

1.0 INTRODUCTION

This Record of Decision (ROD) contains the decisions of the Bonneville Power Administration (BPA), based on the record compiled in this rate proceeding, with respect to the adoption of power rates for the five-year rate period commencing October 1, 2001, through September 30, 2006. This “2002 Wholesale Power Rate Adjustment Proceeding” is the pricing implementation of BPA’s Power Subscription Strategy adopted December 21, 1998. The Subscription Strategy, as well as other agency processes, provide the policy context for this rate case. This context is described in ROD chapter 2.

This ROD follows a full evidentiary hearing, briefing, and oral argument before the BPA Administrator. Parties had the opportunity to file briefs on exception to the Draft ROD before the Administrator issued the final rate proposal. ROD chapters 3 through 19 present the issues raised by parties to this proceeding, the parties’ positions, BPA’s position on the issues, BPA’s evaluation of the positions, and BPA’s decisions.

1.1 Procedural History of this Rate Proceeding

1.1.1 Issue Workshops

Six months prior to the release of its initial power rate proposal, BPA sponsored workshops on a variety of issues related to its ratemaking. The workshops covered topics ranging from proposed rate designs, revenue requirements, risk management, and inter-business line issues. These workshops were held between BPA and interested parties to develop a common understanding of the issues and to generate ideas and propose alternative solutions to issues in specific areas when possible. Conducting these issue workshops prior to development of the initial power rate proposal enabled BPA to freely exchange ideas and comments relevant to power rates issues with its customers without the restriction of the prohibition on *ex parte* communication which goes into effect prior to the formal rate proceeding. The *ex parte* prohibition went into effect on June 23, 1999, as BPA began development of its initial power rate proposal. The proposal incorporated many of the ideas and solutions arising from these workshops, and this ROD reflects them where appropriate.

1.1.2 Rate Proceeding

Section 7(i) of the Pacific Northwest Electric Power Planning and Conservation Act, 16 U.S.C. §839e(i) (Northwest Power Act), required that BPA’s wholesale power rates be established according to certain procedures. These procedures include, among other things, issuance of a Federal Register Notice announcing the proposed rates; one or more hearings; the opportunity to submit written views, supporting information, questions, and arguments, and a decision by the Administrator based on the record. This proceeding is governed by BPA’s rules for general rate proceedings contained in the *Procedures Governing Bonneville Power Administration Rate Hearings*, 51 Fed. Reg. 7611 (1986) (hereinafter Procedures). The Procedures implement the section 7(i) requirements.

On August 13, 1999, BPA published its notice of *2002 Proposed Wholesale Power Rate Adjustment, Public Hearing, and Opportunities for Public Review and Comment*, 64 Fed. Reg. 44318 (1999). BPA's 2002 wholesale power rate proceeding began with a prehearing conference on August 24, 1999. At the prehearing conference, the Hearing Officer issued orders concerning procedural matters in this proceeding. On August 30, 1999, the Hearing Officer issued an Order establishing the schedule for this rate proceeding. On September 1, 1999, the Hearing Officer issued an Order concerning data request procedures adopting the electronic discovery procedures proffered by BPA and the parties. On September 2, 1999, the Hearing Officer issued an Order granting in part, and denying in part, petitions to intervene and adopted a service list for BPA's 2002 Wholesale Power Rate Adjustment Proceeding.

BPA's 2002 initial power rate proposal, filed on August 24, 1999, was supported by prefiled written testimony and studies sponsored by approximately 68 witnesses. Oral clarification on BPA's initial power rate proposal occurred from September 13-19, 1999. Direct testimony was filed by the parties on November 2, 1999. Clarification on the parties' direct testimony occurred from November 15-19, 1999. On December 17, 1999, litigants to the proceeding filed testimony in rebuttal to the parties' direct cases. The parties filed their prehearing briefs one week later. Clarification on the litigants' rebuttal testimony occurred from January 4-5, 2000. Written discovery of BPA's and the parties' direct and rebuttal cases occurred throughout the hearing. BPA responded to 1,196 data requests concerning its initial rate proposal and its rebuttal testimony.

Cross-examination took place from January 24, 2000, through February 4, 2000. The parties submitted initial briefs on February 28, 2000. Oral argument before the Administrator was held on March 2, 2000. The Draft ROD was issued and distributed to parties on April 10, 2000. On April 24, 2000, the parties submitted briefs on exceptions in response to the Draft ROD.

This ROD is based on the Administrator's consideration of the entire rate case record, including oral and written comments discussed in ROD section 18.4, *infra*. This ROD was made available on May 15, 2000.

For interested persons who do not wish to become parties to the formal evidentiary hearings, BPA's Procedures provide opportunities to participate in the ratemaking process by submitting oral and written comment. *See* §1010.5 of BPA's Procedures. BPA took oral and written comments at transcribed filed hearings conducted throughout the region between September 30 and October 14, 1999, in eight locations: Idaho Falls, Idaho; Missoula, Montana; Pasco, Spokane, Everett, and Olympia, Washington; and Eugene, and Portland, Oregon. As the result of a public request, BPA held an additional field hearing on November 9, 1999, in Seattle, Washington. BPA received and considered 7,087 written comments submitted during the participant comment period, which officially ended on November 30, 1999. BPA also received written comments after the end of the official comment period and included in the official rate case record those comments received before BPA issued the Draft ROD. The transcribed field hearings and the comments from these rate case participants are part of the record upon which the Administrator bases her decisions.

1.1.3 Waiver of Issues By Failure to Raise in Briefs

While the parties have raised many issues in this proceeding in their briefs, there are a number of issues raised by the parties during the hearing that were not raised in the parties' briefs. Pursuant to §1010.13(b) of the *Procedures Governing BPA Rate Hearings*, arguments not raised in parties' briefs are deemed to be waived. Such issues will be implemented based on BPA's stated position in the record.

1.2 Legal Guidelines Governing Establishment of Rates

1.2.1 Statutory Guidelines

Section 6 of the Bonneville Project Act of 1937 (Project Act), 16 U.S.C. §832e, requires that the Administrator prepare schedules of rates and charges for electric energy sold to purchasers. Under the Project Act, rate schedules become effective upon confirmation and approval by the Federal Power Commission, succeeded by the Federal Energy Regulatory Commission (FERC or Commission). Section 6 of the Project Act directs the Administrator to establish rates with a view to encouraging the widest possible diversified use of electric energy. Section 7 provides that rate schedules are to be established having regard to the recovery of the cost of producing and transmitting electric energy, including amortization of the capital investment over a reasonable period of years. 16 U.S.C. §832f.

The Flood Control Act of 1944 contains ratemaking requirements similar to the Project Act. Section 5 of the Flood Control Act directs that rate schedules should encourage the most widespread use of power at the lowest possible rates to consumers consistent with sound business principles. 16 U.S.C. §825s. Section 5 also provides that rate schedules should be drawn having regard to the recovery of the cost of producing and transmitting electric energy, including the amortization of the Federal investment over a reasonable number of years. *Id.*

The Federal Columbia River Transmission System Act of 1974, 16 U.S.C. §838 (Transmission System Act), contains requirements similar to those of the Project Act and the Flood Control Act. Section 9 of the Transmission System Act, 16 U.S.C. §838g, provides that rates shall be established: (1) with a view to encouraging the widest possible diversified use of electric power at the lowest possible rates consistent with sound business principles; (2) with regard to the recovery of the cost of producing and transmitting electric power, including amortization of the capital investment allocated to power over a reasonable period of years; and (3) at levels that produce such additional revenues as may be required to pay when due the principal, premiums, discounts, expenses, and interest in connection with bonds issued under the Transmission System Act. Section 10 of the Transmission System Act, 16 U.S.C. §838h, allows for uniform rates and specifies that the costs of the Federal transmission system be equitably allocated between Federal and non-Federal power utilizing the system.

In addition to the Bonneville Project Act, the Flood Control Act, and the Transmission System Act, the Northwest Power Act provides numerous rate directives. Section 7(a)(1) of the Northwest Power Act directs the Administrator to establish, and periodically review and revise, rates for the sale and disposition of electric energy and capacity and for the transmission of

non-Federal power. 16 U.S.C. §839e(a)(1). Rates are to be set to recover, in accordance with sound business principles, the costs associated with the acquisition, conservation, and transmission of electric power, including the amortization of the Federal investment in the Federal Columbia River Power System (FCRPS) (including irrigation costs required to be repaid by power revenues) over a reasonable period of years. *Id.* Section 7 also contains rate directives describing how rates for individual customer groups are derived.

1.2.2 Additional Statutory Guidelines for Inter-Business Line Charges

BPA must satisfy section 212(i) of the Federal Power Act, 16 U.S.C. §824k(i), which states that transmission rates will be governed only by otherwise applicable law, except that no BPA transmission rate applicable to transmission service ordered by the Commission shall be unjust, unreasonable, or unduly discriminatory or preferential as determined by the Commission.

1.2.3 The Broad Ratemaking Discretion Vested in the Administrator

The Administrator has broad discretion to interpret and implement statutory standards applicable to ratemaking. These standards focus on cost recovery and do not restrict the Administrator to any particular rate design methodology or theory. *See Pacific Power & Light v. Duncan*, 499 F. Supp. 672 (D.C. Or. 1980); *accord City of Santa Clara v. Andrus*, 572 F. 2d 660, 668 (9th Cir. 1978) (“widest possible use” standard is so broad as to permit “the exercise of the widest administrative discretion”); *ElectriCities of North Carolina v. Southeastern Power Admin.*, 774 F. 2d 1262, 1266 (4th Cir. 1985).

The United States Courts of Appeals of the Ninth Circuit has also recognized the Administrator’s ratemaking discretion. *Central Lincoln Peoples’ Utility District v. Johnson*, 735 F. 2d 1101, 1120-29 (9th Cir. 1984) (“[b]ecause BPA helped draft and must administer the Northwest Power Act, we give substantial deference to BPA’s statutory interpretation”); *PacifiCorp v. F.E.R.C.*, 795 F. 2d 816, 821 (9th Cir. 1986) (“BPA’s interpretation is entitled to great deference and must be upheld unless it is unreasonable”); *Atlantic Richfield Co. v. Bonneville Power Admin.*, 818 F. 2d 701, 705 (9th Cir. 1987) (BPA’s rate determination upheld as a “reasonable decision in light of economic realities”); *Aluminum Company of America v. Central Lincoln Peoples’ Utility District*, 467 U.S. 380, 389 (1984) (“The Administrator’s interpretation of the [Northwest Power] Act is to be given great weight”); *Department of Water and Power of the City of Los Angeles v. Bonneville Power Admin.*, 759 F. 2d 684, 690 (9th Cir. 1985) (“Insofar as agency action is the result of its interpretation of its organic statutes, the agency’s interpretation is to be given great weight”).

1.3 Federal Energy Regulatory Commission (FERC) Confirmation and Approval of Rates

BPA’s rates become effective upon confirmation and approval by FERC. 16 U.S.C. §839e(a)(2) and (k). FERC’s review is appellate in nature, based on the record developed by the Administrator. *United States Department of Energy--Bonneville Power Admin.*, 13 F.E.R.C. ¶ 61,157, 61,339 (1980). The Commission may not modify rates proposed by the Administrator, but may only confirm, reject, or remand them. *United States Department of*

Energy--Bonneville Power Admin., 23 F.E.R.C. ¶ 61,378, 61,801 (1983). Pursuant to section 7(i)(6) of the Northwest Power Act, 16 U.S.C. §839e(i)(6), FERC has promulgated rules establishing procedures for the approval of BPA rates. 18 C.F.R. Part 300 (1997).

1.3.1 Firm Power Rates

With respect to rates, FERC determines whether: (1) rates are sufficient to assure repayment of the Federal investment in the FCRPS over a reasonable number of years after first meeting BPA's other costs; (2) rates are based on BPA's total system costs; and (3) transmission rates equitably allocate the cost of the Federal transmission system between Federal and non-Federal power using the system. 16 U.S.C. §839e(a)(2). See *United States Department of Energy--Bonneville Power Admin.*, 39 F.E.R.C. ¶ 61,078, 61,206 (1987). The limited FERC review of rates permits the Administrator substantial discretion in the design of rates and the allocation of power costs, neither of which is subject to FERC jurisdiction. *Central Lincoln Peoples' Utility District v. Johnson*, 735 F. 2d 1101, 1115 (9th Cir. 1984).

1.3.2 Nonfirm Energy (NF) Rates

Although both regional and extraregional rates are established by the Administrator under common statutory standards, FERC review of extraregional rates for sales of nonfirm energy is undertaken pursuant to section 7(k) of the Northwest Power Act. 16 U.S.C. §839e(k). FERC reviews extraregional nonfirm energy rates to ascertain that BPA has designed the rates: (1) having regard to the recovery of the cost of generation and transmission of such electric energy; (2) so as to encourage the most widespread use of BPA power; (3) to provide the lowest possible rates to consumers consistent with sound business principles; and (4) in a manner that protects the interest of the United States in amortizing its investments in the projects within a reasonable number of years. *United States Department of Energy--Bonneville Power Admin.*, 36 F.E.R.C. ¶ 61,335, 61,798 (1986); *United States Department of Energy--Bonneville Power Admin.*, 54 F.E.R.C. ¶ 61,235, 61,294 (1991).

FERC review of BPA's extraregional nonfirm energy rates is based upon the evidentiary record developed by BPA pursuant to section 7(i) of the Northwest Power Act, 16 U.S.C. §839e(i). *Aluminum Company of America v. Bonneville Power Admin.*, 903 F. 2d 585, 592 (9th Cir. 1990). This review is consistent with FERC authority to confirm, reject, or remand BPA's rates. *United States Department of Energy--Bonneville Power Admin.*, 23 F.E.R.C. ¶ 61,378, 61,801 (1983); *Central Lincoln Peoples' Utility District v. Johnson*, 735 F. 2d 1101, 1113 n.6 (9th Cir. 1984).

The Northwest Power Act provides no specific guidance to BPA as to how to apply the section 7(k) statutory standards while designing nonfirm energy rates. *Aluminum Company of America v. Bonneville Power Admin.*, 903 F. 2d 585, 598 (9th Cir. 1990). In *Aluminum Company*, the court noted that BPA had three conflicting obligations in conforming its rates to the section 7(k) statutory standards. BPA must ensure that nonfirm energy is sold at the lowest possible rates consistent with sound business principles, but must also ensure cost recovery and Treasury repayment, while encouraging the most widespread use of electricity. *Id.* As concerns the requirements of lowest possible rates and widespread use, the court determined that these requirements afford BPA wide latitude in nonfirm energy rate design, providing BPA with so

much discretion that there is no law to apply. *Id.* However, BPA is constrained in its discretion by the other directives in section 7(k), since nonfirm energy rates must be designed with regard to cost recovery and amortization of the investment of the U.S. Treasury over a reasonable period of years.

1.3.3 Inter-Business Line Charges

BPA is determining certain inter-business line costs and unit costs that will affect the transmission and ancillary services rates BPA develops in its separate transmission rate proceeding. With respect to transmission and ancillary services rates, BPA must satisfy section 212(i) of the Federal Power Act (FPA), 16 U.S.C. §824k(i), which states that transmission rates will be governed only by otherwise applicable law, except that no BPA transmission rate applicable to transmission service ordered by the Commission shall be unjust, unreasonable, or unduly discriminatory or preferential as determined by the Commission. Section 212(i) does not require the Commission to examine BPA rates under this standard independent of an Order directing BPA to provide transmission service, but the Commission has previously done so upon BPA's request when presented with transmission rates established by the Administrator in a 7(i) proceeding. *See United States Department of Energy--Bonneville Power Admin.*, 80 F.E.R.C. ¶ 61,118, at 61,370 (1997). Presently, BPA will seek a determination by the Commission as to whether the inter-business line charges established in this rate proceeding will allow the Commission to determine whether transmission and ancillary service rates developed in a separate 7(i) process may satisfy the FPA section 212(i) standard. To this end, BPA will encourage the Commission to examine the methodologies used to develop the inter-business line charges and the results obtained and conclude whether the inter-business line charges are not unjust, unreasonable, or unduly discriminatory or preferential.

1.4 Standard of Judicial Review

Section 9(e)(2) of the Northwest Power Act provides that "final determinations regarding rates under section 7 shall be supported by substantial evidence in the rulemaking record required by section 7(i) considered as a whole." 16 U.S.C. §839f(e)(2). In describing the applicable standards of judicial review, the Ninth Circuit has stated that "[t]his court must affirm the rates if 'substantial evidence in the rulemaking record' supports BPA's determination . . . We must also affirm the agency's action unless it is arbitrary, capricious, an abuse of discretion or in excess of statutory authority." *Alcoa v. Bonneville Power Administration*, 891 F. 2d 748, 752 (9th Cir. 1990). *See also, Southern California Edison Co. v. Jura*, 909 F. 2d 339, 342 (9th Cir. 1990); *Central Lincoln Peoples' Utility District et al. v. Johnson*, 735 F. 2d 1101, 1115 (9th Cir. 1984).