Week in Summary

[6] BPA Won't Revise Its Load Forecast Despite Planned SN CRAC

BPA does not intend to revise its load forecasts or revenue estimates even though it is planning to raise rates to all-time highs, the agency confirmed last week. BPA said previous increases have resulted in little variation. The agency doesn't expect much price elasticity of demand, even with higher rates, in part because so much of its power is sold under take-or-pay contracts. In addition, such a study would cost as much as $40,000 at a time the agency is watching its costs. ***BPA plans for no elasticity at [12].***

[12] BPA Won't Revise Load Forecast Despite SN CRAC ■ *from [6]*

Even though it is preparing a substantial increase in rates, BPA is not revising the load forecasts it adopted in 2002, the agency said last week. Nor does it anticipate that the percentage increase in revenue it will see will be any less than the percentage of the rate increase.

Barney Keep, BPA manager of power products, prices and rate making, said the agency decided against doing a study of the economic impact of its proposed rate increase under the safety net cost recovery adjustment clause because it would cost $20,000 to $40,000 at a time the agency is trying to contain costs. Some constituents, including at least one member of the congressional delegation, have asked BPA whether it is investigating the price elasticity of demand under the proposed SN CRAC.

Price elasticity of demand is a measure of the responsiveness of demand for a product following a change in its price. The method can be used to project future demand for power, as well as to estimate how much economic impact a rate increase may have. Because the economy is already strained, some BPA customers wonder if another rate increase could yield diminishing returns.

On the financial side, Keep said BPA believes if it raises rates a net of 15 percent, it will bring in 15 percent more revenue. "There are no guarantees, but that is our assumption." He said part of the agency's confidence is based on the fact that well over two-thirds of its load--nearly 5000 MW--is being served under take-or-pay contracts. Only about 2200 MW is provided through full service contracts, under which BPA would sell less power if the customer's load declined. Moreover, the difference could still be sold on the open market as surplus power, Keep pointed out. The shift of risk away from BPA to its customers was one of the main principles adopted in the 1996 Regional Review.

As for the load forecast, Keep pointed out that since the beginning of the rate period, loads have varied little, despite rate increases under both the load-based and financial-based CRACs. "We have seen load vary within a 1 percent range," not enough to incline the agency to revise its load forecast for the five-year rate period.

"Whether it's because of conservation, the downturn in the economy, the mild winter" or some other factor, Keep could not say. "We have been tracking this, but there is not enough difference to revise the forecast."

Keep emphasized he was talking only of public agency load; BPA has revised downward its projection of direct service industry load--from 1500 MW in the last rate case to less than 100 MW in the studies being prepared for the SN CRAC.

In the 1990s, when BPA's forecasting group was much larger, elasticity studies were prepared. "We saw some price effects," Keep allowed, "but you were not getting a lot of elasticity response. And we figured relatively speaking, it was still cheap." At the time, BPA's rates were generally well below market.

Keep said he is fully aware that a lot of customers are concerned. "We are about to hit a step function, in which whole industries would shut down, rather than backing off a shift," he said. "Maybe we will cross the line and see things shut down. We don't know. We are going into new territory here because rates have never been this high."

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That new territory could mean rates as high as 40 mills/KWh, said Ken Canon, executive director of Industrial Customers of Northwest Utilities. "From Bonneville you get: 'These are just customers whining; they can take it and move on,'" Canon said. "That may be true when the rates are going from 22 mills to 23 mills, or 18 mills to 22 mills. But this is 32 mills going potentially to 40 mills in a crappy economy.

"You've wiped out one class of customers--the aluminum smelters--and are now looking at the next tier of manufacturing," he added. "There are wide-ranging impacts." Canon said that when PGE raised its commercial/industrial rates 53 percent in 2002, it saw a load reduction of 10 percent to 12 percent.

At Grays Harbor PUD, rates are pushing the price elasticity theory to its limits. General Manager Rick Lovely said the PUD realized no revenue increase at all from its last rate hike. Under a common rule of thumb, every increase of 10 percent is supposed to yield a load reduction of between 1 percent and 1.5 percent, he said. For the last rate increase, the PUD expected a revenue drop of $3 million; the actual drop was closer to $11 million. Lovely said he might now consider a surcharge, but worries some customers might just stop using electricity altogether. He has even pondered *lowering* rates in an effort to *increase* revenue.

BPA's Keep said the variety of ways utilities deal with increases complicates the elasticity analysis. "It's hard to measure" the impact of an increase. Many customers don't pass on increases in full; some eat the increase for a few months, while others move more quickly or adopt other rate designs, he said.

Customers often "give you the impression their total costs are driven by Bonneville rates, but that is not the case. Normally about half the costs are the customer's own internal and distribution costs," Keep said. "It's hard to sort out what they are responding to. Customers don't even pass on the monthly or seasonal" changes that are built into BPA's actual rates. That makes it "hard for us to do an assessment of what happens to retail loads based on our price changes," he said ***[Ben Tansey].***