consideration of the overall impact of the various parts of the PFR. We feel that any proposal to provide benefits to the DSIs also cannot be viewed in isolation, but needs to be part of a larger rate strategy. (The 27 mill rate cap is more than 20% higher than the BPA rate that prevailed prior to the energy crisis.)

**The Cost Of Any Service To The DSIs Should Not Exceed \$40 Million/Year**

As part of ensuring that DSI benefits stay under the 27 mill rate cap, the cost of any service to the DSIs should not exceed \$40 million/year, which works

out to about a half-mill increase in BPA's rates. One of the worrisome things that became evident when BPA conducted its workshop on DSI service on March 1 is that the DSIs also have considerable differences of opinion regarding potential BPA service to the DSIs. If one added together the requests for benefits that DSI representatives made at that workshop, the total amount of MWs requested would be almost twice the amount proposed in BPA's 500 MW/\$40 million/year straw proposal.

A cap is important in order to limit BPA's (and BPA customers') liability in the event of another energy crisis. BPA should not think that it has agreed to a \$40 million level of benefit to the DSIs, only to discover that the agreement has morphed into a \$400 million or a billion dollar level of benefit.

### **BPA Should Not Obligate Itself To Ensuring That The DSIs Are Capable Of Operating Under Any Set Of Market Conditions**

The fact that the sum total of DSI requests for power were nearly double those laid out in the straw proposal is even more troublesome when coupled with statements by DSI representatives that a 10 mill subsidy would not be sufficient to get smelters operating – that the subsidy would have to be around 20 mills. Combining the DSIs request for near-doubling of the total amount of MW provided the DSIs plus a doubling of the subsidy provided per MW would lead to a cost of serving the DSIs on the order of \$150 million, not \$40 million.

BPA has noted that it is not obligated to serve the DSIs. BPA's determination that it is going to provide some level of benefit to the DSIs should not be interpreted as an obligation that BPA must to provide a level of subsidy sufficient to guarantee operation of the smelters under any circumstances. Power market prices are currently quite high (exacerbated by the persistence of the Northwest drought, of course), and alumina prices (a major input to the aluminum smelting process) are now also at a very high level. BPA should not feel compelled to offer a subsidy to ensure that smelters operate, given both the effects of the drought and the high international market price of alumina. The 10 mill level of benefit proposed in the straw proposal should provide a reasonable chance for the smelters to operate if and when power and alumina prices are closer to historical levels.

### **BPA Should Try To Maximize The Chances That DSI Benefits Track BPA's Rates To Its Other Customers, Subject To the \$40 Million Cap**

We consider the \$40 million cap to be a prerequisite for offering benefits to the DSIs. While that cap is a paramount consideration, it would also be desirable for the level of DSI benefits to fluctuate with the changes in the rate that BPA

charges other customers. This implies that under some circumstances, the level of DSI benefits should be under the cap – if the DSIs simply get \$40 million in benefits no matter what is happening to BPA’s costs and rates, then the DSIs would lose interest in controlling the level of BPA’s costs and rates. While keeping DSI benefits under the cap may not always be possible, trying to maximize the circumstances when this occurs is desirable. Thus we oppose the plan offered by some DSIs that if some of the companies are unable to utilize the benefit provided by BPA, that those benefits should then automatically flow to other DSI companies, effectively making the \$40 million a floor on DSI benefits, as well as a ceiling. Benefits to the DSIs should be determined on a company-by-company basis.

### **BPA Should Provide Benefits To The DSIs In A Manner That Does Not Place Undue Reliance On BPA’s Settlement Authority**

While we do not opine on what the precise mechanism that BPA should use to provide benefits to the DSIs, we would like to caution BPA not to use one that relies unduly on BPA’s settlement authority. We are currently involved in litigation against BPA offering benefits to the IOUs, based on BPA’s broad interpretation of its settlement authority, and we want to avoid becoming embroiled in this issue again over benefits to the DSIs.

### **There Are A Number Of Other Important Features That Should Be Included In Any Offer Of Benefits To the DSIs**

We have identified a number of other important features that should be included in an offer of benefits to the DSIs (several of them drawn from BPA’s straw proposal). For simplicity’s sake, they are listed in bullet form:

- BPA should minimize credit risk in providing benefits to the DSIs, since preference customers suffer the consequences of DSIs defaulting on their obligations to BPA.
- The DSIs should not have remarketing rights.
- Under no circumstances should the rate paid by DSIs be lower than the rate paid by preference customers.
- Any power supply arrangement with the DSIs should not reduce the amount of power available to allocate to the preference customers for the post-2011 period.

- The DSIs should receive benefits only if they actually operate their Northwest facilities.
- The IOUs should share in the cost of providing DSI service.
- The DSIs should not receive better contract terms (duration, etc.) than those presented to other customers.

Thank you for the opportunity to submit these comments.

Sincerely,

A handwritten signature in black ink, appearing to read "C. Clark Leone", is centered on a light gray, textured rectangular background.

C. Clark Leone  
Manager

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