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REBUTTAL TESTIMONY OF

MARK H. EBBERTS, BYRON G. KEEP, WILLIAM J. DOUBLEDAY,  
HARRY W. CLARK, AND RODNEY E. BOLING

Witnesses for Bonneville Power Administration

**SUBJECT: Rebuttal Testimony for Rate Directives**

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6 **SUBJECT: REBUTTAL TESTIMONY FOR RATE DIRECTIVES**

7 **Section 1. Introduction and Purpose of Testimony**

8 *Q. Please state your names and qualifications.*

9 A. My name is Mark Ebberts and my qualifications are contained in WP-02-Q-BPA-18.

10 A. My name is Byron G. Keep and my qualifications are contained in WP-02-Q-BPA-34.

11 A. My name is William J. Doubleday and my qualifications are contained in  
12 WP-02-Q-BPA-17.

13 A. My name is Harry W. Clark and my qualifications are contained in WP-02-Q-BPA-12.

14 A. My name is Rodney E. Boling and my qualifications are contained in WP-02-Q-BPA-07.

15 *Q. What is the purpose of your testimony?*

16 A. The purpose of this testimony is to respond to the arguments raised by the rate case  
17 parties regarding the Pacific Northwest Electric Power Planning and Conservation Act's  
18 (Northwest Power Act) rate directives.

19 *Q. How is your testimony organized?*

20 A. This testimony is organized in five sections. Section 1 outlines the purpose of our  
21 testimony. Section 2 addresses the parties' arguments regarding the rate directives  
22 generally. Section 3 addresses the parties' arguments regarding the section 7(b)(2) rate  
23 test. Section 4 addresses the parties' arguments regarding the determination of average  
24 system costs (ASC). Section 5 addresses the parties' arguments regarding section 7(c)(2)  
25 of the Northwest Power Act.  
26

1 **Section 2. Rate Directives**

2 *Q. Please summarize the Direct Service Industrial Customers' (DSIs) arguments regarding*  
3 *the Northwest Power Act's rate directives.*

4 A. The DSIs argue that Bonneville Power Administration (BPA) has published nothing in its  
5 2002 Supplemental Power Rate Proposal (Supplemental Proposal) to show that its  
6 proposed rates comport with the statutory requirements of section 7 of the Northwest  
7 Power Act. Schoenbeck and Bliven, WP-02-E-DS-06, at 3. The DSIs argue that because  
8 system augmentation costs are Federal Base System (FBS) costs which BPA fully  
9 expects to incur under its most-likely view of the future, they impact the implementation  
10 of the rate directives. *Id.* at 4. The DSIs argue that the fact that BPA may be somewhat  
11 uncertain on the precise level of these previously unanticipated costs provides no basis  
12 for simply ignoring them in connection with the rate directives because all of BPA's  
13 revenue requirement is based on forecasts which always contain uncertainty in their  
14 accuracy. *Id.* The DSIs also argue that while BPA has determined that its adjustable  
15 rates need to be increased by at least 22 percent above the May Proposal, and perhaps as  
16 much as 10 times that amount, BPA has not performed any of the rate studies to check or  
17 to demonstrate compliance with the rate directives. *Id.* Finally, the DSIs argue that BPA  
18 should redo the section 7(b)(2) rate test, the section 7(c)(2) linkage of the Priority Firm  
19 Power (PF) and Industrial Firm Power (IP) rates, and the section 7(c)(2) floor rate test  
20 using the best available cost, revenue and market data, and revisit and modify as  
21 necessary every aspect of BPA final studies in May 2000. *Id.* at 5.

22 *Q. Do you agree with the DSIs' arguments?*

23 A. No. First, BPA has developed a tremendous volume of material in the WP-02 rate case  
24 record, including its 2002 Initial Power Rate Proposal (May Proposal), 2002 Amended  
25 Power Rate Proposal (Amended Proposal), and Supplemental Proposal, which  
26 demonstrate that BPA's proposed rates comport with the statutory requirements of

1 section 7 of the Northwest Power Act. The portion of the rate case record that relates  
2 only to BPA's Supplemental Proposal is merely one part of the entire administrative  
3 record. The DSIs' claim that the limited record of the Supplemental Proposal should be  
4 the only part of the record to be reviewed in determining BPA's compliance with rate  
5 directives is misplaced.

6 The DSIs argue that system augmentation costs are FBS costs that BPA expects to  
7 incur and therefore impact the implementation of the rate directives. Schoenbeck and  
8 Bliven, WP-02-E-DS-06, at 4. The DSIs' position, essentially, is that where there are  
9 changes in BPA's costs, BPA must redo its rate case studies. This position is  
10 unreasonable for the reasons stated in greater detail below. In addition, the DSIs have  
11 simply dismissed BPA's policy approach, as stated in both its Amended and  
12 Supplemental Proposals, for developing rates in the current volatile power market. *See*  
13 *Burns, et al.*, WP-02-E-BPA-62; *Burns, et al.*, WP-02-E-BPA-70. BPA's policy  
14 witnesses concluded that "BPA does not believe redoing all of the forecasts is the best  
15 policy choice to address current market volatility." *Burns, et al.*, WP-02-E-BPA-62(E1).  
16 These reasons will not be reiterated here. Notably, however, the DSIs make no effort to  
17 demonstrate that their proposal would accomplish the policy objectives that BPA has  
18 consistently advocated, or to explain why those policy goals are no longer valid.

19 Furthermore, the DSIs openly acknowledge that BPA is uncertain of the precise  
20 level of the previously unanticipated costs that have appeared since BPA's May Proposal.  
21 Schoenbeck and Bliven, WP-02-E-DS-06, at 4. Although it is true that BPA's revenue  
22 requirement is based on forecasts which always contain some uncertainty in their  
23 accuracy, the uncertainty BPA has encountered historically in developing its prior  
24 wholesale power rates is dramatically different from the uncertainty BPA faces in  
25 developing its current rates. For example, in BPA's 1996 rate case, BPA forecasted that  
26 it could serve loads with existing resources plus a small amount of balancing purchases

1 that could be purchased in a relatively stable power market. In contrast, BPA's load  
2 obligation for the Fiscal Year 2002-2006 rate period far exceeds existing resources and  
3 BPA now faces the likelihood of purchasing as much as 3,305 average megawatts (aMW)  
4 of system augmentation in addition to balancing purchases. In a volatile power market,  
5 the cost of these purchases could be subject to extreme variations. These dramatic  
6 differences support BPA's current risk mitigation approach which deals with the problem  
7 in a flexible manner. The flexibility inherent in the design of the risk mitigation package  
8 avoids a great deal of the risk of underrecovery or overrecovery that could result from  
9 locking in highly uncertain and variable augmentation costs based on a forecast  
10 developed prior to the rate period.

11 *Q. The DSIs also argue that BPA has determined that its adjustable rates need to be*  
12 *increased by at least 22 percent above the May Proposal, but BPA has not performed any*  
13 *of the rate studies to check or to demonstrate compliance with the rate directives.*  
14 *Schoenbeck and Bliven, WP-02-E-DS-06, at 4. Please respond.*

15 *A. The DSIs ignore the existing record of this proceeding. BPA has performed all of its rate*  
16 *studies in developing BPA's proposed rates. See, e.g., 2002 Wholesale Power Rate*  
17 *Development Study, WP-02-FS-BPA-05; 2002 Section 7(b)(2) Rate Test Study,*  
18 *WP-02-FS-BPA-06. These studies demonstrate compliance with BPA's rate directives.*  
19 *In addition, the policy testimony in BPA's Amended and Supplemental Proposals notes*  
20 *how BPA identified a risk mitigation problem in BPA's May Proposal that could best be*  
21 *addressed through the revision of BPA's risk mitigation tools. See Burns, et al.,*  
22 *WP-02-E-BPA-62; Burns, et al., WP-02-E-BPA-70. BPA clearly has not ignored the*  
23 *Northwest Power Act's rate directives. As noted above, BPA's Amended and*  
24 *Supplemental Proposals must be viewed in conjunction with the foundation of BPA's*  
25 *May Proposal, which addresses BPA's compliance with the directives in great detail.*  
26 *The latter stages of this proceeding have dealt specifically with unprecedented market*

1 conditions, characterized by enormous volatility and extremely high prices. From a  
2 ratemaking perspective, it is prudent to deal with these problems through flexible risk  
3 mitigation tools, rather than subjecting consumers to cost allocations and rate increases  
4 that are predicated, in large part, on future events that are extremely volatile.

5 *Q. The DSIs argue that BPA should redo the section 7(b)(2) rate test, the section 7(c)(2)*  
6 *IP-PF link, and the section 7(c)(2) floor rate test using the best available data, but the*  
7 *DSIs do not appear to argue that BPA should conduct an entirely new rate case.*  
8 *Schoenbeck and Bliven, WP-02-E-DS-06, at 5. Please respond.*

9 *A. The DSIs' suggestion that BPA should "redo" only the ratemaking elements that might*  
10 *contribute to the development of a more favorable IP rate is inappropriate. If BPA were*  
11 *to accept the DSIs' proposal, BPA's studies would not be the only elements of rate*  
12 *development reviewed by BPA. There are hundreds of issues in every BPA rate case that*  
13 *must be decided by the agency, including policy, technical, and legal issues. If BPA*  
14 *were to revise studies for the reasons proposed by the DSIs, BPA would also properly*  
15 *review other issues that could significantly affect the results of those studies. For*  
16 *example, BPA would likely review the issue of the DSI margin. Similarly, BPA would*  
17 *review the manner in which the costs of the section 7(b)(2) rate test are allocated to other*  
18 *power rates, including the DSIs. BPA would likely review the manner in which market*  
19 *costs are reflected in the Industrial Firm Power Targeted Adjustment Charge rate, and so*  
20 *on. The DSIs' limited approach would not be a proper way to develop rates. Instead,*  
21 *rates would need to be developed from the ground up. BPA's approach of developing*  
22 *flexible risk mitigation tools avoids this complication. The base rates are not changed,*  
23 *and the risk mitigation package is designed to make sure that customers are assigned an*  
24 *appropriate share of actual augmentation costs. This concept is reflected in BPA's policy*  
25 *testimony, which concludes that the most appropriate method for addressing existing*  
26 *market uncertainties is through BPA's risk mitigation approach.*

1           In addition, the incomplete nature of the DSIs' proposal would make its adoption  
2 highly problematic from a practical standpoint. In developing an initial rate proposal,  
3 more time is needed by BPA staff to develop the proposal prior to beginning the formal  
4 hearing portion itself. For example, BPA staff's work on BPA's initial WP-02 rate  
5 proposal took approximately 10 months. After preliminary staff work had been  
6 completed, BPA conducted informal workshops with interested parties. These informal  
7 workshops provide BPA with input from customers and others to shape BPA's initial  
8 proposal. The formal hearing portion of the WP-02 rate development took approximately  
9 nine months. Thus, it would not be surprising if a new general wholesale power rate case  
10 to consider the DSIs' proposal took as long as 19 months. In order to implement new  
11 power sales contracts, however, BPA must file its current proposed rates with the Federal  
12 Energy Regulatory Commission no later than the end of June 2001. BPA cannot simply  
13 extend its current rates because those rates do not contain some of the new rate schedules  
14 needed to implement BPA's new subscription contracts (*e.g.*, the RL and PF Exchange  
15 Subscription rates). Moreover, there has been no demonstration that BPA's current rates  
16 would fully recover BPA's costs given current market conditions. Due to the incomplete  
17 nature of the DSIs' proposal, BPA would not have sufficient opportunity to develop an  
18 acceptable proposal along the lines envisioned by the DSIs.

19           Finally, the rate development process must take into account the fact that BPA  
20 cannot continually revise a rate proposal to reflect new conditions. The DSIs' proposal  
21 ignores this issue by proposing that BPA incorporate certain assumptions regarding loads  
22 and market prices that could change drastically within a few months and thereby  
23 undermine the basis for the rates.

24           The DSIs' arguments that BPA should redo the section 7(b)(2) rate test, the  
25 section 7(c)(2) linkage of the PF and IP rates, and the section 7(c)(2) floor rate test are  
26 addressed individually below.

1 **Section 3. Section 7(b)(2) Rate Test**

2 *Q. Please summarize the DSIs' arguments regarding the section 7(b)(2) rate test.*

3 A. The DSIs argue that BPA should redo the section 7(b)(2) rate test. Schoenbeck and  
4 Bliven, WP-02-E-DS-06, at 5. The DSIs state that the public agency loads to be placed  
5 on BPA exceeded BPA's May estimate by 1,472 aMW and that this change in public  
6 agency load, combined with the additional resource augmentation required to serve this  
7 load, necessitates recomputing load and resource balances and performing the 7(b)(2) rate  
8 test to ensure compliance with the Northwest Power Act's rate directives. *Id.* The DSIs  
9 argue that without completing the 7(b)(2) rate test, BPA has no way of knowing whether  
10 the PF rate determined in this proceeding is in compliance with federal law. *Id.*

11 *Q. Do you agree with the DSIs' arguments regarding the section 7(b)(2) rate test?*

12 A. No. The DSIs' argument has been addressed in BPA's policy testimony, which explains  
13 why BPA is proceeding with changes in its risk mitigation strategy instead of conducting  
14 a completely new rate case. *See* Burns, *et al.*, WP-02-E-BPA-62; Burns, *et al.*,  
15 WP-02-E-BPA-70. In addition, as noted above, BPA's proposed rates comport with  
16 BPA's rate directives; BPA has developed an appropriate policy approach to address the  
17 unprecedented volatility in the electric power market (*see* Burns, *et al.*,  
18 WP-02-E-BPA-62; Burns, *et al.*, WP-02-E-BPA-70); BPA is facing unprecedented  
19 uncertainty in the development of its rates; BPA has properly performed all of its rate  
20 studies; assuming that BPA were to revise its rate studies, BPA would also review all  
21 other policy, technical, and legal issues regarding the development of rates; BPA lacks  
22 the time necessary to conduct a completely new rate case; and there must be some end to  
23 the incorporation of changed conditions in rates in order to conclude the rate  
24 development process. These reasons argue against conducting a new section 7(b)(2)  
25 study, among other rate studies, which essentially would require BPA to conduct a new  
26 rate case.

1 Q. Do the DSIs raise any other arguments regarding the section 7(b)(2) rate test?

2 A. Yes. The DSIs state that in BPA's May Proposal, net Residential Exchange Program  
3 (REP) benefits for the five-year rate period were about \$240 million, after the  
4 section 7(b)(2) rate test determined that there was a 3.4 mills/kWh trigger. Schoenbeck  
5 and Bliven, WP-02-E-DS-06, at 6. The DSIs state that in the Subscription Step of the  
6 rate design process, BPA converted these calculated REP benefits into 1,000 aMW of  
7 power sales plus \$349 million in financial benefits. *Id.* The DSIs state that, given the  
8 steep increases in BPA's resource costs due to its system augmentation which BPA has  
9 defined as FBS costs, it is likely that the rate test would not trigger. *Id.* The DSIs argue  
10 that if performing a new section 7(b)(2) rate test did not result in a rate test trigger, the  
11 net exchange benefits would now be at least \$350 million, assuming BPA's best guess of  
12 market prices during the rate period. *Id.* The DSIs argue that if the rate test continued to  
13 trigger, all REP benefits and costs could be eliminated entirely. *Id.* The DSIs argue that  
14 this single matter could change BPA's costs by hundreds of millions of dollars and  
15 BPA's failure to comply with the rate directives means no record exists to address  
16 whether the resulting rates comply with the rate directives. *Id.*

17 Q. Do you agree with the DSIs' argument?

18 A. No. First, the DSIs argue that net REP benefits for the five-year rate period in BPA's  
19 May Proposal were about \$240 million, and in the Subscription Step of the rate design  
20 process, BPA converted these calculated REP benefits into 1,000 aMW of power sales  
21 plus \$349 million in financial benefits. Schoenbeck and Bliven, WP-02-E-DS-06, at 6.  
22 This is incorrect. BPA did not convert REP benefits into power sales and financial  
23 benefits in BPA's May Proposal. The Rate Design Step and the Subscription Step that  
24 were used in developing BPA's May Proposal are explained at great length in the record.  
25 *See, e.g.,* 2002 Final Power Rate Proposal, Administrator's Record of Decision,  
26 WP-02-A-02, at 12-12 to 12-14, and materials cited therein. Basically, the Rate Design

1 Step reflects the continued existence of the traditional REP, and the Subscription Step  
2 reflects the adoption of the proposed REP settlements by the regional investor-owned  
3 utilities (IOUs). The REP benefits in the Rate Design Step are not converted into  
4 settlement benefits in the Subscription Step.

5 The DSIs argue that given the steep increases in BPA's resource costs, it is  
6 unlikely that the rate test would trigger, in which case net exchange benefits would be at  
7 least \$350 million. Schoenbeck and Bliven, WP-02-E-DS-06, at 6-7. The DSIs  
8 alternatively argue that if the rate test continued to trigger, all REP benefits and costs  
9 could be eliminated entirely. There are many variables and inputs into the section 7(b)(2)  
10 rate test. While the DSIs propose only a limited number of changes, performing the  
11 section 7(b)(2) rate test again would require BPA to review all of its inputs as well as  
12 policy, technical, and legal issues. Given these variables, one cannot accurately predict  
13 the results of the section 7(b)(2) rate test in the event the test were conducted anew.

14 The DSIs argue that this single matter could change BPA's costs by hundreds of  
15 millions of dollars and BPA has failed to comply with the rate directives. Schoenbeck  
16 and Bliven, WP-02-E-DS-06, at 7. To the contrary, BPA has conducted the section  
17 7(b)(2) rate test and has incorporated the results of the rate test into BPA's proposed  
18 rates. *See, e.g.*, 2002 Final Power Rate Proposal, Administrator's Record of Decision,  
19 WP-02-A-02, at 13-1 to 13-63. Because facts that affect the section 7(b)(2) rate test  
20 change every day, under the DSIs' proposal one could argue that the section 7(b)(2) rate  
21 test should constantly be rerun. This, of course, would be absurd. BPA must conduct the  
22 rate test and develop rates. This is what BPA has done.

23 **Section 4. Average System Costs**

24 *Q. Please describe the DSIs' arguments regarding ASCs.*

25 *A. The DSIs argue that despite a dramatic change in market prices, which have a direct*  
26 *impact on the ASCs of each utility through either a wholesale revenue credit, the costs of*

1 purchased power, or both, BPA has not modified or reevaluated the ASCs it had  
2 projected for each of the IOUs. Schoenbeck and Bliven, WP-02-E-DS-06, at 6. The  
3 DSIs argue that BPA cannot evaluate the amount of actual REP load or the net exchange  
4 costs that utilities are entitled to receive under the Northwest Power Act except by  
5 revising or updating the ASCs. *Id.* The DSIs argue that because BPA has not performed  
6 this analysis, BPA does not know if the REP settlement is reasonable. *Id.*

7 *Q. Please respond.*

8 A. First, the DSIs' central argument is that BPA does not know if the REP settlements with  
9 the IOUs are reasonable. BPA's wholesale power rate cases, however, do not establish  
10 settlement agreements or determine the reasonableness of BPA's settlements. BPA  
11 conducted a separate public involvement process regarding the development and offer of  
12 the REP settlements. *See* "Residential Exchange Program Settlement Agreements With  
13 Pacific Northwest Investor-Owned Utilities, Administrator's Record of Decision,"  
14 October 2000. The DSIs were among the parties commenting on the proposed  
15 settlements in that forum. After issuance of the May ROD in June 2000, the REP  
16 settlements were executed by BPA and the IOUs in October 2000. BPA will not revisit  
17 that decision to determine the reasonableness of the REP settlements in this forum.

18 Second, the DSIs argue that despite a dramatic change in market prices, BPA has  
19 not modified or reevaluated the IOUs' projected ASCs. This issue has been implicitly  
20 addressed in BPA's policy testimony. BPA's policy testimony describes BPA's approach  
21 to its Amended and Supplemental Proposals at length, concluding that "BPA does not  
22 believe redoing all of the forecasts is the best policy choice to address current market  
23 volatility." Burns, *et al.*, WP-02-E-BPA-62(E1). *See also* Burns, *et al.*,  
24 WP-02-E-BPA-70. BPA also has previously described many reasons why it would be  
25 inappropriate to rerun all of BPA's studies or to conduct a completely new rate case.  
26 These reasons are also applicable here.

1 **Section 5. Section 7(c)(2) Floor Rate Test**

2 *Q. Please describe the DSIs' arguments regarding the need to redo the floor rate test.*

3 A. The DSIs argue that the proposed IP rate established as a result of BPA's May Proposal  
4 was set equal to the floor rate since BPA's cost of serving the DSIs at that time was less  
5 than the comparable IP-83 charges. Schoenbeck and Bliven, WP-02-E-DS-06, at 5. The  
6 DSIs argue that including the additional cost of serving the 1,472 aMW of additional  
7 public agency load as an FBS cost – or a 7(b) resource pool cost – would undoubtedly  
8 alter the floor rate test and the resulting IP rate. *Id.* The DSIs argue that in the May  
9 Proposal, roughly 25 percent of the difference between the PF rate and the IP rate was  
10 caused by the floor rate test. *Id.* at 7. The DSIs argue that at the higher rates now  
11 proposed by BPA the floor rate differential would be eliminated, but BPA did not  
12 evaluate the IP rate in the Supplemental Proposal against the section 7(c) directives,  
13 given BPA's newly added costs of serving an additional 1,472 aMW of public agency  
14 load. *Id.* The DSIs argue that BPA simply proposes to assess a Cost Recovery  
15 Adjustment Clause increase against the IP rate determined in the May Proposal, without  
16 consideration that this would eliminate the floor rate had rates been properly calculated.  
17 *Id.* As a result, the DSIs argue that they are being required to pay higher rates than are  
18 supportable under the ratemaking requirements of the Northwest Power Act. *Id.*

19 *Q. Do you agree with the DSIs' arguments?*

20 A. No. BPA properly conducted the section 7(c)(2) floor rate test in BPA's May Proposal as  
21 part of the ratemaking process that established the IP-02 rate. The May Proposal's base  
22 rates have not changed in BPA's Amended and Supplemental Proposals. Therefore, there  
23 is no reason to selectively revisit the 7(c)(2) floor rate test. In order to accommodate  
24 possible increased costs to serve additional loads, BPA is proceeding with changes in its  
25 risk mitigation strategy instead of conducting a completely new rate case. *See Burns,*  
26 *et al.*, WP-02-E-BPA-62; *Burns, et al.*, WP-02-E-BPA-70. BPA's policy testimony

1 describes BPA's rate mitigation approach at length, concluding that "BPA does not  
2 believe redoing all of the forecasts is the best policy choice to address current market  
3 volatility." Burns, *et al.*, WP-02-E-BPA-62(E1). *See also* Burns, *et al.*,  
4 WP-02-E-BPA-70. BPA also has previously described the many reasons why it would be  
5 inappropriate to rerun all of BPA's studies or to conduct a completely new rate case.  
6 These reasons are also applicable here.

7 *Q. Does this conclude your testimony?*

8 *A. Yes.*

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