

UNITED STATES OF AMERICA
U.S. DEPARTMENT OF ENERGY
BEFORE THE
BONNEVILLE POWER ADMINISTRATION

Proposed Safety-Net Cost Recovery)
Adjustment Clause Adjustment to) BPA Docket No.: SN-03
2002 Wholesale Power Rates)

BRIEF ON EXCEPTIONS
OF
PNGC GROUP (PN)

Pacific Northwest Generating Cooperative, Blachly-Lane County Cooperative Electric Association, Central Electric Cooperative, Inc., Clearwater Power Company, Consumers Power, Inc., Coos-Curry Electric Cooperative, Inc., Douglas Electric Cooperative, Inc., Fall River Rural Electric Cooperative, Inc., Lane Electric Cooperative, Inc., Lost River Electric Cooperative, Inc., Northern Lights, Inc., Okanogan County Electric Cooperative, Inc., Raft River Rural Electric Cooperative, Inc., Salmon River Electric Cooperative, Inc., Umatilla Electric Cooperative Association, West Oregon Electric Cooperative, Inc.

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June 20, 2003

1 **TABLE OF CONTENTS**

2 Contents Page

3 I. INTRODUCTION.....1

4 II. STATEMENT OF THE PNGC GROUP’S CASE..... 1

5 III. ISSUES AND ARGUMENT.....3

6 A. Incorporation and Reassertion of Arguments Made in Prehearing Briefs and

7 Initial Brief.....3

8

9 B. The Draft Record of Decision is Unsupported by Data in the Record.....3

10

11 *Request for Direction by the Administrator to Produce Information*.....5

12

13 C. The Proposed Decisions in the Draft Record of Decision Belie Concern for

14 Retail Customers and the Economy of this Region.....5

15

16 1. BPA Should Not Misuse a “Tool of Last Resort” to Achieve Vast

17 Discretion to Raise Rates.....6

18

19 2. BPA Should Renounce Insistence on Making Customers Pay for the

20 Agency’s Own Prospective Failure to Solve its Controllable Costs

21 Problems..... 8

22

23 3. BPA Should Not Use Improved Hydrological, Market and Financial

24 Conditions as an Excuse to Make it *Easier* to Impose an SN CRAC

25 and Raise the Customers’ Rates by Making More Stringent its

26 Treasury Payment Risk Calculus.....10

27

28 IV. CONCLUSION.....11

29

30 EXHIBIT A.....13

1 **I. INTRODUCTION**

2 The PNGC Group submits this Brief on Exceptions pursuant to the *Special Rules*
3 *of Practice to Govern These Proceedings* (Special Rules) issued on March 31, 2003 (SN-
4 03-O-01 at p. 6), the *Procedures Governing Bonneville Power Administration Rate*
5 *Hearings*, 51 Fed. Reg. 7611 (1986) (Procedures), Rule 1010.13.

6 **II. STATEMENT OF THE PNGC GROUP’S CASE**

7 BPA does not need to impose any SN CRAC charge for FY 2004. The Draft
8 Record of Decision (“DROD”) itself makes that clear—BPA is at virtually no risk of
9 missing its next Treasury payment and cannot credibly justify recasting the issue as a
10 “remainder of the rate period” problem.

11 BPA has made good progress in cutting forecasted controllable costs, but much
12 more needs to be done. The Administrator’s new initiative for disclosing to customers on
13 a regular basis substantive information about agency costs and how well its spending is
14 tracking its budgets is both welcome and constructive. It will, however, have to be
15 followed up with lean budgets and actual spending controls.

16 If we could support any form or level of SN CRAC in FY 2004, we might
17 welcome the DROD’s constructive receptiveness to other customers’ proposals for
18 modifying and limiting an SN CRAC to facilitate cost control and avoid over-collection
19 of revenues under an SN CRAC surcharge.

20 PNGC Power, however, finds no basis in the DROD to alter its position. We
21 continue in the strongest terms to discourage the Administrator from imposing any SN
22 CRAC surcharge in FY 2004.

1 Moreover, there is much in the DROD that gives rise to heightened concern about
2 BPA's intentions. The DROD is materially different than BPA's Initial Proposal. These
3 differences and changed hydrological, market and financial circumstances affecting the
4 agency make it impossible to evaluate fully the implications of the many proposed
5 revisions to the GRSPs affecting the SN CRAC surcharge. The DROD nowhere states
6 the expected percentage surcharge for the proposed SN CRAC based on current
7 information. It is impossible to evaluate the assertion that BPA will have \$354 million in
8 FY 2006 ending reserves. This is a matter of serious concern because the Initial
9 Proposal contemplated recovering "zero net revenues" for the five year rate period,
10 implying BPA intended to use the SN CRAC to replenish its FY 2002 starting reserves.
11 Such an intention or effect would be an egregious abuse of the SN CRAC tool.

12 BPA voices concern at many places in the DROD for the economic welfare of the
13 Region, but the proposed decisions outlined in the DROD contradict that expression.
14 BPA demonstrates extraordinary zeal in interpreting the current GRSPs to vest the
15 Administrator with vast discretion to raise rates by using the *Safety Net* CRAC, a "tool of
16 last resort," when BPA is comfortably meeting its obligations and there is no emergency
17 in sight. BPA refuses to accept financial discipline or take responsibility for the
18 consequences of its own failure to meet cost cutting targets widely touted by senior
19 management. Instead, BPA misapplies the Regional Act's rate directives to shift this risk
20 to the Region, still mired in economic crisis. Perhaps most astonishingly, BPA strains to
21 conclude that its vastly improved hydrological, market and financial conditions now
22 should make it easier for the agency to impose an SN CRAC and to set it at a higher
23 level.

1 PNGC and its Members believe that the Administrator would inflict considerable
2 unnecessary and avoidable harm on the Region’s retail ratepayers by adopting as the
3 Final Record of Decision anything resembling this DROD.

4 **III. ISSUES AND ARGUMENT**

5 **A. Incorporation and Reassertion of Arguments Made in Prehearing Briefs**
6 **and Initial Brief.**

7
8 PNGC Power incorporates by this reference as if fully set forth here and reasserts
9 the arguments set forth or incorporated into its Prehearing Briefs (SN-03-P-CC-01, SN-
10 03-P-JC-01, and SN-03-P-PP-01) and its Initial Brief (SN-03-B-PN-01).

11 **B. The Draft Record of Decision is Unsupported by Data in the Record.**

12 The Draft Record of Decision (“DROD”) does not contain any analysis, studies or
13 technical documentation to support the proposal in the DROD. For example, there is no
14 support for the assertions that imposing an average 5% overall rate increase over FY
15 2003 rate levels for the next three fiscal years, *see* SN-03-A-01, page 2.7-13, will
16 produce an 80% TPP or an ending reserves balance in FY 2006 of \$354 million. SN-03-
17 A-01, page 2.8-18. While BPA and the customers now know that its revenue forecasts
18 in the Initial Proposal are substantially understated, the DROD contains no current
19 forecasted revenue base against which to compare calculated SN CRAC revenues and
20 determine the scale of the increase.

21 BPA has, among other things, retreated materially from its Initial Proposal, *e.g.*,
22 the decision to raise the threshold of acceptable Treasury payment probability, SN-03-A-
23 01, pages 2.7-8 to 2.7-14, accepted some GRSP revisions proposed by other customer
24 groups, and wasted the customers’ time and resources initiating extensive discussions and
25 generating information concerning the use of additional available cash tools which it now

1 refuses to employ to avoid a rate increase. The customers can no longer look to studies
2 and model runs provided with the Initial Proposal or during the course of the rate case to
3 evaluate which outcomes the revised GRSPs may produce.

4 Yet, simultaneously with the release of the DROD earlier this week, BPA account
5 executives were able to provide some customers with a table entitled “Expected Power
6 Rate Adjustments over May 2000 Base Rates FY 2002-2006 with SN CRAC” that
7 included specific SN CRAC figures—14% for FY 2004, 16% for FY 2005, and 15% for
8 FY 2006. However, the DROD does not even contain such a chart and specifies no SN
9 CRAC rate. Annexed to this Brief as Exhibit A is a copy of this chart as provided to
10 PNGC Power.

11 Given the lack of data and analysis supplied by BPA and the short amount of time
12 from their publication late on June 16 to the deadline for this brief on June 20, 2003, it is
13 impossible to make a technical analysis to verify what the real SN CRAC rate increases
14 are, what the TPP is, what the end of period reserves level is, whether BPA’s data and
15 assumptions are appropriate, or what other mischief may ensue from the GRSPs set forth
16 in the Appendix to the DROD.

17 It is virtually certain that BPA’s customers will have to adjust their retail rates in
18 response to BPA’s SN CRAC rate decisions. Those rates will have to be communicated
19 and justified to retail customers, who then may have to make abrupt personal and
20 business decisions about their power use.

21 BPA has apparently interpreted the language of the current GRSPs, WP-02-A-09,
22 Appendix, page 26, to permit it to conduct studies and prepare documentation outside the
23 process of this rate proceeding but to supply it to the FERC when BPA seeks review and

1 confirmation of the SN CRAC rate. This is unlike past rate cases when the agency was
2 updating data and studies thoroughly examined in the proceeding and not materially
3 altered for FERC’s consumption. Here, BPA has refused to provide the customers a
4 supplemental proposal setting forth materially changed facts and analysis. Apparently,
5 BPA is either affirmatively concealing what it knows about the data and implications of
6 its proposal, or plans to make the facts and analysis on which its decision rests *after* it
7 concludes what the decision will be.

8 This approach is an abuse of the rate case process. The process that BPA is
9 providing its customers is inadequate, improper and lacking in fundamental fairness. *We*
10 *request the Administrator immediately to direct (1) the inclusion of the rate adjustment*
11 *chart (Exhibit A) in the administrative record, (2) that staff and counsel to make*
12 *available promptly the underlying assumptions, data and computer model runs that*
13 *produce these conclusions, (3) that the customers be afforded a reasonable opportunity*
14 *to test these assumptions, data, model runs and conclusions, and (4) that the rate case*
15 *schedule be modified to permit customers a reasonable opportunity to respond.*

16 **C. The Proposed Decisions in the Draft Record of Decision Belie Concern**
17 **for Retail Customers and the Economy of this Region.**
18

19 At many places in the DROD, BPA says that it is concerned about the welfare of
20 the Pacific Northwest and its economy. Yet throughout the DROD the agency employs
21 its familiar rhetoric about the inarguable, *viz.*, its obligations to recover its costs, pay
22 Treasury on time, and make “prudent” and “businesslike” decisions, to bury any
23 suggestion that it might decide to do something really helpful to retail customers who
24 need rate relief *now*.

1 The Region’s retail customers will not rejoice that BPA’s proposed SN CRAC for
2 FY 2004 is only 14% instead of 30% or more, or that overall BPA rates will increase by
3 only 5% instead of 15%. They will not fail to notice that the LB CRAC will drive up
4 rates by nearly 11% only six months later, and that BPA forecasts no rate relief for the
5 balance of this rate period.

6 **1. BPA Should Not Misuse a “Tool of Last Resort” to Achieve Vast**
7 **Discretion to Raise Rates.**

8
9 BPA on the one hand acknowledges that “the SN CRAC was intended to be a tool
10 of last resort,” SN-03-A-01, pages 2.1-10, and “was designed to recover from bad
11 financial results because of the triggering potential based on actually *missing* a payment
12 to [T]reasury or [an]other creditor.” SN-03-A-1, page 2.7-14, *quoting* Keep, *et al.*, SN-
13 03-E-BPA-11, page 31 (emphasis in original and quoted testimony).

14 On the other hand, BPA repeatedly asserts that “there are no limits to the types of
15 BPA costs that the SN CRAC can recover.” SN-03-A-01, pages 2.1-10 and 2.1-16. And,
16 there is no need for either “extraordinary or catastrophic events,” SN-03-A-01, page 2.1-
17 10, or “emergency conditions” to occur for BPA to impose an SN CRAC surcharge. SN-
18 03-A-01, page 2.1-11. And further, BPA can use the SN CRAC to recover “potentially
19 very large amounts of potential revenues.” *Id.*

20 BPA says that “[t]his proceeding presents a somewhat unique rate decision for the
21 Administrator.” SN-03-A-01, page 2.7-9. It characterizes existing GRSP language as
22 “expansive” and gives the Administrator “broad discretion” to do, essentially, just what
23 the agency wants to do in this case. SN-03-A-01, page 2.7-10.

24 Further, “[b]ecause the Administrator is given broad discretion and can weigh a
25 variety of factors . . . , the decisions here reflect the unique set of circumstances The

1 decision . . . should not be seen as creating any precedent The decisions reflected
2 here evidence a careful weighing of the particular set of factors”

3 To top things off, the DROD repeats Regional Act legal criteria (“adequate,
4 efficient, economical, and reliable power supply” and “sound business principles”) to
5 justify the decisions. However, applied with an honest concern for the welfare of the
6 Region’s retail ratepayers and even a passing acknowledgement that the real world does
7 not allow anyone, even BPA, to eliminate all risk, these criteria actually require that no
8 SN CRAC be imposed in FY 2004: (1) an unnecessary rate increase is inconsistent with
9 an economical power supply, and (2) sound business principles do not call for raising
10 prices when doing so will drive customers out of business.

11 As remolded by the agency, the SN CRAC does not resemble the tool that BPA’s
12 customers crafted to demonstrate loyalty, lend financial strength, and help the agency
13 overcome the consequences of its errors (vast and inexcusable underestimation of
14 preference customer load) and bad conduct (illegal sales to DSI customers at subsidized
15 rates; “litigation penalty” payments offered to certain IOUs).

16 When the negotiations and settlement of the Supplemental WP-02 proceedings
17 took place, the Region’s economy and the welfare of retail power customers were in a far
18 different condition, and the customers had some leeway to extend flexibility to BPA.
19 And, BPA has experienced some very challenging financial conditions, particularly in
20 late 2002 and very early 2003.

21 But circumstances have improved dramatically for the agency. The chance that
22 BPA will miss its next Treasury payment is virtually nil. Instead of backing off its
23 aggressive insistence on imposing a multiyear SN CRAC surcharge and permitting retail

1 customers to experience some relief from massive and relentless BPA rate increases,
2 BPA pretends that it still needs a rate increase in FY 2004. None of those established
3 central principles governing BPA's ratemaking, individually or collectively, compels the
4 outcomes set forth in the DROD. The nature and features of the proposed SN CRAC
5 surcharge ensue because BPA frames the issues with an eye to the result it wants. The
6 underlying drivers are BPA's attempt to pressure public power into anteing up more
7 consideration to settle pending litigation with Investor Owned Utilities, *see* SN-03-A-01,
8 page 2.1-16, and BPA's (or DOE's) mistaken political calculus to avoid at all costs a rate
9 increase in an election year.

10 **2. BPA Should Renounce Insistence on Making Customers Pay for**
11 **the Agency's Own Prospective Failure to Solve its Controllable**
12 **Costs Problems.**
13

14 BPA's customers unanimously appealed to the agency both within and outside
15 this proceeding to reduce its spending and account prospectively in a regular and
16 meaningful fashion for its costs, revenues and adherence to budgets. The Administrator
17 accepted this appeal and has announced both cuts in forecasted controllable costs and the
18 intention to provide meaningful financial information to customers on timely basis. SN-
19 03-A-01, page 2.1-18. However, disclosure of costs, customer review and opportunities
20 for input are no substitute for *control* of costs. The agency has much more work to do.

21 The Western Public Agencies Group and other customer groups have encouraged
22 the Administrator to place limits on an SN CRAC by means of cost and revenue caps and
23 to afford a remedy for over-collection of revenues under an SN CRAC, and the DROD
24 indicates the Administrator is receptive to a number of these proposals.

1 Nonetheless, the DROD persists in laying at the doorstep of the customers the risk
2 that BPA will fail or refuse to control its internal spending. Unless cost cuts are
3 identified “with a high level of certainty,” BPA plans to use the SN CRAC to charge
4 customers for these costs regardless of whether savings are realized. SN-03-A-01, page
5 2.1-14. BPA insists that it is not required to cut costs in order to avoid a rate increase,
6 and that the customers must provide a financial remedy in the event the agency does not
7 cut its costs. SN-03-A-01, page 2.1-18. It justifies this attitude by pointing to the rate
8 directive that requires BPA rates to cover its system costs. *Id.*

9 To contend that the Regional Power Act’s rate directive to recover its system
10 costs prevents BPA from setting rates in anticipation of reducing its controllable costs is
11 to misapply and abuse that directive. This interpretation of the rate directive seeks to
12 justify a practice that is irrational, inefficient, and anything but businesslike.

13 BPA’s most senior management has made strong statements in many forums
14 preceding and during this rate case about its intention to reduce controllable costs to
15 levels at and below FY 2001 actual levels. These statements are important and welcome.
16 Refusing to set rates in contemplation that this reasonable, but not terribly aggressive,
17 goal will be achieved and on a timely basis gives license to BPA middle management
18 responsible for hiring and spending to ignore it.

19 The level of spending on BPA’s controllable internal costs is a matter within the
20 power of BPA alone to manage. The risk that BPA will fail to achieve identifiable,
21 controllable cost reductions is one that must rest with BPA and be its responsibility to
22 manage. Not even the most egregious mismanagement of staff and internal spending
23 could foreseeably result in cost reduction targets being missed to such a degree that BPA

1 would risk missing a Treasury payment. The rate directive to cover system costs cannot
2 be misused to sanction business as usual. The Administrator need not, and should not,
3 fear managing the risk that cost and spending reductions might not be realized. Unless he
4 does accept that risk and order that his cost reduction goals be accomplished, they will
5 not succeed and customer confidence and trust will diminish further.

6 **3. BPA Should Not Use Improved Hydrological, Market and**
7 **Financial Conditions as an Excuse to Make it *Easier* to Impose an**
8 **SN CRAC and Raise the Customers' Rates by Making More**
9 **Stringent its Treasury Payment Risk Calculus.**

10
11 One of the most surprising and disappointing aspects of the DROD is the
12 agency's proposed retreat from its Initial Proposal's three financial standards (TPP, TRP
13 and zero net revenues) for setting the SN CRAC surcharge. SN-03-A-01, page 2.7-14.
14 PNGC did not endorse the Initial Proposal's revised standards, but viewed with favor a
15 moderate and responsible alteration of BPA's Treasury payment risk calculus to reduce
16 the likelihood of an SN CRAC trigger and the rate of any SN CRAC surcharge.

17 The DROD is so lacking in evidentiary support that there is no way to evaluate
18 how BPA's latest revised Treasury payment risk calculus would actually operate. The
19 only thing that we do know is that this revision is specifically intended to make it easier
20 for BPA to take more money from the Region's retail customers at the worst time.

21 The DROD cites not a single example of improvement in the region's
22 unemployment rate, employee compensation levels, costs of doing business, or business
23 failure rate. There is not a shred of evidence of any improvement in employment or the
24 economy in the record of this case.

25 BPA admits that dramatic improvements in its own financial condition have
26 occurred. "[S]ubstantial cost reductions, cash improvement and improved secondary

1 revenue now makes the likelihood of paying the [T]reasury in full in FY 2003 close to
2 100 percent.” SN-03-A-01, page 2.7-8. Yet, the authors of the DROD devote several
3 pages of text to justifying making it *easier* for BPA to impose an SN CRAC, and easier
4 for BPA to impose a *higher* SN CRAC, while the Region’s economy continues to suffer.

5 This logic is perverse. The improved conditions affecting BPA render less, not
6 more, risky the Initial Proposal’s treatment of Treasury payment probability. The
7 customers have urged the agency time and time again to avoid an SN CRAC for FY
8 2004. It is obvious that no SN CRAC can be justified for FY 2004 unless BPA persists in
9 recasting the issue as a “balance of the rate period” problem, and even then the agency
10 has ample means to set an FY 2004 SN CRAC at zero.

11 While the Region’s economy languishes and unemployment remains high, BPA
12 wants to make it easier for itself to raise rates. It even resorts to employing vastly
13 improved hydrological, market and financial conditions as justifications for raising rates.
14 The Region deserves better than this sophistry. BPA can afford a zero SN CRAC in FY
15 2004, and it should ask no more of, and shift no more risk to, the Region’s retail
16 ratepayers.

17 **IV. CONCLUSION**

18 For the reasons stated in this Brief, PNGC Power and its fifteen Members
19 respectfully request, and urge, the Administrator to impose no SN CRAC surcharge
20 during FY 2004 and to direct the agency to undertake a fundamental rethinking of its
21 attitude toward risk and toward the Region’s retail customers. The agency is now so
22 profoundly risk averse, that it is about to transfer the burden of risk to the regions retail
23 consumers and inflict significant harm through imposition of its proposed SN CRAC

1 surcharge. Further, the imposition of the SN CRAC may be done without and adequate or
2 complete record and apparently in an effort to expand the Administrator's discretion
3 while limiting any review or criticism of the approach.

4 The Administrator still has a chance to demonstrate that BPA is not really blind or
5 indifferent to the economic woes of the Region. More rhetoric in the Final ROD like that
6 in the DROD will not suffice. The agency can move beyond its own self-interest and do
7 what the Region so obviously needs. Without strong measures, such as eliminating an
8 unneeded SN CRAC, to spur an economic recovery in the near term, the agency's long-
9 term welfare may not be of much interest to the customers for some time. BPA needs to
10 do the right thing now, move beyond this rate case, and take steps to foster an
11 environment of trust, confidence and collaboration with its customers. It would be wrong
12 to forego an opportunity to forge a long- term relationship between BPA and its
13 customers that can succeed in retaining the benefits of the FCRPS for the Region.

14

15 Respectfully submitted this 20th day of June, 2003.

16

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R. ERICK JOHNSON PC

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By: /s/ R. Erick Johnson

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R. Erick Johnson

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EXHIBIT A

[Exhibit A is a one page PowerPoint file distributed
to PNGC Power staff on Monday, June 16, 2003, by BPA staff.]