A PUBLICATION OF THE BONNEVILLE POWER ADMINISTRATION

keeping CURRENT

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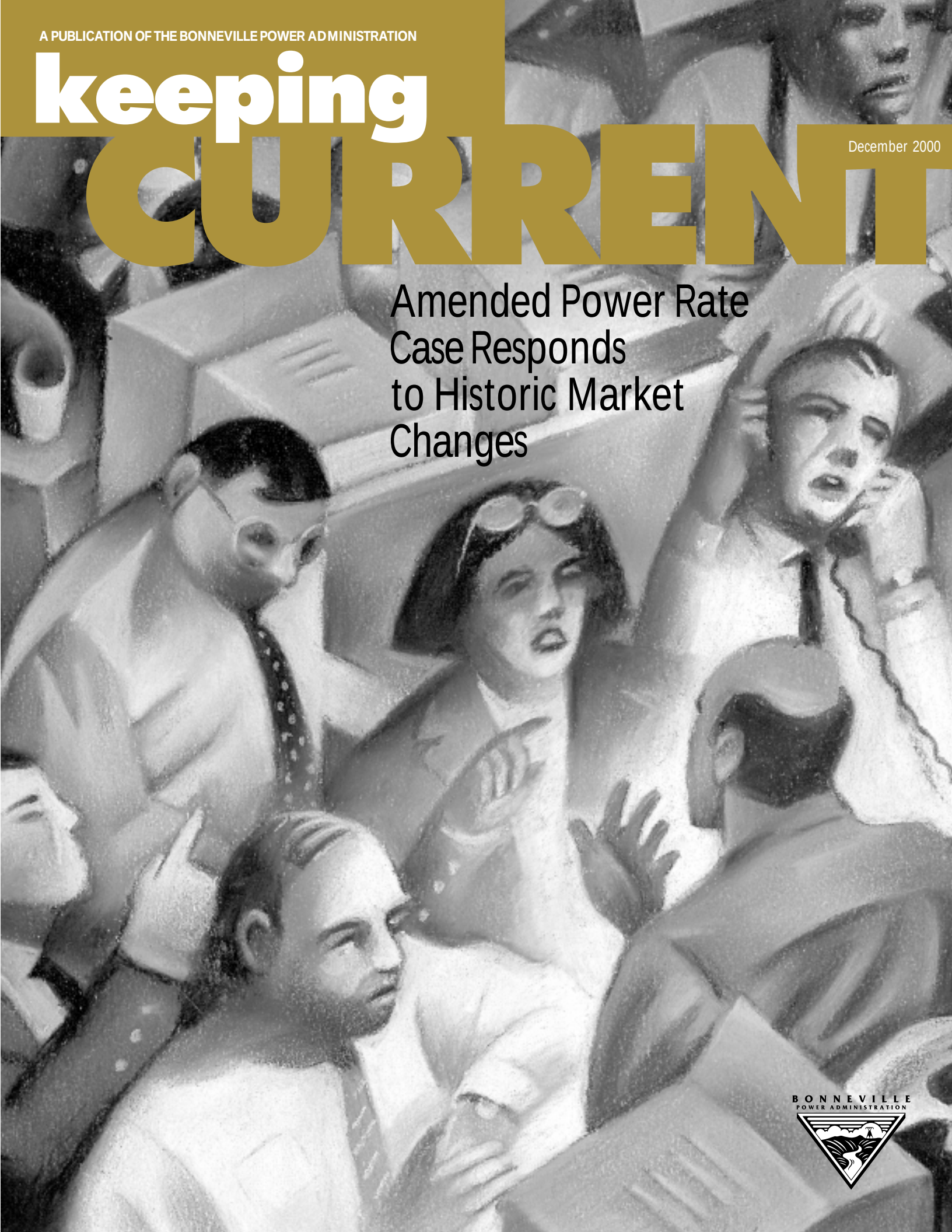
Amended Power Rate Case Responds to Historic Market Changes



BONNEVILLE POWER ADMINISTRATION

This Keeping Current provides a general description of the Bonneville Power Administration's amended power rate proposal and the current status of the rate case proceeding.

Background

Over the last several months, the wholesale market price for electricity has shown volatility and price levels never before seen on the West Coast. During this period, BPA and its customers were negotiating Subscription contracts for the period beginning in October 2001. The Subscription process was concluded on Oct. 31, 2000, with total Subscription sales over 9,000 average megawatts. The total sales were about 1,500 megawatts more than anticipated in the 2002-2006 power rate case that ended in May of this year. Much of the increase in sales can be attributed to the higher, and more volatile, market prices for energy, which had the effect of making BPA Subscription sales more attractive to BPA's customers. The increase in Subscription sales means that BPA will have to augment its power supply from other sources besides the federal system in order to meet all of its contractual commitments.

The dramatic changes in the market have created additional cost pressures on BPA in two ways. First, BPA will need to purchase more power than originally planned in order to meet much greater firm loads; and, second, BPA will likely have to pay more for the power than forecast in the rate case that ended in May 2000. Unless BPA responds to these market changes, BPA's standard for maintaining an 80 to 88 percent probability of making its annual payment to the U.S. Treasury on time and in full would be considerably undermined.

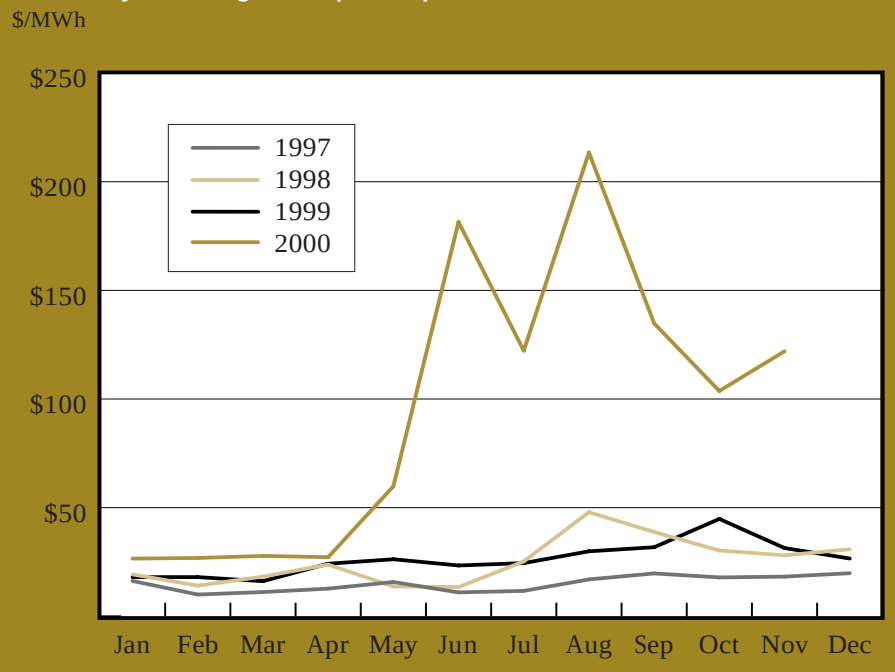
BPA's Treasury payment probability is important because, under the priority of payments established by statute, the U.S. Treasury is lowest priority and is therefore paid last. The administration's Fish and Wildlife Funding Principles include a commitment to achieving a Treasury payment probability within the range of 80 to 88 percent.

After considering comments received from customers and other regional stakeholders, BPA decided to amend its rate proposal, currently before the Federal Energy Regulatory Commission.

The amended power rate proposal

The amended power rate case will focus primarily on modifications to the cost recovery adjustment clause, or CRAC. The original intent of the CRAC was to achieve the probability of BPA making its annual payment to the U.S. Treasury on time and in full at a range of 80 to 88 percent. The combined effects of market volatility, rising wholesale electricity prices and substantially more load from BPA's customers than anticipated

Monthly average on-peak prices



This graph shows how overall market volatility has increased. The annual average on-peak price in 1997 was $15 per megawatt-hour compared to $95 per megawatt-hour in 2000.

during the 2002-2006 rate case has made it necessary to revise the CRAC mechanism in order to maintain an acceptable range.

In the proposed rates currently before FERC, BPA had a single CRAC, which could trigger each year, if actual accumulated net revenues fell below a predetermined threshold. In addition, the amount that could be collected each year was capped at a certain amount.

The proposed new CRAC is larger than the one included in the May rate filing, and it has three components. The new proposal would modify the CRAC structure as follows:

Load-based CRAC: This CRAC is a cost adjustment tied to the amount of augmentation power that has not yet been purchased. BPA is proposing that the load-based CRAC be based on a value of $34 per megawatt-hour and additional augmentation of approximately 2,400 average-megawatts that remain to be purchased. It will raise approximately $180 million per year. If adopted in the amended rate proceeding and if triggered, the load-based CRAC would have the effect of about a 15 percent increase over the base power rate in the May proposal, which averages 3.3 mills per kilowatt-hour across all Subscription sales. It will go into effect on Oct. 1, 2001, but the exact amount will not be known until the amended rate case proceeding is finished.

Financial-based CRAC: The financial-based CRAC is closest to the CRAC that was proposed in the rate case. It would trigger if BPA's forecast of end-of-year accumulated net revenues fall below the equivalent of $660 million in reserves and would be capped at $330 million per year. If needed, it would trigger for only one year at a time – although it is possible that it could trigger in each of the five years of the rate period. BPA is proposing that all financial-based CRAC revenues be collected during the four-month period from March through June. Since the financial-based CRAC would trigger based on a forecast, the amount of the CRAC would be trued-up based on audited actual net revenues once they are available.

On an expected value basis, the financial-based CRAC would raise about $60 million per year, resulting in a rate adjustment of about 1.0 mill.

In summary, the load-based and financial-based CRAC will apply to firm power purchases under the priority firm (PF) (excluding Slice customers), industrial firm (IP), residential load (RL) and new resource (NR) rate schedules. These CRACs will not apply to pre-subscribers, Slice, or the financial portion of the Residential Exchange Settlement.

Safety-net CRAC: This is a CRAC that would trigger if BPA has missed a payment to Treasury, or forecasts that it will miss a payment to Treasury even after taking into

Subscription process completed

BPA concluded the Power Subscription Process on Oct. 31, 2000. The final results are impressive.

BPA's total Subscription sales were 9,082 average megawatts.

- 135 public customers signed up for 6,596 megawatts. This includes pre-subscription signers, other federal agencies and contingent signers. It also includes 30 customers who signed up for 2,000 megawatts of Slice and 1,218 megawatts of BPA's block power product. Of the 135 public customers, 127 signed 10-year contracts; eight signed for five years.
- 6 investor-owned utilities signed contracts for 1,000 megawatts of power. Five of these signed 10-year contracts; one signed for five years.
- 8 direct service industry customers signed contracts totaling 1,486 megawatts.

The number of 10-year Subscription contracts is good news for BPA and the region, helping to insure that the agency will have the financial stability it needs to fulfill its public purposes such as funding Northwest fish and wildlife programs and providing market incentives for the development of conservation and renewable resources while still ensuring BPA makes its treasury payment. BPA's rates are subject to revision in the rate proceeding for the 2007-2011 period.

consideration the implementation of the financial-based CRAC and all prudent cost-management measures available. Its purpose would be to avoid a second missed Treasury payment. If this CRAC component is triggered, BPA will propose a temporary upward adjustment to rates, possibly with a cap and duration in excess of those in the financial-based CRAC. BPA would conduct a public process on its proposal prior to making a final decision on the CRAC adjustment.

How the CRAC mechanisms will affect different customer classes

BPA's proposal does not redesign the basic rates developed in the earlier phase of this rate case. Instead, the intent and design of the proposed CRAC mechanism is to mitigate risks that have been created by the immediate problem of rising prices in a market that is more volatile than anticipated. The load-based CRAC is required because unforeseen developments in the wholesale power market resulted in the forecast amount of public load and market prices being higher than expected.

As outlined in the previous section, assuming a 15 percent load-based CRAC, preference customers will see an increase in their priority firm rate of about 3.3 mills/kilowatt-hour from the load-based CRAC.

Investor-owned utilities will see an increase from the load-based CRAC of about 2.9 mills/kilowatt-hour on the residential load (RL) rate. The amended proposal will also increase the value of the 900 average megawatts financial portion of the IOU residential settlement by basing the financial benefits on a value of $34 per megawatt-hour rather than $28 per megawatt-hour. These financial benefits would be subject to the safety-net CRAC, but not the load-based or financial-based CRACs. The 1,000 average megawatts of physical power deliveries to the IOUs would be subject to all three CRAC mechanisms, the same as other loads.

Direct service industry customers will see an increase of about 3.5 mills per kilowatt-hour on the industrial firm (IP) targeted adjustment clause rate. This is the rate they will pay for the 1,400-plus average megawatts of actual power they will receive from BPA.

Consistent with the May proposal, neither the load-based CRAC nor the financial-based CRAC applies to Slice customers. Because Slice customers assumed BPA's risks associated with market volatility directly, they were not subject to CRAC or planned net revenues for risk. One of the risks assumed was the net cost of augmenting the system to meet load. Slice customers will continue to pay their pro rata share of BPA's actual augmentation costs. This is likely to be more than the limited augmentation cost exposure these customers had in BPA's original rate proposal. The Slice customers will be significantly impacted because they will be responsible to pay for a pro rata share of BPA's actual augmentation cost expense rather than a forecast of those costs.

Even if both the load-based and the financial-based CRACs trigger, BPA's cost-based rates will continue to be well below the market alternatives. But we realize that this is cold comfort. Our customers depend on us for low cost-based rates and BPA understands the hardships created by rate increases as well as the delay and uncertainty created by the rate amendment proposal. We are taking this step only because we see no viable alternative.

What happens next?

The pre-hearing conference will be held on Dec. 12, 2000. At that time, the hearing officer will set the schedule for the amended power rate process including the public comment period and a field hearing designed to collect comments from the general public and other non-rate case parties. BPA plans to complete the final, amended Record of Decision by mid-June of 2001 and would then submit the amended record to FERC for interim and final approval sometime in July 2001.

For more information, visit BPA's Web site at: *http://www.bpa.gov/Power/PSP/rates/RateCase/*, or call (503) 230-4328 or toll free 1-800-622-4519.

Bonneville Power Administration
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