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Mr. Steve Wright
Administrator
Bonneville Power Administration
905 NE 11th Street
Portland, OR 97232

RE: Initial Comments on the Integrated Program Review and Debt Service Options

Dear Mr. Wright:

I am writing on behalf of The Public Power Council (PPC), to offer these initial comments on the Integrated Program Review (IPR). Representing the broad cross section of preference customers of the Bonneville Power Administration (BPA), PPC and its members have an intense focus on agency budgets and how that translates into the rates set for wholesale power and transmission. We appreciate the work BPA staff has put into presenting this budget information and responding to customer requests for data. We look forward to your response and to further involvement upon receipt of the IPR close-out letter.

For more than two years the United States economy has been suffering through a severe recession that has profoundly affected the Northwest power industry. Public power utilities' loads and revenues have dropped very significantly as local businesses have closed and residential customers have lost their jobs. These conditions do not appear ready to change soon; the regional economy continues to be stagnant and unemployment continues to be high. Utilities have responded to the needs of their customers and communities by cutting budgets, laying off staff and putting off non-critical investments. The goal of these actions has been simple: to reduce power rate increases to the maximum extent possible in order to avoid further damage to their customers and local economies.

BPA, too, has felt the effects of the current recession. BPA's proposed budget, however, does not adequately reflect these economic realities. Power Services' proposed expense increases *alone* would represent an estimated power rate increase of between 12 and 20%. This initial proposal does not indicate that Power Services has taken sufficient steps to tighten its belt. Rather, it appears there was a tendency is to roll up program budgets that may be desirable or needed without full regard to the impact on consumers in this circumstance.

In regard to Power Services' budgets, the bulk of the agency response to current cost pressure appears to be the proposal to lengthen repayment of CGS debt to correspond to the current expiration of CGS' license, as well as possibly capitalizing certain items that are currently expensed. While we are generally supportive of such measures, and think they are appropriate and desirable, these measures do not address cost levels, but rather defer such costs into some point in the future. In order to further reduce the size of the looming rate increase, explicit steps should be taken to reduce costs, not rely on cost deferrals.

As a start, we would urge a more explicit identification of the *critical* needs (both capital and expense) in the upcoming rate period and establishment of budgets to do those things. While we understand that there has been an underinvestment in some power and transmission systems, an efficient approach to prioritization is crucial.

That being said, we note a number of improvements in the IPR process.

- An asset management approach is a good idea. It is a good tool to identify critical projects, justify their criticality, and to rank their importance. We have questions about the implementation of the asset management tool. Different programs appear to be implementing the concept differently and the results of the asset management plans are not coordinated so that commitments of capital can be prioritized.
- We also commend BPA for its creative approach to reducing the impact of federal COLA increases by assuming greater efficiency and lower costs as an offset to salary increases. This is a helpful assumption. We urge the other entities that depend on BPA for funding to do the same (*e.g.*, ENW, the Corps, the Bureau, and the Council).

In the next IPR we would like a list of the lower priority programs and costs that were *not* included in the proposed program capital and expense budgets, and a list of the programs for which BPA did not consider budget reductions (i.e., programs included in the base budgets that were not specifically called out for reductions in the workshops).

A. BPA Capital Program Generally

PPC was concerned and surprised to learn that, even with the recent substantial increase in BPA's borrowing authority, the agency expects to run out of borrowing authority between 2016 and 2018. Much of the capital program for maintenance and replacement investments in the hydro-power system are clearly critical and needed to ensure that BPA can meet its existing obligations to its customers into the future. The same is true for much, although not all, of the proposed transmission system investment. The discussions of the BPA capital programs and budgets in IPR have been helpful to our understanding of the budgeting processes and needs of the power and transmission systems. These discussions have not demonstrated, however, how BPA is making decisions regarding use of its available capital such that it will be able to make investments in the future that are needed to meet its existing obligations.

The customers need to gain a greater understanding of why and to what end BPA is expending its borrowing authority so rapidly. Overall, our impression is that BPA is not adequately prioritizing its capital projects and ranking them, or evaluating their need, so as to meet all of its obligations.

B. Transmission Services Costs

Capital Program

In regard to transmission system replacements, reinforcements and load-service investment, BPA Transmission Services is investing money in line with the needs of the system. Our overall goal in examining TS's capital budget is to see that BPA completes projects that meet load service and system reliability needs and that these projects are not being delayed in favor of other types of projects. To that end we encourage BPA to report to its customers throughout the rate period regarding the status of its transmission capital projects and analytical work being done to support proposed (currently unfunded) projects. To that end we request that BPA to provide the following periodically during the fiscal year:

- A list of the capital projects detailing the money that was budgeted, as per the FY Rate Case and SOY forecasts, and the annual amount actually spent per project;
- Information regarding outages and causes that would permit customers to validate BPA's asset management plan to determine whether sufficient and correct investments are being made; and
- Information regarding the costs, need for, and purposes of projects proposed for capital funding in the current or succeeding rate periods.

PPC requests that presentation and discussion of this information be combined with, or added to, BPA's quarterly financial reviews.

On other matters, BPA has established an availability target for Category 1 & 2 lines (98%) but not for Category 3 & 4 lines. BPA does not expect to establish an availability target for Category 3 & 4 lines until the end of 2010. Performance of Category 3 & 4 lines should be held to a high standard. The primary purpose of the FCRTS is load service in the NW and the Category 3 & 4 lines are an essential element in meeting that purpose. We think that Transmission Services should commit to meet with customers to discuss the establishment of a performance target and the potential capital program impacts.

In regard to wood pole lines, BPA is still gathering and analyzing data on the health of active components and poles. We would appreciate being kept up-to-date on this information so that the program costs are not increased in the Final Studies for the rate case without an opportunity to discuss the issues.

Expense Budgets - Transmission

We urge BPA Transmission to re-evaluate, and discuss with its customers, the level of staffing and succession planning that BPA needs in key areas of Transmission Services. These areas include Operations, Scheduling, Policy and Rates, and Reliability Compliance. These are key areas that Bonneville employees, not contractors, should staff in order to preserve expertise and ensure continuity of policy implementation.

With regard to NERC standard compliance in particular, BPA needs to ensure that it assigns sufficient staff with the needed expertise to ensure not only that BPA is compliant, but also that standards involving BPA customers and their equipment that interfaces with the BPA system are compliant. BPA must provide timely compliance documentation to its customers. We appreciate the efforts undertaken by BPA staff to become more attuned to its customers needs in this area, but we remain concerned about the challenges ahead.

C. Power Services Costs

PPC has preliminary comments regarding various components of the Power Services expense and capital budgets. Those are detailed below.

Columbia Generating Station

The costs associated with the Columbia Generating Station's debt and operations are a significant share of the BPA Power Services budget. As such, the way in which those costs are handled is important. BPA and the customers should carefully analyze the structure of Energy Northwest debt for WNP-1, -3 and the Columbia Generating Station. BPA forecasts currently that all but a small amount of the debt for existing investments will be paid off by 2019. Amortization of Federal debt is forecast to decline considerably between 2015 and 2017. Amortization of non-Federal debt (most Energy Northwest debt) grows to $722 million in 2017 and then drops to $68 million in 2019.

The authors of this debt structure were concerned that these debts not be imposed on future ratepayers. However, CGS is currently licensed to 2024. We believe that BPA and Energy Northwest should stretch out the CGS debt structure so that the CGS debt is completely paid back when the CGS' license expires, which would reduce BPA's costs in the next rate period by about $100 million. WNP-1 and -3 debt should be repaid according to the existing debt repayment schedule (by FY 2018), or in a slightly accelerated fashion. In making this recommendation regarding debt restructuring, the PPC Executive Committee wanted to make clear that this assent only pertains to the current situation, and that customers continue to expect in-depth involvement regarding any future proposals regarding federal and non-federal debt.

In addition, we believe that BPA should amortize the purchase of fuel for CGS over the life of the fuel burn. Ninety-seven percent of the $55 million annual increase in CGS costs from the FY 2010-11 period to the FY 2012-13 period is caused by fuel cost increases and fuel revenue declines. Relatively low-cost fuel purchases under the DOE pilot program are ending and will be replaced by market purchases. Nuclear fuel is unique in the amount of time that passes between the initial mining of uranium and the actual burning of the fuel in the reactor, and many utilities around the nation amortize nuclear fuel purchases over the fuel burn, rather than expense them. Amortizing fuel costs over the fuel burn would decrease the initial rate impact of the $47 million increase in fuel cost by about two thirds.

FCRPS Maintenance

Another, and even larger source of power costs, is the operation and maintenance of the Federal Columbia River Power System (FCRPS). Like the CGS costs, FCRPS costs can be managed in part by capitalizing some costs. BPA should investigate capitalizing non-routine extraordinary maintenance on the FCRPS. About 15% of Corps and Bureau O&M program costs are for non-routine extraordinary maintenance (NREX), the large infrequent activities associated with returning failed units to service, repairing gates and other large equipment and structures, as well as the work required for overhauling the big 805 & 600 MW units in the Grand Coulee Third Powerhouse. These costs are being treated as an expense even though this represents maintenance and repairs on long-lived assets and will be at a very high level for years as the Grand Coulee Third Powerhouse is refurbished from FY 2011 to FY 2016. BPA's costs in the next rate period could be reduced by about $5 million a year by capitalizing non-routine extraordinary maintenance.

Energy Efficiency

Another area in which capitalization of costs may be considered is conservation. BPA's proposal to capitalize conservation acquisition costs rather than expensing those costs deserves additional consideration. Capitalizing the acquisition costs may make sense because some conservation is a long-term resource that will serve load over a period of years. Additionally, given the large increase in both the level of conservation that needs to be acquired and its increasing cost, fully expensing conservation acquisition costs could alone create a rate increase of 5%, all else equal; capitalizing those costs appears to result in a slight rate decrease in the short term. We also support BPA looking at amortizing conservation over the expected life of the conservation measures, which may be more than the 5 years BPA is currently using.

The agency should continue to assume that *at least* 25% of the conservation acquisition dollars will be self-funded by customers. Customers have demonstrated their commitment to self-funding conservation over the past years. Given the new price signals under tiered rates, state initiatives, and other drivers, we can expect that level of self-funding to continue if not increase.

Renewable Resources

BPA proposes in the Renewable Resources budget to expend $4 million per year on "Resource Development." The customers need more information on what the $4 million per year for "Resource Development" will be used for. This is a new line item in the renewables program budget, so a clearer understanding of what these funds would be used for and how they will benefit Tier 1 customers is needed.

With regard to the costs incurred to staff and fund the efforts of the Wind Integration Team, BPA has not yet adequately disclosed these such that customers can accurately gauge the costs of the program. For example, with regard to staffing, the methodology described as the manner in which FTE and contractors were counted indicates that the staff count for WIT could be substantially underreported. PPC requests that BPA provide updated information. Also in regard to WIT costs, BPA purports to "offset" the costs of the program by the application of "Green Energy Premium" (GEP) revenues. This is both inappropriate and unsupported by logic; GEP revenues are to be spent on projects that will benefit Tier 1 customers because those are the customers who paid the GEP. This "offset" should be removed from the WIT budget in order to provide a more accurate picture of the overall costs.

Fish & Wildlife

BPA and the action agencies recently failed to apply and defend in court the federal agencies' own science (on operational questions of spill or maximum transport), which underpins the current BiOp. If the federal agencies' lack of application of the BiOp results in additional customer costs, then a commensurate level of offsetting reductions should be found in other areas to keep customers whole. Having strongly supported the BiOp and its science, and recognizing the enormous costs of that effort, customers will continue to pursue this issue of consistency in all available forums.

A key addition to this area of the budget would be for BPA to set an overall cap on the Direct Fish and Wildlife Program expenditures for the duration of the BiOp. This will make it necessary for BPA and the Council to transfer some of the expenditures in Research, Monitoring and Evaluation (RM&E) in order to fund new on-the-ground project proposals. Also, it would set clear program expectations and send a strong signal to program managers that they must control RM&E costs. The program would be more efficient and effective in spending ratepayer funds in ways that result in real improvements in fish and wildlife productivity and survival. To help implement the cap, any non-Accord projects that fail science review should not be funded.

We realize that contracts for the MOA projects have the troubling aspect of an automatic 2.5% increase in payments per year. We would like BPA's budgets for these projects to recognize that the actual expenditures lag behind the budgeted amounts and it is reasonable to reflect this lag in rates.

When projects within the direct program cannot ramp-up as quickly as expected, or for other reasons BPA's cost projections for the direct program are inaccurate and cause BPA to over-collect in rates for fish and wildlife expenses, the unspent funds should be earmarked for future fish and wildlife projects and offset rates in subsequent rate periods.

BPA should develop a plan regarding MOA funding determinations in the case that the BiOp is struck down or materially changed by the judge. Ratepayers did not oppose these increases in fish and wildlife program funding because there was expectation that this funding increase would provide some stability among river interests for the long-term and that this would allow the region to move ahead with the BiOp. If the BiOp is struck down or substantively changed, the accord parties need to address whether a "material" change has taken place. As public power customers fund the MOAs, BPA should consider whether a "material" change has altered the nature of the accords and negated any benefits received by its customers and take action to protect the customers' interests.

BPA should encourage the Council to use the Independent Economic Analysis Board (IEAB) to a greater degree. The Council recently debated the value of the IEAB and came to the realization that the IEAB was underutilized. The IEAB can provide useful insight as to the relative cost-effectiveness of the program and the value of the FCRPS at large. The IEAB may be of particular value with respect to prioritization of RM&E projects. BPA should specifically request that the Council task the IEAB with a "big picture" cost/benefit review of projects in the program.

<u>Northwest Power and Conservation Council</u>

The Northwest Power and Conservation Council (Council) budget was reviewed as part of the fish and wildlife budget during the IPR workshops. The Council's $9.4 million budget in 2009 is projected to increase approximately half a million dollars from by 2011 and a full $1 million between 2009 and 2012. The Council should work with BPA, the customers and possibly the IEAB to identify cost-savings, such as increasing web-based communication, reviewing office space options, or freezing hiring during this economic crisis.

D. Agency Services (Allocated to Power and Transmission)

BPA's proposed Agency Services costs for FY 2012-13 are a significant increase over the current rate period (up $44 million, or 17%, from the 2011 Rate Case to the FY 2012-13 average). Over the slightly longer-term, Agency Services costs are escalating from $205 million in FY09 to $304 million in FY13 – an escalation of 48% in only four years. Discussions with BPA staff have clarified that this escalation from 2009 to 2013 is *not* the result of functions being shifted from other business lines to BPA corporate. Rather, the increases reflect real escalation in BPA costs. The IPR presentations did not indicate that there has been adequate higher-level scrutiny of what is the acceptable escalation in Agency Services costs. Rather, it appears so far that the Agency Services budgetary process has provided a large amount of approval of the proposed budgets of each of the constituent parts of Agency Services, adding up to a large increase overall as noted above.

Given the economy and the financial losses that the agency has incurred over the last couple of years, it is incumbent on management (possessing the knowledge on where to pursue reduction) to put an overall limit on the allowable escalation in Agency Services costs, and then enforce that limit.

Additionally, we would identify other specific cuts in BPA's proposed budget that should be made. For example, a portion of the increase in Agency Services' costs is related to a BPA proposal to purchase insurance for the FCRPS and some transmission facilities at a cost of approximately $15 million per year. This is a policy level decision as to whether BPA should purchase this insurance. The general rule is that the federal government self-insures, and this is not the time to change "insurance companies." Second, BPA has identified and applied lapse factors for capital investments for transmission, FCRPS, and other investments. BPA should identify and apply a lapse factor for IT investments as well.

Conclusion

Given the continuing moribund state of the Northwest economy, now is not the time for BPA's costs to be rising from 12 to 20% (to say nothing of the other factors, like reserve funding, in the upcoming rate case that could increase BPA's rates more than that). It is incumbent on the agency to carefully reexamine its cost structure, to continue to see where cost savings can be achieved. As with the tough decisions being made in the utilities that the agency serves, BPA budgets cannot be created independent of the circumstances surrounding them. The overall rate increase that BPA is contemplating, along with the state of the regional economy need to be key drivers in BPA's budget decision-making.

Thank you very for the opportunity to submit these initial comments. We would be happy to discuss any of these comments with you, and we look forward to working with you as this important budgeting process continues.

Sincerely,

Scott Corwin

Scott Corwin