DEPARTMENT OF ENERGY
BONNEVILLE POWER ADMINISTRATION

Legal Interpretation of Section 7(b)(2) of the Pacific Northwest Power Planning and Conservation Act

I. Background

A. Relevant Statutory Provisions

BPA is charged with the responsibility of implementing section 7(b)(2) of the Northwest Power Act. An agency's interpretation of the statute it is charged to administer is entitled to great deference; in particular, the United States Supreme Court has held that "it is clear that the Administrator's interpretation of the Regional [Northwest Power] Act is to be given great weight." *Aluminum Co. of America v. Central Lincoln Peoples' Util. Dist.*, 467 U.S. 380, 389 (1984).

Basic principles of statutory construction must be followed in interpreting the Northwest Power Act. These principles require that particular provisions of a statute be interpreted to give effect to its overall purposes. *United States v. Am Trucking Ass'n*, 310 U.S. 534, 543 (1950). Wherever possible, statutory provisions should be construed so as to be consistent with each other. *Adams v. Howerton*, 673 F.2d 1036, 1040 (9th Cir. 1982), cert. denied, 458 U.S. 1111 (1982). Thus, BPA interprets the Northwest Power Act in a manner which seeks consistency among the requirements of each section of the Northwest Power Act.

In addition to the Northwest Power Act, BPA is governed by the Bonneville Project Act. 16 U.S.C. § 832, *et seq.*, the Federal Columbia River Transmission System Act, 16 U.S.C. § 838 *et seq.*, and the Flood Control Act of 1944, 16 U.S.C. § 825 *et seq.* These statutes require BPA to set rates, in accordance with sound business principles, at levels sufficient to recover BPA's total system costs, including repayment of the Federal Treasury investment in the Federal Columbia River Power and Transmission System. All statutory provisions concerning the timely recovery of BPA's revenue requirement are relevant to the interpretation of the Northwest Power Act. For "[w]hen there are two acts upon the same subject, the rule is to give effect to both if possible." *Morton v. Mancari*, 417 U.S. 535, 551 (1974), quoting *United States v. Borden Co.*, 308 U.S. 188, 198 (1939).

Section 7 of the Northwest Power Act, 16 U.S.C. § 839e, contains a number of directives that the BPA Administrator must consider in establishing rates for the sale of electric energy and capacity and for the transmission of non-Federal power. Section 7(b)(2), commonly referred to as the "rate test," is one of these directives. Section 7(b)(2) of the Northwest Power Act, 16 U.S.C. § 839e(b)(2), provides:

> After July 1, 1985, the projected amounts to be charged for firm power for the combined general requirements of public body, cooperative, and Federal agency customers exclusive of amounts charged such customers under subsection 7(g) of this section for the costs of

conservation, resource and conservation credits, experimental resources and uncontrollable events, may not exceed in total, as determined by the Administrator, during any year after July 1, 1985, plus the ensuing four years, an amount equal to the power costs for general requirements of such customers if, the Administrator assumes that--

(A) the public body and cooperative customers' general requirements had included during such five-year period the direct service industrial customer loads which are

(i) served by the Administrator, and

(ii) located within or adjacent to the geographic service boundaries of such public bodies and cooperatives;

(B) public body, cooperative, and federal agency customers were served, during such five-year period, with Federal base system resources not obligated to other entities under contracts existing as of December 5, 1980, (during the remaining term of such contracts) excluding obligations to direct service industrial customer loads included in subparagraph (A) of this paragraph;

(C) no purchases or sales by the Administrator as provided in section 5(c) were made during such five-year period;

(D) all resources that would have been required, during such five-year period, to meet remaining general requirements of the public body, cooperative and Federal agency customers (other than requirements met by the available Federal base system resources determined under subparagraph (B) of this paragraph) were--

(i) purchased from such customers by the Administrator pursuant to section 6, or

(ii) not committed to load pursuant to section 5(b),

and were the least expensive resources owned or purchased by public bodies or cooperatives; and any additional needed resources were obtained at the average cost of all other new resources acquired by the Administrator; and

(E) the quantifiable monetary savings, during such five-year period, to public body, cooperative and federal agency customers resulting from--

(i) reduced public body and cooperative financing costs as applied to the total amount of resources, other than Federal base system resources, identified under subparagraph (D) of this paragraph, and

(ii) reserve benefits as a result of the Administrator's actions under this Act

were not achieved.

16 U.S.C. § 839e(b)(2).

B. Scope of Interpretation

This Legal Interpretation resolves only the basic legal issues necessary to implement section 7(b)(2) and modifies the first Legal Interpretation issued June 8, 1984. *See* Legal Interpretation of Section 7(b)(2) of the Pacific Northwest Electric Power Planning and Conservation Act, 49 Fed. Reg. 23,998 (June 8, 1984).

II. Interpretation

A. Definitions

This section contains definitions applicable to section 7(b)(2). Terms identified in the Northwest Power Act have the same meaning in this interpretation, unless further defined.

1. Relevant Rate Case: The section 7(i) wholesale power rate adjustment proceeding being conducted at the time the projections for section 7(b)(2) are made, and in which any adjustment to rates in accordance with section 7(b)(2) may be reflected.

2. General Requirements: The public body, cooperative and Federal agency customers' electric power assumed in the Relevant Rate Case to be purchased from BPA, exclusive of new large single loads. General Requirements are limited to power purchased from BPA under section 5(b) of the Northwest Power Act; section 5(c) purchases from BPA are not included.

3. 7(b)(2) Customers: Those firm power customers of BPA that are listed in section 7(b)(2) of the Northwest Power Act as subject to the rate test, *viz*, public bodies, cooperatives, and Federal agencies.

4. Applicable 7(g) Costs: The costs identified in section 7(g) of the Northwest Power Act that are also listed in section 7(b)(2), *viz*, costs chargeable to 7(b)(2) Customers for conservation, resource and conservation credits, Experimental Resources and Uncontrollable Events.

5. Uncontrollable Event: A discrete event which differs from the continuum of changing events that occur in nature, business and government (such as changes in water conditions, aluminum prices, and electricity markets) and that are routinely reflected in ratemaking.

6. Experimental Resources: Resources that are undergoing research and development and are funded by BPA in full or in part.

7. Five-Year Period: The rate recovery period of the Relevant Rate Case, plus the ensuing four years. If the Relevant Rate Case has more than a one-year rate recovery period, the Five-Year Period will be greater than five years.

8. Program Case: The entire process of calculating rates to be charged in the Five-Year Period of the Relevant Rate Case under the provisions of the Northwest Power Act other than section 7(b)(2), including all specific data, assumptions, and results.

9. 7(b)(2) Case: The entire process of calculating rates for the relevant Five-Year Period under the provisions of section 7(b)(2) of the Northwest Power Act, including all specific data, assumptions, and results.

10. Five Assumptions: The five differences between the Program Case and the 7(b)(2) Case specified in subsections (A) through (E) of section 7(b)(2) of the Northwest Power Act.

11. DSI Loads: Those loads of direct service industries (DSI) that are forecast to be served by BPA, during the Five-Year Period, pursuant to sections 5(d)(1) or 5(f) of the Northwest Power Act.

12. Within or Adjacent: Relating to DSI customer loads determined in accordance with section 7(b)(2)(A) to be electrically within or adjacent to the geographic service territories of 7(b)(2) Customers.

13. Quantifiable Monetary Savings: The change in annual costs attributable to differences in resource financing or Reserve Benefits.

14. Reserve Benefits: The annual financial value of interruptible load that forestalls a resource acquisition by virtue of the ability to curtail the load at a time when off-line generation would otherwise need to be available to startup and serve load during unexpected conditions.

B. General Approach and Specific Issues of Interpreting Section 7(b)(2)

Section 7(b)(2) assures that 7(b)(2) Customers are charged no more for their General Requirements after July 1, 1985, than they would have been charged if the Five Assumptions were to be realized. These assumptions direct BPA to hypothesize power supply arrangements between itself and its customers that are quite different from reality. Implementation of the Five Assumptions listed in section 7(b)(2) is by nature an exercise in speculation. This interpretation was undertaken to reduce this inherent speculation insofar as possible.

1. Interpretation: Section 7(b)(2) limits the 7(b)(2) Case to the Five Assumptions listed in section 7(b)(2) and the secondary effects of those assumptions.

Discussion:

The Northwest Power Act provides that after July 1, 1985, the 7(b)(2) Customers' power costs "may not exceed … as determined by the Administrator" the power costs for General Requirements based on the enumerated Five Assumptions. 16 U.S.C. § 839e(b)(2). This language grants the Administrator discretion to determine the manner in which the Five Assumptions of section 7(b)(2) are applied and the rate test is implemented. However, BPA recognizes that the reasonableness of methodologies used to implement section 7(b)(2) will be tested in the Relevant Rate Case.

The Administrator will exercise his discretionary authority in the following manner. Except for the Five Assumptions specified in section 7(b)(2), all underlying premises will remain constant between the Program Case and the 7(b)(2) Case. Assumptions not specified by the statute will not be considered. Secondary effects, however, of the Five Assumptions will be given full recognition in the modeling of the 7(b)(2) Customers' power costs in the 7(b)(2) Case. This general approach will allow the 7(b)(2) Case to be modeled under the same accepted ratemaking techniques used in the Program Case. This approach will also avoid the modeling of a hypothetical world that attempts to reflect in extreme detail what would have occurred had the Northwest Power Act not been enacted.

The legislative history of the Northwest Power Act supports limiting the assumptions of the 7(b)(2) Case to those specified in the statute. The House Committee on Interstate and Foreign Commerce Report accompanying S. 885 (the bill that became the Northwest Power Act) notes that "[t]he assumptions to be made by the Administrator in establishing this ceiling are specifically set forth." H. Rep. No. 976-I, 96th Cong., 2d Sess. 68 (1980). Similarly, the Report of the House Committee on Interior and Insular Affairs declares that "[s]ubsection 7(b)(2) establishes a 'rate ceiling' for BPA's preference customers, and specifies the method of calculating this ceiling…" H. Rep. No. 976-II, 96th Cong., 2d Sess. 52 (1980).

Legislative history also supports including the unavoidable secondary effects of the assumptions listed in the Northwest Power Act. In particular, in addressing Reserve Benefits, Appendix B to the Report of the Senate Committee on Energy and Natural Resources provides that in addition to costs specifically described in sections 7(b)(2)(B) and (D), the Administrator is to consider "[a]ny other general system operating costs, including reserves…" S. Rep. No. 272, 96th Cong., 1st Sess. (1979), Appendix B at 58.

As an illustration of the secondary effects referred to above, BPA has identified two secondary effects of the Five Assumptions found in section 7(b)(2). These effects involve surplus levels and secondary energy markets. The secondary effects must be included in section 7(b)(2) methodologies as natural consequences of the Five Assumptions in section 7(b)(2) on the results of underlying premises that are held constant between the Program Case and the 7(b)(2) Case. Surplus levels and the secondary energy market must change as a natural consequence of the Five Assumptions. As the DSIs are assumed to shift to the private utilities and 7(b)(2) Customers under section 7(b)(2), BPA's load/resource balance changes. This change will affect the level of BPA's surplus. The secondary energy market will also change; the top quartile of DSI Loads will not be served by BPA's secondary energy.

Section 7(b)(2) requires BPA to assume that the 7(b)(2) Case is identical to the Program Case except for those differences required by the Five Assumptions set out in section 7(b)(2)(A)-(E). Present modeling techniques used in the Program Case, which will be used in the modeling of the 7(b)(2) Case, incorporate secondary effects.

2. Interpretation: Implementation of section 7(b)(2), and any subsequent reallocation pursuant to section 7(b)(3), will not conflict with the requirements of section 7(a).

Discussion:

BPA will conscientiously follow the requirements of section 7(b)(2) to perform the "rate test" for its public body, cooperative and Federal agency customers. If the results of the rate test indicate that BPA must recover costs in excess of those allowed under section 7(b)(2), BPA will implement the section 7(b)(3) supplemental rate charge provision for that purpose. BPA's concern is that failure to recover some, or all, of the reallocated costs "through supplemental rate charges for all other power sold by the Administrator to all customers" may result in BPA's inability to meet the requirements of section 7(a). Such a determination, if it occurs, would be rigorously documented and exposed to careful review during the section 7(i) process for the Relevant Rate Case. Should this occur, BPA would be forced to resolve a possible conflict among sections 7(b)(2), 7(b)(3), and 7(a).

Section 7(a) of the Northwest Power Act requires that BPA rates recover the costs of the electric power and transmission systems, including the repayment of Federal Treasury investments in those systems. Section 7(a) reaffirms this long-standing obligation which was articulated earlier in the Bonneville Project Act and the Federal Columbia River Transmission System Act. Section 7(b)(2) must be applied in a manner which enables BPA to set rates at levels sufficient to recover costs, or the rates will not receive confirmation and approval from the Federal Energy Regulatory Commission. *See* 16 U.S.C. § 839e(a)(2).

The legislative history of the Northwest Power Act supports application of section 7(b)(2) in a manner consistent with BPA's primary statutory obligation that its rates recover costs. The House Interior Committee report declares that:

> Section 7 of the legislation sets out the requirements BPA must follow when fixing rates for the power sold its customers under this legislation. Subject to the general requirement (contained in section 7(a)) that BPA must continue to set its rates so that its total revenues continue to recover its total costs, BPA is required by the legislation to establish the following rates: [report continues by setting out rate structure of the Act].

H. Rep. No. 976-11, 96th Cong., 2d Sess. 36 (1980).

Section 7(a)(2) illustrates the importance of BPA's statutory obligation to set rates at levels sufficient to collect its costs. Section 7(a)(2) states that FERC cannot approve BPA's rates unless the rates "are sufficient to assure repayment of federal investment in the Federal Columbia

River Power System over a reasonable number of years after first meeting the Administrator's other costs," 16 U.S.C. § 839e(a)(2)(A), and "are based upon the Administrator's total system costs…" 16 U.S.C. § 839e(a)(2)(B). Indeed:

> BPA is a self-financed agency under the terms of the Federal Columbia River Transmission System Act of 1974. This means that BPA receives no appropriations. It is required by law to cover its full costs through its own revenues derived from the sale of power and other services… The United States of America does not stand behind BPA's obligations. … BPA alone must meet these obligations, and BPA's rates cannot be approved by FERC unless they are sufficient to meet these obligations. These requirements, and the lack of any Federal guarantees, are made explicit in sections 6(j) and 7(a) of S 885, even though they are also explicit in the Federal Columbia River Transmission System Act.

126 Cong. Rec. H9843 (daily ed. Sep. 29, 1980) (statement of Rep. Ullman).

BPA is neither predetermining the results of the rate test nor suggesting a disregard for section 7(b)(2) with this discussion. BPA is not suggesting a solution to any problem arising from a potential conflict among sections 7(a), 7(b)(2), and 7(b)(3). BPA is merely attempting through this interpretation to alert its customers and the public to one possible problem which may present itself in the future.

3. Interpretation: Applicable 7(g) Costs are to be excluded from the Program Case rates and the 7(b)(2) Case rates prior to comparison with the 7(b)(2) Case rates.

Discussion:

Section 7(b)(2) states: "…the projected amounts to be charged for firm power for the combined general requirements of public body, cooperative and Federal agency customers, exclusive of amounts charged such customers under subsection (g) for the costs of conservation, resource and conservation credits, experimental resources and uncontrollable events, may not exceed in total, … an amount equal to the power costs for general requirements of such customers if the Administrator assumes…" the Five Assumptions. 16 U.S.C. § 839e(b)(2).

The foregoing language describes the basic comparison of the Program Case and the 7(b)(2) Case in performing the section 7(b)(2) rate test. In particular, it sets forth the instructions on how BPA is to initially construct the two revenue requirements that will serve as the foundation of the rate test comparison. The language begins with the Program Case. The revenue requirement in the Program Case rate is to be constructed from the "projected amounts to be charged for firm power" for the "general requirements" of BPA's preference customers. This phrase refers to the firm power costs BPA is proposing to recover through its 7(b) rates. Thus, BPA is to start with its total revenue requirement in the Program Case.

The statutory language further directs BPA to modify this revenue requirement by excluding "the amounts charged such customers under subsection (g) for the costs of conservation, resource and conservation credits, experimental resources and uncontrollable events…" In other words, BPA must subtract the identified 7(g) costs (referred to hereafter as Applicable 7(g) Costs) from the Program Case revenue requirement. This reduces the revenue requirement in the Program Case, resulting in the power costs to be recovered in the Program Case.

The second half of the above-noted language then describes how BPA is to initially construct the revenue requirement in the 7(b)(2) Case. Specifically, the 7(b)(2) Case revenue requirement is equal to "the power costs for general requirements of such customers…" as modified by the Five Assumptions. The phrase "power costs for general requirements of such customers" is a direct reference back to the same power costs, general requirements, and customers discussed in the earlier clause when calculating the costs of the Program Case. The only substantive textual difference between this clause and the previously discussed language is the reference to "power cost." That difference, however, is immaterial because the phrase "power costs" is simply a short-hand reference to the longer description of "the amounts to be charged for firm power" used in the preceding section. Because the two clauses are identical in all material respects, the two provisions should be interpreted consistently. Consequently, the same power costs that were used to serve the "general requirements" in the Program Case should be used to construct the revenue requirement for the 7(b)(2) Case; that is, "the projected amounts to be charged for firm power … exclusive of" Applicable 7(g) costs.

This interpretation, in addition to being consistent with the aforementioned statutory text, also makes practical sense when actually implementing the 7(b)(2) rate test. First, having symmetry between the initial power costs in the Program Case and the 7(b)(2) Case ensures that the later application of the Five Assumptions is the central reason the rate test triggers or fails to trigger. Congress specifically identified the Five Assumptions as the factors the Administrator was to "assume" in conducting the rate test. By limiting the cost differences between the Program Case and the 7(b)(2) Case before the application of these assumptions, BPA can give the full and proper effect to the rate test construct envisioned by Congress. Without this symmetry, the rate test results may become skewed by factors other than the Five Assumptions. For example, if Applicable 7(g) costs were excluded from the Program Case (making it less expensive), but included in the 7(b)(2) Case (making it more expensive), it could create a cost incongruity that could become a determinative factor in whether the rate test will trigger. Having an equilibrium between the costs in the Program Case and the 7(b)(2) Case reduces these unintended consequences and preserves the Congressionally identified drivers of the rate test—the Five Assumptions.

Second, this interpretation also avoids potential conflicts with the remaining sections of the 7(b)(2) rate test. Specifically, if the "power costs" used in the 7(b)(2) Case were not interpreted to mean the same power costs in the Program Case, a conflict would occur between the above-mentioned paragraph and section 7(b)(2)(D)(i), the fourth of the Five Assumptions. The fourth assumption specifies that any remaining General Requirements in the 7(b)(2) Case that have not been satisfied by Federal Base System (FBS) resources pursuant to the second assumption (*i.e.*,

section 7(b)(2)(B)) are met with resources taken from a resource stack developed in accordance with subsection 7(b)(2)(D). *See* Issue 11 *supra*.

Section 7(b)(2)(D) provides:

> all resources that would have been required, during such five-year period, to meet remaining general requirements of the public body, cooperative and Federal agency customers (other than requirements met by the available Federal base system resources determined under subparagraph (B) of this paragraph) were –
> (i) purchased from such customers by the Administrator pursuant to section 6, or
> (ii) not committed to load pursuant to section 5(b),
> and were the least expensive resources owned or purchased by public bodies and cooperatives; and any additional needed resources were obtained at the average cost of all other resources acquired by the Administrator…

16 U.S.C. § 839e(b)(2)(D). Resources that meet the criteria identified in section 7(b)(2)(D) are assumed to be in a "resource stack," available for use to serve the General Requirements of the 7(b)(2) Customers in the 7(b)(2) Case. This resource stack includes three types of resources. Type 1 resources are resources the Administrator acquired or plans to acquire from 7(b)(2) Customers pursuant to section 6 of the Northwest Power Act. Type 2 resources are not committed to load pursuant to section 5(b). Type 3 resources are any remaining needed resources. *See* Issue 11 *supra*. It is the Type 1 resources that create an anomaly in the treatment of 7(g) costs.

When resources are included in the resource stack, they are not used to serve General Requirements in the 7(b)(2) Case unless needed and selected from the stack. Section 7(b)(2)(D) refers to "resources … purchased from such [7(b)(2)] customers by the Administrator pursuant to section 6 [of the Northwest Power Act]." *Id.* Conservation is a resource that is assumed to be available in the resource stack. The Northwest Power Act specifically defines conservation as a resource:

> "Resource" means – electric power, including the actual or planned electric power capability of generating facilities, or actual or planned *load reduction resulting from* direct application of a renewable energy resource by a consumer, or from *a conservation measure*.

16 U.S.C. § 839a(19) (emphasis added). Furthermore, conservation is acquired pursuant to section 6 of the Act. Section 6 provides, *inter alia*, that "[t]he Administrator shall acquire such resources through conservation…" 16 U.S.C. § 839d(a)(1). Therefore, conservation is a Type 1 resource and must be included in the resource stack.

Conservation resources and billing credit resources, however, can only be included in the resource stack if Applicable 7(g) costs are removed from the 7(b)(2) Case. Recall that the Applicable 7(g) costs exclude the cost "*of conservation, resource and conservation credits*, experimental resources and uncontrollable events…" 16 U.S.C. § 839e(b)(2) (emphasis added).

The import of leaving the Applicable 7(g) costs in the 7(b)(2) Case is that the costs of "conservation, resource and conservation credits" will remain in the 7(b)(2) revenue requirement. With conservation costs already in the costs of the 7(b)(2) Case, there is no logical way for conservation resources to be available *again* in the resource stack. To do so would be to effectively double-count the conservation costs – first in the 7(b)(2) revenue requirement (because they were never taken out), and second as the costs of a Type 1 resource (assuming it is selected). The only way to avoid this double-counting is to either remove the conservation costs from the 7(b)(2) Case revenue requirement *or* remove conservation resource costs from the resource stack.

In BPA's view, the more appropriate alternative is the former. Treating conservation as a Type 1 resource gives full effect to section 7(b)(2)(D)(i). The Administrator will be fulfilling the Congressional mandate to include resources in the 7(b)(2) Case resource stack "purchased from such customers by the Administrator pursuant to section 6…," *e.g.*, conservation resources. 16 U.S.C. § 839e(b)(2)(D)(i). By contrast, the latter alternative of removing all conservation costs from the resource stack would completely frustrate the purpose of referring to section 6 resources in section 7(b)(2)(D)(i). The better interpretation is therefore to include conservation as a Type 1 resource. To effectuate this interpretation, Applicable 7(g) costs, which include conservation costs, must be removed from the 7(b)(2) Case revenue requirement.

In summary, BPA will interpret the aforementioned statutory language as meaning that the Program Case and 7(b)(2) Case must begin with the same power costs. That is, the Applicable 7(g) costs will be excluded from both the Program Case and the 7(b)(2) Case prior to application of the Five Assumptions. This interpretation is consistent with the statutory language and the purpose of the section 7(b)(2) rate test. It also avoids unnecessary conflicts with, and gives full effect to, the other provisions of section 7(b)(2).

4. Interpretation: The appropriate Five-Year Period is the rate recovery period for the applicable rate case plus the ensuing four years.

Discussion:

Section 7(b)(2) states: "…during any year after July 1, 1985, plus the ensuing four years, …" and several times thereafter "…during such five-year period…" "Any year," in this context, refers to the period of time applicable to the opening statement of section 7(b)(2), namely, the period over which "the projected amounts to be charged for firm power" is applicable, otherwise known as the revenue recovery period.

BPA has had varying lengths of revenue recovery periods in the 22 years between July 1, 1985, and October 1, 2007. Four times BPA has used two-year periods, twice BPA has used five-year periods, once for one-year, once for three-years, and once for 27 months. In each of these periods, the rate test was performed on the basis that the revenue recovery period was the "first year" of the Five-Year Period. For each of these rate tests, the four years subsequent to the last year of the revenue recovery period were appended to form the Five-Year Period.

It is reasonable to consider that the Five-Year Period might encompass more than 60 months. As noted above, the rate test is to compare the projected amounts to be charged for firm power. In the instance of a revenue recovery period that encompasses more than 12 months, the projected amounts to be charged are developed for the entire revenue recovery period. Therefore, to be consistent with the development of the amounts to be charged, it is reasonable to consider that time period, be it for 12 months or more, the first year of the period of consideration for the rate test.

5. Interpretation: 7(b)(2) Customers' loads include DSI Loads that are Within or Adjacent to the 7(b)(2) Customers' service territories.

Discussion:

Section 7(b)(2)(A) provides that BPA is to assume that "the public body and cooperative customers' general requirements had included during such five-year period the direct service industrial customer loads which are: (i) served by the Administrator, and (ii) located within or adjacent to the geographic service boundaries of such public bodies and cooperatives…" 16 U.S.C. § 839e(b)(2)(A). The plain language of section 7(b)(2)(A) requires the Administrator to assume that 7(b)(2) Customers' loads include any Within or Adjacent DSI Loads during the Five-Year Period.

The legislative history of the Northwest Power Act also supports BPA's interpretation of the statute. In the analysis of the section 7(b)(2) directives contained in Appendix B to the Senate Report, S. Rep. No. 272, 96th Cong. 1st Sess., at 65-79 (1979), forecasted DSI Loads were transferred from BPA to 7(b)(2) Customers for the entire test period regardless of contracts in effect as of the effective date of the Northwest Power Act. In the projections contained in Appendix B, calculations of public agency loads for the 7(b)(2) Case included a full 85 percent of projected DSI Loads beginning in 1980 (85 percent was the amount determined to be "Within or Adjacent" to preference agency service areas). Although Appendix B is not conclusive evidence of legislative intent, it was "an important part of the common understanding about how the costs of resources would be distributed as a result of [the Northwest Power Act]." *Id.* at 31. Appendix B is a useful tool for statutory construction where it does not conflict with the language of the statute.

6. Interpretation: BPA will use Appendix B of the Senate Report to assist in determining which DSI Loads are Within or Adjacent to the geographic service boundaries of 7(b)(2) Customers.

Discussion:

Section 7(b)(2)(A) requires the Administrator to assume that during the relevant Five-Year Period, "the public body and cooperative customers' general requirements had included … the direct service industrial customer loads which are … located within or adjacent to the geographic service boundaries of such public bodies and cooperatives…" 16 U.S.C. § 839e(b)(2)(A). It is

not apparent from the statute how BPA is to resolve the question of which DSIs are Within or Adjacent to public body and cooperative customers' boundaries. Therefore, BPA must look to legislative history to resolve the ambiguity.

The legislative history of the Northwest Power Act indicates that a determination of which DSIs are Within or Adjacent to public body and cooperative customers' boundaries was made in Appendix B. S. Rep. No. 272, 96th Cong., 1st Sess., Appendix B at 66. Appendix B includes a table listing the DSIs "within BPA preference customers' service areas," DSIs "adjacent to BPA preference customers' service areas" and those DSIs that "could not readily be served by BPA preference customers." *Id.*

The Within or Adjacent table in the numerical analysis in Appendix B is accompanied by a narrative explanation which states that the loads for establishing resource requirements under section 7(b)(2) will include "DSI total loads within or adjacent to the service territory of the public bodies and cooperatives. (85 percent of existing DSIs as shown in the attached table)." *Id.* at 58. The detailed nature of the Within or Adjacent table and the narrative explanation in Appendix B convince BPA that Congress intended the Appendix B table to be used in resolving which DSIs are Within or Adjacent to the service territory of public body and cooperative customers. The Appendix B table will be disregarded only if conditions of service to those DSI customers change, such as in the case of termination of BPA service to a DSI industrial plant or if the location of the DSI changes from an IOU service territory to a public utility service territory.

Adjacent will be assessed on electrical connections rather than a strictly locational basis. Circumstances may occur where a DSI's location may be outside of a 7(b)(2) Customer's service territory, but a direct electrical connection exists between the DSI and the 7(b)(2) Customer. Conversely, a DSI's location may be inside a 7(b)(2) Customer's service territory, but no direct electrical connection exists between the DSI and the 7(b)(2) Customer. This determination will consider normal operating electrical connections and disregard emergency connections.

7. Interpretation: All DSI Loads assumed to be placed on 7(b)(2) Customers will be treated as firm loads.

Discussion:

Section 7(b)(2)(A) provides that BPA is to assume "that the public body and cooperative customers' general requirements had included during such five-year period the direct service industrial customers loads…" 16 U.S.C. § 839e(b)(2)(A). Section 7(b)(2)(A) does not expressly state the nature or quality of service assumed to be provided by the public bodies and cooperatives to the relevant DSI Loads.

The DSI Loads originally served by BPA under the Northwest Power Act included three quartiles that were firm loads and one quartile (the first quartile) that BPA did not plan or acquire resources to serve. However, the language of the Act is compelling that Congress intended all

relevant DSI Loads, assumed to be served by public bodies and cooperatives, to be treated as firm.

Section 7(b)(2)(A) requires BPA to assume that the loads of relevant DSIs are included in the 7(b)(2) Customers' "general requirements," a term defined by section 7(b)(4) of the Northwest Power Act as limited to electric power purchased from the Administrator under section 5(b) of the Act. Section 5(b) deals exclusively with firm power. In addition, sections 7(b)(2)(B) and 7(b)(2)(D) require that FBS and additional resources be assumed to serve the total General Requirements of the 7(b)(2) Customers.

The legislative history of the Northwest Power Act supports interpreting the statute to require 7(b)(2) Customers' firm power General Requirements in the 7(b)(2) Case to include all DSI Loads served by the Administrator. This includes DSI Loads that BPA does not plan or acquire resources to serve (*e.g.*, first quartile service) in the Program Case. In Appendix B, all four quartiles of DSI Loads were treated as firm when assigned to public agency customers in the 7(b)(2) Case.

8. Interpretation: Section 7(b)(2)(B) necessitates an examination of Program Case contracts in the determination of "Federal base system resources not obligated to other entities."

Discussion:

Section 7(b)(2)(B) provides that the Administrator is to assume that 7(b)(2) Customers were served by FBS resources "not obligated to other entities under contracts existing as of December 5, 1980, (during the remaining term of such contracts) excluding obligations to direct service industrial customer loads included in [Section 7(b)(2)(A)])." 16 U.S.C. § 839e(b)(2)(A). Unlike the assumption relating to DSI Loads served by public body and cooperative customers, section 7(b)(2)(B) requires BPA to make two factual determinations: (1) what the level of FBS resources is, and (2) what level of FBS resources is obligated for service to other entities, for all or a portion of the relevant Five-Year Period. The first determination is necessary because the FBS includes resources purchased by BPA under long-term contracts. Expiration of these contracts may cause a change in the size of the FBS during the relevant Five-Year Period.

The second determination concerns BPA power sales contracts or other obligations existing as of the effective date of the Northwest Power Act. Should these contractual obligations on FBS resources be removed through expiration of the relevant contracts, the size of FBS resources available to 7(b)(2) Customers would increase. Obligations on FBS resources include uses of power mandated by treaty, statute, or contracts entered into by BPA before December 5, 1980. The DSI obligations referenced in subsection 7(b)(2)(B) have since expired, rendering the "excluding obligations" language as no longer effective.

Any contract that BPA enters into subsequent to December 5, 1980, that exchanges FBS capacity for energy, exchanges seasonal FBS energy, or for the sale of FBS capacity with the return of the energy, will be assumed only if there is FBS surplus to 7(b)(2) Customer needs.

Therefore, the energy and revenue from such contracts will not be recognized in the 7(b)(2) Case unless, and to the extent that, there is surplus FBS in the 7(b)(2) Case.

9. Interpretation: Section 7(b)(2)(B) requires the allocation of resource pools to load pools in the Program Case to be reconsidered in the 7(b)(2) Case.

Discussion:

Section 7(b)(2)(B) states that the Administrator is to assume that "public body … customers were served … with Federal base system resources not obligated to other entities under contracts existing as of December 5, 1980 … excluding obligations to direct service industrial customer loads included in subparagraph (A) of this paragraph." 16 U.S.C. § 839e(b)(2)(B).

In the Program Case, section 7(b)(1) sets forth the sequence of allocating resource pools to load pools.

> Such rate or rates shall recover the costs of that portion of the Federal base system resources needed to supply such loads until such sales exceed the Federal base system resources. Thereafter, such rate or rates shall recover the cost of additional electric power as needed to supply such loads, first from the electric power acquired by the Administrator under section 5(c) and then from other resources.

The hierarchy established by section 7(b)(1), and complemented for other rates in sections 7(c)(1)(A) and 7(f), is that the FBS is to be used first to serve 7(b) loads, then for 7(c) loads and 7(f) loads until the FBS resources are exhausted. After the FBS resources are exhausted, BPA uses power acquired from the section 5(c) exchange to serve remaining loads. After using FBS and exchange resources, other resources acquired by BPA, also referred to as new resources, are used to serve remaining loads.

The Program Case uses this hierarchy to apply the resource pools, and their costs, to the load pools as the method of assigning resource costs to the load pools. However, in the 7(b)(2) Case, the size of the load pools will be different than in the Program Case. For example, section 5(c) exchange loads are removed from the 7(b)(2) Case load pool, thereby creating a smaller 7(b) load pool in the 7(b)(2) Case.

As a result of the different sizes of load pools in the two cases, the 7(b)(2) Case must construct its own separate allocation of resource pools to load pools. Furthermore, because of the explicit exclusion of the section 5(c) exchange in the 7(b)(2) Case, the exchange resource pool is eliminated. Lastly, because additional resources necessary in the 7(b)(2) Case are to be added through the 7(b)(2)(D) resource stack, the new resource resource pool is eliminated from the 7(b)(2) Case. All of these differences will result in different resource cost allocations than in the Program Case.

10. Interpretation: Section 7(b)(2)(C) requires the exclusion of all costs relating to the section 5(c) exchange, otherwise known as the Residential Exchange Program, from the 7(b)(2) Case. In addition, the loads and resources associated with the exchange will also be excluded from the 7(b)(2) Case.

Discussion:

Section 7(b)(2)(C) states that the Administrator is to assume that "no purchases or sales by the Administrator as provided in section 5(c) were made during such five-year period." 16 U.S.C. § 839e(b)(2)(C). This language unmistakably provides that the 7(b)(2) Case is to assume that the Residential Exchange Program is to be excluded from consideration. This includes all aspects of the exchange: the costs, the purchases and the sales. Further, any implementation costs included in the Program Case should be excluded from the 7(b)(2) Case, as should any costs associated with a settlement of residential exchange benefits.

11. Interpretation: Section 7(b)(2)(D) identifies three additional resource types assumed to be available to meet the 7(b)(2) Customers' General Requirements when FBS resources are exhausted. Type 1 are those resources not included in the FBS that are actually acquired by BPA from 7(b)(2) Customers in the Program Case. Type 2 are those resources owned or purchased by the 7(b)(2) Customers and not dedicated to load by public agencies or investor-owned utilities pursuant to section 5(b). These two types of resources are to be stacked in order of cost and then pulled from the stack to meet 7(b)(2) Customers' loads as needed, least expensive first. Type 3 resources are additional acquired resources not included in the FBS, which are priced at the average cost of all new resources acquired by BPA from non-7(b)(2) Customers during the Five-Year Period.

Discussion:

Section 7(b)(2)(D) describes the manner in which additional resources are assumed to be acquired to meet the 7(b)(2) Customers' loads when FBS resources are exhausted. Three types of additional resources are available in the 7(b)(2) Case. The first type of resource is described in section 7(b)(2)(D)(i) as being resources that were "purchased from such customers by the Administrator pursuant to section 6." These are the resources actually acquired by BPA from the 7(b)(2) Customers in the Program Case.

Conservation is defined in the Northwest Power Act as a resource. "'Resource' means … actual or planned load reduction resulting from direct application of a renewable energy resource by a consumer, or from a conservation measure." 16 U.S.C. § 839a(19). In addition, conservation is acquired by BPA under section 6. "The Administrator shall acquire such resources through conservation, implement all such conservation measures, and acquire such renewable resources which are installed by a residential or small commercial consumer to reduce load…" 16 U.S.C. § 839d(a)(1). Because conservation is acquired from 7(b)(2) Customers, it is a Type 1 resource. Such being the case, section 7(b)(2)(D) requires that any conservation being

acquired by BPA must be included in the resource stack as a non-FBS resource and available to serve 7(b)(2) Customer load to the extent it is needed and it is among the least expensive resources available. *See* Issue 4 *infra*.

Section 7(b)(2)(D)(ii) describes the second type of resource as those "not committed to load pursuant to section 5(b)." These are resources owned or purchased by the 7(b)(2) Customers that are not dedicated to load. Section 5(b)(1) of the Northwest Power Act provides:

> Whenever requested, the Administrator shall offer to sell to each requesting public body and cooperative entitled to preference and priority under the Bonneville Project Act of 1937 and to each requesting investor-owned utility electric power to meet the firm power load of such public body, cooperative or investor-owned utility in the Region to the extent that such firm power load exceeds—(A) the capability of such entity's firm peaking and energy resources used in the year prior to the enactment of this Act to serve its firm load in the region, and (B) such other resources as such entity determines, pursuant to contracts under this Act, will be used to serve its firm load in the region.

16 U.S.C. § 839c(b)(1). As noted in section 3(19) of the Northwest Power Act, the term "resource" includes "electric power." 16 U.S.C. § 839a(19). Because section 5(b) applies to requirements determinations for both preference customers and investor-owned utilities, section 7(b)(2)(D)(ii) precludes BPA from including resources owned or purchased by 7(b)(2) Customers in the 7(b)(2) Case resource stack if such resources are committed to load by preference customers or investor-owned utilities.

Together, sections 7(b)(2)(D)(i) and (ii) result in a list of resources which are assumed to be available to meet 7(b)(2) Customer loads. The remainder of section 7(b)(2)(D) outlines how this list of resources is to be used to serve the 7(b)(2) Customers' loads and describes the third type of resources available to meet 7(b)(2) Case loads. BPA is to assume for the 7(b)(2) Case that any required additional resources "were the least expensive resources owned or purchased by public bodies or cooperatives." This means that 7(b)(2)(D)(i) and (ii) resources are stacked in order of cost and pulled from that stack to meet 7(b)(2) Customers' loads in order of least to greatest cost. Should these resources be insufficient to satisfy the General Requirements of 7(b)(2) Customers, section 7(b)(2)(D) provides the assumption that "...any additional needed resources were obtained at the average cost of all other new resources acquired by the Administrator." This third resource type consists of the other new resources acquired by BPA in an amount required to meet the 7(b)(2) Customers' remaining loads, the cost of which is determined by the average cost of all new resources acquired by BPA from non-7(b)(2) Customers during the relevant Five-Year Period.

12. Interpretation: Section 7(b)(2)(E) requires an assessment of the Quantifiable Monetary Savings that are realized by public body financing of resources that are in the resource stack.

Discussion:

Section 7(b)(2)(E) states that the Administrator is to assume that "the quantifiable monetary savings, during such five-year period, to public body, cooperative and federal agency customers resulting from reduced public body and cooperative financing costs as applied to the total amount of resources, other than Federal base system resources, identified under subparagraph (D) of this paragraph, … were not achieved." 16 U.S.C. § 839e(b)(2)(E). The legislative history adds some clarification to this language. "Costs of new resources, either actual or hypothetical, constructed or acquired by the public bodies and cooperatives as necessary to meet these preference customer load requirements using the financing costs of such agencies that would have resulted if actions of the Administrator under Section 6 of the Bill were not achieved." S. Rep. No. 272, 96th Cong., 1st Sess., Appendix B at 58.

This subsection provides that the 7(b)(2) Case is to assume that the cost of resources in the subsection 7(b)(2)(D) resource stack is to exclude any 7(b)(2) Customer's financing benefits due to BPA's purchase of the output of the resource.

13. Interpretation: Section 7(b)(2)(E) requires an assessment of the value of Reserve Benefits acquired by BPA due to the Northwest Power Act.

Discussion:

Section 7(b)(2)(E) states that the Administrator is to assume that "the quantifiable monetary savings, during such five-year period, to public body, cooperative and federal agency customers resulting from … reserve benefits as a result of the Administrator's actions under this chapter were not achieved." 16 U.S.C. § 839e(b)(2)(E). Reserve Benefits result from BPA's restriction rights on loads provided for in power sales contracts. In the 7(b)(2) Case, these restriction rights are unavailable to BPA. Without the restriction rights, BPA would have to incur the costs of providing an equivalent amount of reserves from another source. This subsection provides that the 7(b)(2) Case is to assume that cost reductions attributable to Reserve Benefits are not achieved in the 7(b)(2) Case. Therefore, the 7(b)(2) Case revenue requirement is to assume the extra cost of procuring the reserves provided to the Program Case.