BPA – Transmission Business Line
Programs in Review 2006
Joint Comments of Northwest Requirements Utilities, the Public Generating Pool, PNGC Power, and the Public Power Council
September 7, 2006

The above-named entities (Joint Customers) welcome the opportunity to submit the following comments on BPA's proposed transmission investment and spending plans for FY08-09 (Programs in Review, or PIR). In general, the Joint Customers applaud BPA's overall response to the unanticipated revenue decline in FY05, thus avoiding any need for a emergency rate adjustment. This response demonstrates that transmission costs, though largely viewed as fixed, can be successfully managed in the face of unexpected revenue reductions. The Joint Customers also appreciate BPA's efforts to manage toward a lower level of FTE, while simultaneously facing a transition in staffing needs due to expected retirements. In general, the Joint Customers support the overall levels of investment and expenses proposed for the FY08-09 rate period, and look forward to the opportunity to settle the upcoming transmission rate case. Meanwhile, we strongly recommend that BPA use the freed-up time and human resources to focus discussions on a few key areas where difficult (but not intractable) issues lie before the region, including the following:

- analyzing options for long-term investments in the transmission system and making related choices among potentially competing projects based on clearly articulated and well understood economic principles;
- addressing the transmission aspects of the Regional Dialogue proposal so that new non-federal resources can successfully be integrated into the system to serve the growing loads of Northwest utilities on a comparable basis to federal resources
- making best use of limited Treasury borrowing authority by encouraging cost-effective use of third-party financing;
- understanding the impacts of proposed changes in market design in California and how those changes may spill over into the Northwest as capacity on the Southern Intertie increases;
- easing congestion on the I-5 corridor, especially between Seattle and Portland and north of Seattle;
- implementation of regional planning and expansion processes, as contemplated by ColumbiaGrid;
- continuing to implement the recommendations that are emerging from the EPIP process; new functional reviews (supply chain and O&M) should be released and additional comments solicited; and
- identifying opportunities for joint maintenance exercises, to make best use of scarce human resources and minimize planned outages on the grid.

The remainder of our comments expands on these themes. We look forward to continued collaboration with BPA in these areas.

<u>Improving Customer Involvement in Capital Planning</u>

Based on our understanding of BPA's planning processes, PIR comes near the end of a process that begins early in the calendar year. (See slide 4 of the 2006 PIR Presentation.) Customers perceive that their input is sought after many of the critical decisions have been made for the upcoming rate period. In the final analysis, BPA's revenues from customers must cover expected revenue requirements, and so it is proper for customers to be involved in the process <u>before</u>, not after, critical decisions have been made. BPA has made great strides in recent years in the area of customer involvement by providing quarterly reviews of current revenues and current expenses, which help reduce "surprises" regarding both power and transmission rates. This effort should be expanded to capital planning decisions, not only for transmission but agency-wide. In short, PIR should not be a biennial event, but should be part of a continual review of BPA spending and investments, more intensive at some times than others, but always in the context of involving customers in decisions that they, in turn, will have to pay for.

We have identified several specific needs in this area. First, BPA has indicated that economic principles form part of the basis for investment decisions, and has provided some documentation of the application of those principles in the form of "samples". Customers should be provided an opportunity both to understand the economic principles underlying investment decisions, and to provide feedback to BPA on the appropriateness of these principles and their application. After the close of comment on the 2006 PIR, and assuming that the transmission rate case for FY08-09 can be largely settled, BPA should schedule one or more workshops for an in-depth review of the economics of transmission planning as practiced at BPA. This will become even more important as the region moves to implement the ColumbiaGrid Planning and Expansion Functional Agreement over the next few years.

Second, there should be well-defined opportunities for customer involvement during the capital budgeting process that occurs during February through July of each fiscal year. We are not recommending that customers be present during all deliberations, and we respect the procedural constraints that BPA faces as a federal agency that is part of the overall budgeting process of the executive branch of the federal government. However, the capital budgets eventually find their way into rates paid by end-use consumers in the Pacific Northwest (and to some extent elsewhere), and those consumers should have their interests represented throughout the decision-making process.

Third, it appears that BPA is facing some near-term decisions on specific projects in the I-5 corridor, aimed at reducing congestion especially during the summer months and reducing the likelihood of "OTC excursions". Again, all of BPA's customers will be asked to pay for these projects, and many of BPA's customers will be directly affected as well through improvements (presumably) in reliability. Customer involvement in the decisions related to these projects is critical to their acceptability. (See also comments below on third-party financing).

Improving Third-Party Financing Opportunities

BPA recently held an "open season" to solicit third-party financing of a potential upgrade on the West-of-McNary (WOM) cutplane. Although the upgrade was ultimately not implemented for a variety of reasons, there has been no *post mortem* on the various causes for the decision not to fund this project. (Again, we are not challenging this decision at this time.) Some of these reasons were probably outside BPA's control, such as the lack of success of independent power producers (IPPs) in signing long-term sales agreements with buyers, which might have provided more secure funding for long-term investments by the IPPs. Other reasons were undoubtedly within BPA's control, such as the decision to change the method for calculating Available Transfer Capability (ATC) on the WOM cutplane. Yet a third category of reasons may have something to do with the commercial arrangements offered by BPA to potential investors. Given limitations on BPA's borrowing authority, third-party financing should remain a viable alternative. To that end, a thorough public review of all the causes for the failure of the WOM open season is required.

Although we want to maintain third-party financing as an option, we also need to understand the true cost of third-party financing, especially as it was implemented for the Schultz/Wautoma upgrade. We still have questions about the economic rationale for payments made up front by BPA to secure third-party funding, which effectively reduced the proceeds of the bond sale and raised the cost of this debt. Again, a thorough public review of the Schultz/Wautoma financing is in order.

Implications Of Third-Party Financing

During BPA's Capital Planning Review workshop, it was stated that BPA is considering using third-party financing for potentially $1.5 billion in future borrowings. Considering the potential financial impact this may have on BPA and its customers, we ask that BPA establish a forum for customer participation to evaluate the risks, benefits, and costs prior to committing to third-party financing.

We just went through a period of confusion over BPA's Debt Optimization Program (DOP), which took an extended period of time to resolve, and we wish to avoid such a reoccurrence with respect to the third-party financing issue. Transparency, understanding, education and discussion with BPA's customers will reduce the opportunity for misunderstanding. Recently, this type of collaboration has been successfully demonstrated through both the PBL Power Function Review and the TBL Programs In Review processes, and we hope that this cooperation will continue.

Regional Transmission Planning, Expansion, and Maintenance Practices

Two recent developments, both still clearly "works in progress", point to the continuing pressure to improve the region's approach to planning and expansion. First, the Federal Energy Regulatory Commission (FERC) has issued a Notice of Proposed Rulemaking

(NOPR, Docket No. RM 05-25-000) that, if finalized, will require jurisdictional transmission providers, and those such as BPA seeking "safe harbor" status through the filing at FERC of a *pro forma* Open Access Transmission Tariff (OATT), to add specific provisions explaining their transmission planning procedures. Second, members of ColumbiaGrid and other interested parties are developing a Functional Agreement on planning and expansion of the regional grid. Both the likely regulatory requirements and the opportunity provided by ColumbiaGrid support the development of clearly stated procedures for joint planning and expansion of the transmission grid. To that end, BPA should lay out a proposal for integration of these two efforts: compliance with FERC requirements and implementation of the Functional Agreement.

We are also concerned about some of the potential impacts of proposed Intertie upgrades. Although increased Intertie capacity should offer the opportunity for additional export revenues for the Northwest (both power and transmission), two questions arise. One has to do with the rights of existing Third AC participants to share in upgrades. Before TBL undertakes any capacity expansion, the agency should review the Third AC Participation agreements with counterparties and ensure that any expansion is undertaken in a manner consistent with all rights and obligations under those agreements. The other question has to do with the potential for additional "spill-over" of price excursions in California into the Northwest. The memories of the West Coast energy crisis of 2000-01 are not gone and in some cases live on in the rates being paid by consumers. Any decision by TBL to upgrade the capacity of the Southern Intertie should be based on an analysis of the economic consequences for the Northwest: will this make Northwest consumers more susceptible to potentially uncompetitive market forces and price excursions in California? In workshops, BPA has informed us that this question is still "under evaluation". Any evaluation should be shared with Northwest consumers before an upgrade is actually undertaken.

Finally, we encourage BPA to explore actively opportunities for joint or shared maintenance activities. This may be undertaken through ColumbiaGrid or through separate bilateral or multilateral arrangements. The objective should be to minimize both the costs of the maintenance itself and the impact on energy transactions. We recommend specifically that BPA develop transparent plans for improved cooperation with other transmission providers in the Northwest in order to reduce the total costs of transmission maintenance.

<u>Other Issues</u>

We understand that part of the basis for essentially flat revenue annual expenses between the current and the upcoming rate periods is a depreciation study that was completed by an outside consultant as of the end of FY04. We would like to understand better the assumptions and calculations in this most recent depreciation study, and recommend that BPA hold at least one additional workshop to review the results of the study, after which we may wish to submit further comments or request additional information.

We understand as well that FY06 is currently projected to be an extremely positive year for both of BPA's business lines, and that financial reserves will most likely be at historically high levels by September 30. In light of this good news, we conclude that BPA has no need to include any revenue financing in the revenue requirement for the upcoming transmission rate period.

Thank you again for the opportunity to provide these comments.