

February 11, 2014

VIA EMAIL

To: techforum@bpa.gov
and BPA Account Executives of each signatory

Re: **Comments of Avista Corporation, Iberdrola Renewables, LLC, PacifiCorp, Portland General Electric Company, Public Utility District No. 1 of Benton County, Washington, and Puget Sound Energy, Inc. on January 28, 2014 BPA Segmentation Materials**

Avista Corporation, Iberdrola Renewables, LLC, PacifiCorp, Portland General Electric Company, Public Utility District No. 1 of Benton County, Washington, and Puget Sound Energy, Inc. respectfully submit these comments to Bonneville Power Administration (“BPA”) concerning the materials presented by BPA in its January 28, 2014 Segmentation Kick-Off regarding BPA transmission facilities (“Segmentation Kick-Off”). BPA requested comments by February 11, 2014.

We appreciate the opportunity to provide these written comments, which address:

- (i) the principles that should be applied in performing an appropriate segmentation of BPA’s transmission revenue requirement; and
- (ii) the studies necessary for such segmentation, which should be based on an analysis of the use of BPA’s facilities; and
- (iii) the methodology that should be used to perform such segmentation.

In the BP-14 Final ROD,¹ the Administrator agreed that “[s]egmentation ... will benefit from further consideration outside the confines of a rate proceeding.”² Further, the Administrator acknowledged that the decision in the BP-14 Final ROD “does not preclude the use of an alternative segmentation in the future.”³ As discussed below, it is particularly important that BPA perform functional studies in the upcoming BP-16 transmission rate proceeding rather than relying on the status quo, which reflects a non-precedential settlement agreement from the 1996 transmission rate proceeding. We look forward to working jointly to develop an alternative segmentation method for use in the BP-16 transmission rate proceeding.

¹ BP-14 Power and Transmission Rate Proceeding, Administrator’s Final Record of Decision. BP-14-A-03 (July 2013) (the “BP-14 Final ROD”).

² *Id.* at page 84.

³ *Id.* at page 85.

A. BPA’s Proposed “Segmentation Principles” Confuse Segmentation With Other Steps in Developing BPA Rates

BPA Staff defined segmentation in the BP-14 transmission rate proceeding as:

the process whereby BPA assigns its transmission facilities to various segments based on the types of services those facilities provide and then assigns the investment as well as historical O&M expenses to the segments.

* * *

Segments are groups of facilities that serve a particular purpose.⁴

The BP-14 Final Segmentation Study⁵ divides total transmission costs into seven segments: (i) Generation Integration, (ii) Integrated Network, (iii) Southern Intertie, (iv) Eastern Intertie, (v) Utility Delivery, (vi) DSI Delivery, and (vii) Ancillary Services.⁶ As implemented, the Final Segmentation Study failed to assign its transmission facilities to various segments based on the customer group or function the facilities are serving.

We submit that the appropriate principles to be followed in the segmentation of BPA’s facilities for the development of transmission rates are the following:

- (i) BPA’s facilities should be segmented based on function, which reflects cost causation⁷ and sound business principles;
- (ii) the functions of BPA’s facilities should be identified by application of FERC’s seven-factor test; and
- (iii) the application of FERC’s seven-factor test to BPA’s facilities should be transparent and verifiable, consistently applied, and based on analysis of the use of BPA facilities.

⁴ Messinger, *et al.*, BP-14-E-BPA-29, at page 2, lines 3-7.

⁵ BP-14 Final Rate Proposal, Transmission Rates Study, BP-14-FS-BPA-07 (July 2013) (the “BP-14 Final Segmentation Study”)

⁶ *Id.* at page 5.

⁷ BPA has recognized that cost causation is an “overarching principle” for its ratemaking. Cost Causation is included as a primary ratemaking principle in James C. Bonbright’s *Principles of Public Utility Rates*—a reference guide on which BPA relies for “important industry ratemaking principles” throughout its initial proposal testimony and that BPA notes is “widely used throughout the utility industry.” Holland, *et al.*, BP-14-E-JP06-01, at page 17, lines 3-7 (quoting Klippstein, *et al.*, BP-14-E-BPA-24, at page 2, lines 2-6); *see also* Bogdon, *et al.*, BP-14-E-BPA-30, at page 10, line 25, through page 11, line 3.

BPA suggested “Proposed Segmentation Principles”⁸ at the Segmentation Kick-Off. With the exception of cost causation, these suggested principles are not appropriate to determine the use of BPA’s facilities. Indeed, a number of these suggested principles attempt to address ratemaking issues that are not appropriate for use in determining the segmentation of BPA’s facilities. BPA’s Proposed Segmentation Principles are set forth below, together with our preliminary observations set forth in italics with regard to each principle:

1. Full and timely cost recovery
If all of BPA’s transmission costs are segmented to and collected from users of a segment, BPA should achieve full and timely cost recovery.
2. Lowest possible rates consistent with sound business principles
BPA’s lowest possible transmission rates consistent with sound business principles should be rates based on a BPA transmission revenue requirement that is segmented using cost causation (i.e., the function or use of the facilities); such rates send an appropriate price signal and are consistent with sound business principles.
3. Equitable cost allocation between federal and non-federal uses of the Transmission system
BPA has not provided information that assigning facility cost to users would create an inequitable cost allocation between federal and non-federal uses. This consideration applies to all segmentation alternatives.
4. Cost causation
BPA’s transmission rates should be based on a BPA transmission revenue requirement that is segmented using cost causation (i.e., the function or use of the facilities).
5. Simplicity, understandability, public acceptance, and feasibility of application
The purpose of the workshops is to bring forth information and proposals that will balance competing objectives.
6. Avoidance of rate shock
BPA does not define or quantify rate shock. In the BP-14 transmission rate proceeding, BPA used 25% as the upper limit for increasing the Utility Delivery Charge. In the early 1980s, BPA increased power rates by 27-59.5% per year. We support developing segmentation alternatives and rate estimates during the study process, and considering alternatives for fairness to all customers.

⁸ Proposed Segmentation Principles suggested by BPA at the Segmentation Kick-Off.

7. Rate stability from rate period to rate period

We support identifying a segmentation method that is based on customers' uses of facilities, which should be durable over time responding to load growth and generation additions and closures without necessitating a change in the segmentation method. Rate stability affects many other considerations.

8. Considers a regional perspective

- Alternatives include how costs are allocated and recovered
- BPA hopes that proponents of alternatives will explain how the region benefits from the alternative compared to status quo

This proposed "regional perspective" principle may relate to BPA rates but does not relate to the methodology for segmentation of BPA facilities. BPA transmission rates should be based on a BPA transmission revenue requirement that is segmented using cost causation (i.e., the function or use of the facilities). It is particularly important that BPA perform functional studies in the upcoming BP-16 transmission rate proceeding rather than relying on the status quo, which reflects a non-precedential settlement agreement from the 1996 transmission rate proceeding.

9. Encourage widest possible diversified use

- Historically BPA has applied uniform rates to achieve widest possible diversified use

BPA has not always applied uniform rates, nor has it shown that uniform rates achieve the widest possible diversified use consistent with sound business principles.

B. BPA Should Perform an Updated Analysis of the Federal Columbia River Transmission System (FCRTS) and Determine the use of the System Facilities and Should Not Rely on the Status Quo, Which Is Based on the Non-Precedential Settlement Regarding Segmentation From the 1996 BPA Rate Case

BPA should perform, and present in its upcoming BP-16 rate proceeding, a sufficient segmentation study to support its proposal in that proceeding. We concur with BPA that facilities should be segmented based on the types of services those facilities provide. BPA's transmission facilities should be segmented based on how the facilities are used. Rates based on such segmentation will send an appropriate price signal by charging those who use facilities for their use. Stated differently, facilities should be segmented based on their *function*.

The purpose of segmentation *in the development BPA's rates* should be to identify the portions of BPA's revenue requirement allocable to various segments of BPA transmission facilities. Such segmentation is essential in developing and adequately supporting BPA transmission rates. For example, a desire to prevent "rate shock" should not and cannot form the basis for development of a proper segmentation. Rather, after the segmented BPA transmission

revenue requirement is developed, it may be appropriate in other ratemaking steps to make adjustments, on an interim basis, to prevent rate shock. (Note, however, that concerns about rate shock did not prevent the imposition of an increase in the BPA Point-to-Point transmission rate by almost 14% in BP-14.)

BPA cannot rely on the status quo with regard to segmentation, which is based on the non-precedential settlement regarding segmentation from the 1996 BPA rate case. Parties to the 1996 rate case vigorously disputed the segmentation in the 1996 Initial Proposal.⁹ The disputes over the segmentation in BPA's 1996 Initial Proposal were not addressed and resolved on their merits.¹⁰ Rather, the ROD in the 1996 rate case relied on the non-precedential settlement.¹¹

Uniform pricing is not a necessary and sufficient condition to establish lawful BPA transmission rates. It is neither necessary nor sufficient. First, uniform pricing is not necessary because the governing statutes provide that BPA “*may provide for uniform rates.*”¹² Nowhere in the Bonneville Project Act or in BPA's other governing statutes does the law require uniform pricing. Second, uniform pricing is not sufficient because BPA's rates must satisfy the statutory requirements to equitably allocate the cost of the transmission system discussed below and cannot be arbitrary and capricious.

The Bonneville Project Act provides that “rates schedule *may provide for uniform rates.*”¹³ The Northwest Power Act states that “rates established under this section *shall become effective only . . . upon a finding by the Commission, that such rates . . . insofar as transmission rates are concerned, equitably allocate the costs of the Federal transmission system between Federal and non-Federal power utilizing such system.*”¹⁴ The Transmission System Act provides that the recovery of cost of the transmission system “*shall be equitably allocated between Federal and non-Federal power utilizing such system.*”¹⁵ In short, uniform rates may be an option; equitable allocation is an obligation.¹⁶

⁹ Holland, *et al.*, BP-14-E-JP06-01, at page 3, lines 17-18; *see also* Exhibit BP-14-E-JP06-03.

¹⁰ Holland, *et al.*, BP-14-E-JP06-01, at page 3, lines 20-21.

¹¹ Holland, *et al.*, BP-14-E-JP06-01, at page 3, lines 21-22.

¹² Bonneville Project Act section 6, 16 U.S.C. § 832e (emphasis added); *see also* Transmission System Act section 10, 16 U.S.C. § 838h.

¹³ Bonneville Project Act section 6, 16 U.S.C. § 832(e) (emphasis added).

¹⁴ Northwest Power Act section 7(a)(2), 16 U.S.C. § 839e(a)(2) (emphasis added).

¹⁵ Transmission System Act section 10, 16 U.S.C. § 838h (emphasis added).

¹⁶ BPA explains that it has historically used the segmentation process to “ensure equitable allocation between Federal and non-Federal uses of the transmission system.” Holland, *et al.*, BP-14-E-JP06-01, at page 16, lines 17-18 (quoting Messinger, *et al.*, BP-14-E-BPA-29, at page 2, lines 12-13); *see also* 16 U.S.C. § 839e(a)(2)(C) (stating that rates must “equitably allocate the costs of the Federal transmission system between Federal and non-Federal power utilizing such system”); 16 U.S.C. § 838h (stating that the “recovery of the cost of the Federal transmission system shall be equitably allocated between Federal and non-Federal power utilizing such system”); Transmission Rates Study, BP-14-E-BPA-07, at page 2, line 22.

C. The FERC Seven-Factor Test Evaluates the Function Performed by Facilities in Order to Classify Them as Transmission or Distribution and Provides an Appropriate Basis for Segmentation of BPA’s Facilities; BPA’s Transmission Rates Should Collect Costs of Service on Transmission and Distribution Facilities Separately

The approach that BPA should use in conducting its segmentation studies is to perform FERC’s Seven-Factor Test to evaluate the function performed by the facilities in order to classify them as bulk transmission level or “distribution like” facilities to provide an appropriate basis for segmentation of BPA’s facilities.

As stated above, BPA’s transmission facilities should be segmented based on how the facilities are used. Rates based on such segmentation will send an appropriate price signal by charging those who use facilities for their use. An appropriate method for distinguishing between transmission- and distribution-like uses of BPA’s facilities is FERC’s seven-factor test. In Order 888, FERC described its seven-factor test as a functional test consisting of the following seven indicators:

- Local distribution facilities are normally in close proximity to retail customers.
- Local distribution facilities are primarily radial in character.
- Power flows into local distribution systems, it rarely, if ever, flows out.
- When power enters a local distribution system, it is not reconsigned or transported on to some other market.
- Power entering a local distribution system is consumed in a comparatively restricted geographical area.
- Meters are based at the transmission/local distribution interface to measure flows into the local distribution system.
- Local distribution systems will be of reduced voltage.¹⁰⁰

¹⁰⁰ The Commission has analyzed utilities' filings required by the Commission's regulations. These filings are made on FERC Form No. 1. While there is no uniform breakpoint between transmission and distribution, it appears that utilities account for facilities operated at greater than 30 kV as transmission and that distribution facilities are usually less than 40 kV.¹⁷

¹⁷ Order No. 888, Appendix G, FERC STATS. & REGS. ¶ 31,036 at 31,981 including n.100.

These indicators evaluate the function or use of various facilities, and no one factor is necessarily determinative. It should be noted that “reduced voltage” is only one of the seven factors. In this regard, BPA’s January 2014 Industry Practices Scan presented at the Segmentation Kick-Off discussed footnote 100 from Order 888 but erroneously suggested that voltage is the test:

The use of this threshold [35kV] is reinforced by a statement by the Commission in its legal analysis of Order 888: “while there is no uniform breakout point between transmission and distribution, it appears that utilities account for facilities operated at greater than 30kV as transmission and that distribution facilities are usually less than 40kV.” Order No. 888, Appendix G, FERC STATS. & REGS. ¶ 31,036 at 31,981 n.100.¹⁸

Read in context, footnote 100 of Order 888 is descriptive language relating to one of the seven factors in the FERC seven-factor test and is a data point based on data drawn from the mid-1990s. In short, footnote 100 in no way establishes a voltage threshold in lieu of applying the seven factors of the seven-factor test.

D. Conclusion

We appreciate that BPA is taking steps to revisit its reliance on the bright-line 34.5 kV and above test for segmentation that was adopted in the non-precedential 1996 settlement. BPA’s transmission facilities should be segmented based on their function, not based on an arbitrary bright-line test adopted as part of a non-precedential settlement. We urge BPA to apply the FERC seven-factor test to evaluate the actual function performed by its facilities so that such facilities are properly identified as transmission or distribution like facilities. Such segmentation will send an appropriate price signal by charging those who use facilities for their use and will be consistent with the statutory requirement that the recovery of cost of BPA’s transmission system “*shall* be equitably allocated between Federal and non-Federal power utilizing such system.”¹⁹

We appreciate the opportunity to submit these comments. We look forward to working with BPA and other stakeholders to develop an appropriate segmentation that can be used in the upcoming BP-16 rate proceeding.

¹⁸ Scan of Industry Segmentation-Related Practices—January 2014, BPA Segmentation Review, Industry Practices Scan (“Industry Scan”) presented by BPA at the Segmentation Kick-Off at page 8.

¹⁹ Transmission System Act section 10, 16 U.S.C. § 838h (emphasis added).