PUBLIC POWER COUNCIL
Bringing public power together

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August 2, 2018

Elliot Mainzer
Administrator, Bonneville Power Administration
Portland, OR 97232
Submitted via email

Re: BPA Integrated Program Review (IPR) and Financial Plan Implementation

Dear Elliot:

PPC appreciates this opportunity to comment on BPA's proposed spending levels in the Integrated Program Review (IPR) processes as well as on certain aspects of implementation for BPA's access to capital strategy and financial reserves policy. As described in our letter of July 2, these efforts are critical for consumers and businesses in the region impacted by power and transmission rates, and for the ability of BPA to offer competitive power products well ahead of when contracts expire in 2028.

PPC also recognizes the hard work by BPA staff in putting together these proposals. PPC is particularly appreciative of staff's efforts to be responsive for requests for more information and to work collaboratively with public power. The financial health of BPA, public power, and the Northwest region are closely tied together. As such, the best solutions to our challenges will also be found through our collective effort.

Integrated Program Review

Overall this IPR has shown good process improvements. PPC particularly supports the move towards a greater emphasis on strategic top-down controls on spending levels that are established at the beginning of the process. Further we appreciate keeping budgets flat relative to BP-18 levels as a starting point. However, given the upward pressure on costs from sources outside of the IPR, we urge BPA to take further steps to control its costs. As discussed below, given that BPA has historically spent significantly less on its programs than currently proposed budgets, this can be accomplished while still fulfilling BPA's mission and providing excellent value to customers.

Increasing cost and rate trajectories are the primary challenge facing Power Services in providing value to preference customers. PPC supports BPA's goals of managing both IPR costs and power rates at *or below* inflation levels. BPA's initial rate preview shows significant upward pressure in costs outside of the IPR. Even with an additional $30 million in savings relative to the initial IPR proposal, the initial preview was for 5% of upward rate pressure in the upcoming rate period.

BPA should work to find at least an additional $20 million in savings (totaling $50 million from the initial IPR) to bring the initial proposal power rate proposal down. This will be challenging, but we believe it is achievable based on the gap between actual historical spending levels and BP-20 budget amounts. BP-16 actuals for Power Services IPR spending are approximately $88 million per year below BP-20 budget levels. Even with $50 million in reduced budget levels from the initial IPR proposal, this leaves $38 million in headroom from BP-16 actual spending for BPA and its generating partners to manage inflationary pressures.

PPC supports BPA's overall approach in prioritizing the highest value capital investments for federal hydro. As power prices continue to reach new lows, another conversation about the ideal level of future capital spending is appropriate. PPC supports BPA's goals for the hydro capital program in this upcoming rate period, but as a practical matter we are concerned that the program execution has been dramatically below budgeted levels in recent years. PPC would like to work with BPA staff to identify appropriate mechanisms or assumptions to ensure that a realistic level of capital spending on federal hydro is included in BP-20 rates.

Transmission services currently faces different challenges in providing value to its customers. Although efficiency and fiscal discipline are still essential, BPA must continue its efforts to be more responsive to meeting customer needs. BPA is also facing legitimate challenges with aging infrastructure. PPC recognizes that meeting these challenges in operations, maintenance and engineering requires adequate resources. At the same time PPC believes that more can be done to capture efficiencies in the transmission organization.

We recommend BPA seek $10 million in overall reductions for transmission costs from the initial IPR proposal. The BP-20 IPR budgets represent a $39 million increase, or 8.5%, over BP-16 actual spending. In the current fiscal year BPA transmission is projected to finish below the rate case budgeted amounts in operations, maintenance, engineering, and Agency Service G&A by a combined total of $22.6 million. We believe BPA is in the best position to identify specific areas to carry forward underspending of current budgets while achieving the desired strategic outcomes. However, we welcome the opportunity to work collaboratively to help identify potential trade-offs and risks.

PPC recognizes the need for significant capital investment in the transmission system both to sustain current capabilities and to be responsive to customer needs. We are not proposing specific adjustments to the proposed levels of capital spending in transmission but in general more clarity on prioritization, and more clear business cases with top down targets is needed.

Additionally, we recognize that the Transmission capital program is evolving away from a few large projects to many small projects. This will create new challenges in terms of prioritization and efficiency. PPC is committed to working closely with BPA to ensure that customer needs are being met while keeping an eye towards efficient use of financial capital.

Financial Reserves Policy Implementation

Variability in BPA's net secondary revenues relative to forecasts is the largest source of uncertainty in power rates. BPA's initial rate preview indicated an $89 million reduction in the forecast for net secondary revenues in the BP-20 rate period. While this level of reduction represents a very large upward pressure on rates, it also creates a significant decrease in the risk that BPA is required to mitigate in power rates through financial reserves and other mechanisms. Given the confluence of these factors, PPC strongly opposes raising the surcharge level to accrue additional financial reserves in the BP-20 rate period. The current $20 million surcharge in combination with a large reduction to the assumed level of net secondary is already burdensome to customers and represents a significant decrease in financial risk to the agency without additional action.

Access to Capital Issues

BPA staff's original "preferred scenario" for access to capital called for approximately $1.6 billion in Energy Northwest refinancing to bridge the gap in access to capital over the following 10 years (in addition to ongoing use of borrowing authority, continuation of the lease-purchase program, and revenue financing as dictated by the Leverage Policy). Subject to certain caveats, PPC was supportive of this portfolio.

BPA's new "preferred scenario" proposes relying on Energy Northwest's tax-exempt financing to the maximum extent possible, approximately $3.5 billion. Most of that additional financing would be used to eliminate BPA's lease-purchase program. Using Energy Northwest refinancing instead of lease-purchase financing can result in interest savings and lower administrative expenses.

At this time PPC does not have a specific recommendation regarding the use of $1.6 billion versus $3.5 billion. Lower costs of financing are of course desirable; but, PPC staff simply has not yet had adequate opportunity to analyze the full implications of the new "preferred scenario." PPC plans to work closely with preference customers, Energy Northwest, and BPA staff over the coming month to come to a recommendation. In the meantime, BPA should maintain the option of using the original "preferred scenario" if the increased use of higher levels of Energy Northwest refinancing is not viable.

Regardless of the level of Energy Northwest refinancing, PPC's previously submitted four criteria should be applied:

- It is important that BPA continue to demonstrate a real commitment in the IPR process to scrubbing and controlling its capital numbers, which could reduce the overall need for Energy Northwest refinancing.
- BPA's authorized Treasury Borrowing Authority is generally the preferred source of capital. BPA should not plan to maintain Treasury borrowing authority above the $1.5 billion planning minimum by over-relying on third party sources of capital financing.
- BPA should seek Energy Northwest approval for up to a specific amount, and should commit to go back to the Energy Northwest governing bodies for approval of any

increase in the amount of refinancing. We would be concerned about an open-ended commitment of funding capacity from Energy Northwest refinancing.

- If Energy Northwest agrees to provide financing capacity, BPA should agree that it would not propose revenue financing of capital investments for Power Services during the ten-year time horizon supported by the refinancing unless there is broad agreement from power customers. Power customers have already taken significant rate actions to place the business line on a deleveraging trajectory.

Conclusion

PPC appreciates your consideration of these comments. Please do not hesitate to contact PPC staff with any questions or concerns. We look forward to working closely together to find the best solutions for BPA to continue providing value to public power and the whole Northwest region.

Sincerely,

Scott Corwin

Scott Corwin
Executive Director