

Providing quality water, power and service at a competitive price that our customers value

January 14, 2008

Nita Burbank
NW Requirements Marketing
Bonneville Power Administration
P.O. Box 3621 - PS-6
Portland, OR 97208-3621

RE: Snohomish County PUD No. 1 Comments on
BPA's Discussion Paper on Tiered Rates Methodology

Dear Ms. Burbank:

Snohomish PUD No. 1 ("District") wishes to thank BPA staff for their willingness to share the preliminary working draft discussion paper of the Tiered Rates methodology ("Draft Paper") entitled Discussion paper on Tiered Rates Methodology. We understand and appreciate BPA's concerns with releasing this document given its preliminary state and lack of internal review. We further understand that various of the concepts presented in the paper could change given such internal review and comments from customers. However, we are of the strong belief that sharing of such preliminary staff thinking and information is extremely important to the expeditious completion of the tiered rates methodology ("TRM"), and that such sharing will help customers further strengthen their confidence in the process and the outcomes of the rate methodology. We applaud BPA's willingness to release such early drafts and encourage BPA to continue this practice.

Recognizing the preliminary nature of the paper and that many details remain to be fully developed, the District will focus its comments primarily at a conceptual level that addresses the fundamentals of the TRM concepts presented in the paper:

We believe BPA's notion of a Customer Charge based upon a customer's percentage of total high water marks is sound and largely "gets it right" at a conceptual level.

Given the tiered rates model, we believe that the concept of a Customer Charge that collects the majority of BPA's revenue requirement through an allocation, based upon a customer's share of the energy benefits of the system, is the right choice. Such a construct will help to avoid many of the significant pitfalls of traditional rate design. A simple allocation of cost, based upon a customer's high water mark ("HWM"), will result in a more stable and an inherently more fair assignment of cost to customers. It will, however, result in some degree of "cost shifts" among customers that may need to be dealt with over some transition period.

Customers should pay the costs of serving their individual loads and not transfer such costs to other customers.

The District believes this should be a fundamental principle. The sharing of cost across customers and customer classes leads to inappropriate actions and investment choices by individual customers. In the new paradigm envisioned in Regional Dialogue, appropriate price signals for load service is paramount to new resource development that is sorely needed.

BPA's concept of a load shaping charge for services to convert the inherent shape of the federal power system energy output to customer load coupled with a demand charge to cover utility peak requirements above that which can be provided by the federal power system is both appropriate and necessary to meet this fundamental principle. Customers should pay the full cost of BPA's purchases and sales to balance loads and resources for their individual utility. This will ensure equity among customers and provide appropriate price signals for investments. However, more explanation and vetting of the concept for a different load-shaping charge to customers below their annual HWM is needed. Snohomish is concerned that this may lead to inappropriate cost-shifts between customers. BPA will incur the full marginal cost of shaping federal resource to a customer's load regardless of whether the customer is above or below their annual HWM.

BPA discretionary long-term "off-the-top" obligations should be eliminated.

The federal power system is no longer surplus in capacity or energy. Such long-term off-the-top obligations act to reduce the effective capacity and energy available for service to preference customer load. Crediting of revenue from such obligations is not a substitute for reliable load service to BPA preference customers.

Stability in the methodology for determining utility costs (TRM) is paramount for customers to have confidence in making future investment choices.

In the Draft Paper, BPA reserves for itself the right to change the TRM in the future utilizing its rate making process. This is a mistake. Utilities will be making long-term, 20-year plus, investments in new resources and/or deciding Tier 2 BPA commitments. To do so, they must have confidence that the cost allocation and rate setting methodology will endure through the term of their contracts. As such, the methodology should be embedded in contract. Only changes in cost and federal power system attributes, that result in a change in rates, should be the subject of the rate making process; the methodology for determining the rates should remain stable.

There must be no bleeding of costs or risk from Tier 2 to Tier 1.

Isolation of Tier 2 costs from Tier 1 is fundamental to the construct of a tiered rate design and necessary for customers to invest in new resources. If Tier 1 becomes the catch-all for unanticipated Tier 2 costs, then Tier 2 will have a significant advantage over the development of new non-federal resources in that they will be essentially absolved from resource development risk. To protect against this, BPA should adopt policy which does not allow for such cost transfers. And, it should not include any risk premium in Tier 1 for Tier 2 risks. Such risks should be entirely borne in the Tier 2 costs.

To protect against such bleeding of cost and risk, BPA should require, at a minimum, from all customers choosing Tier 2 service, regardless of Tier 1 product choice, the following:

- Take-or-pay contracts, with provisions for remarketing any excess commitment, and flowing the revenue back to the customer;
- Adequate credit support;
- Funding up front for customers committing to a long-term resource acquisition. This will place such customers in the same position with respect to financial and performance costs and risks as developers of non-federal resources.

The Draft Paper also states that BPA will operate its Tier 1 and Tier 2 resources in a combined manner to “meet load in the most efficient way.” This is inappropriate. It means, in essence, that Tier 2 resource acquisitions by BPA will have as a back-stop, the federal power system. This is a significant advantage to Tier 2 over non-federal resources developed and operated independently by customers. The operation and dispatch of Tier 2 resources should be isolated from Tier 1 so that there is, as much as possible, equality between the cost and risk of choosing non-federal resource development and Tier 2 load service. To do otherwise will significantly undermine new non-federal resource development by publics.

BPA should offer more flexibility for customer funded conservation and conservation verification timelines.

BPA has proposed that customer funded “custom” conservation products be reviewed for the cost-effectiveness test. The District feels that the District itself should be the accountable party for this determination of cost-effective conservation and asks BPA to provide for custom project conservation achievements, as verified, to be added to a utility’s HWM. There are currently discussions on how to apply cost-effectiveness underway in the Region. Custom projects may fall under a ‘program cost-effectiveness’ guideline, rather than by an individual project. Also, the one-month timeframe presented in section 2.1.5.2 does not appear to provide adequate time to assure that custom projects are verified by BPA as effective conservation achievements and included in the important HWM true-up process.

There should be no melded cost pool.

In the Draft Paper, BPA refers to a melded cost pool for customers that do not receive a HWM. While the specifics of this melded cost pool are unclear, in principle there should not be any such pool. Such a cost pool would be the antithesis of the tiered rates paradigm which customers and BPA have worked so hard on. And, as importantly, it would encourage individual publics in the pool to annex territory. This is because they would not see the cost of such annexation directly; but rather the cost would be spread across the rate pool.

Audit rights should be retained.

BPA has proposed that Slice customers will not retain their contractual audit rights. This is inappropriate. It is the District's opinion that this should be a common right included in all BPA contracts. Customers will be entering into long-term business arrangements with BPA that includes a commitment to cover their share of cost based upon their HWM. This is appropriate; however, it is also appropriate that in such a business arrangement, customers be afforded the right to audit BPA's financial statements. This is an important and integral part of any such business arrangement and is a common element of contracts between private parties who take on such obligations. Inclusion of audit rights is a fiduciary obligation in addition to being simply good business practice.

To minimize the potential burden that audits might impose on both customers and BPA, there should be limits on their frequency, a significant requirement for triggering an audit such as a super majority (based on HWM share) customer request, and limits on the subject of an audit. This would prevent individual or a minority of customers from demanding an expensive and time-consuming process.

It is not clear to the District why a "Load Following Charge" should be assessed by BPA (Section 6.4).

If, as BPA states, customers will pay for load following as part of their transmission rate, it seems such a charge is duplicative. More clarification is needed here.

More detail will be needed with regard to the "Diurnal Flattening Service" which BPA proposes.

An important aspect of such a charge is that it cover the full cost of integrating a resource a making it useful for serving load. This is especially important for intermittent resource acquisitions that impose significant cost on the power system for generation imbalance and extreme inter and intra hour variation. More discussion and detail on the derivation and construct of the charge is needed.

Additional clarification is needed with regard to the “Load Shaping Charge”.

BPA has proposed that customers should be assigned the full net cost of load shaping to meet their load regardless of whether they are above or below their HWM. Any net over collection would then be credited back to the Tier 1 composite rate. It is the District’s opinion that customers should pay or be credited at the same rate, whether they are above or below their HWM. This is a parallel construct for when a Slice customer percentage is reduced due to load loss and resale revenues are credited back to the composite rate cost pool.

The 7(b)(2) rate test should include the cost of non-federal resource acquisitions by publicly owned utilities as well as Tier 2 service costs when determining the residential exchange benefits of the investor owned utilities.

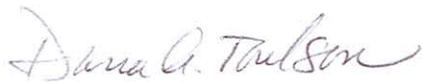
The proposal only contemplates inclusion of Tier 2 resource acquisitions into the residential exchange benefit calculation. This ignores the fact that many publics will make significant investments in non-federal resources for load service, driving up the overall cost of wholesale power to publics. Inclusion of such costs is appropriate in achieving the goal of the Regional Power Act to equalize public and investor owned wholesale power costs.

BPA should no longer subsidize the rates of the Direct Service Industries (“DSIs”).

The District believes that BPA should no longer subsidize rates for the DSIs. Such subsidies result in higher rates for industrial customers of publicly owned utilities to their significant disadvantage. Such subsidies are no longer appropriate or legally required.

Once again, the District appreciates BPA’s willingness to share its preliminary draft discussion paper on the Tiered Rates Methodology. We look forward to continuing to work with BPA in this positive vein as we complete this important work.

Sincerely,



Dana Toulson
AGM Power, Rates & Transmission Management

cc: Stuart Clarke, BPA-PS Account Executive