

1994 MAJORITY STAFF REPORT OF THE TASK FORCE ON BONNEVILLE POWER ADMINISTRATION

OVERSIGHT HEARING BEFORE THE SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS OF THE COMMITTEE ON NATURAL RESOURCES HOUSE OF REPRESENTATIVES

ONE HUNDRED THIRD CONGRESS

SECOND SESSION

ON

1994 MAJORITY STAFF REPORT OF THE TASK FORCE ON BONNEVILLE
POWER ADMINISTRATION, "BPA AT A CROSSROADS"

HEARING HELD IN WASHINGTON, DC
AUGUST 9, 1994

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1994 MAJORITY STAFF REPORT OF THE TASK FORCE ON BONNEVILLE POWER ADMINIS- TRATION

TUESDAY, AUGUST 9, 1994

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS,
COMMITTEE ON NATURAL RESOURCES,
Washington, DC.

The subcommittee met, pursuant to call, at 9:45 a.m., in room 1324, Longworth House Office Building, Hon. Peter A. DeFazio presiding.

STATEMENT OF HON. PETER A. DeFAZIO

Mr. DeFAZIO. Okay. The committee will come to order.

There will be a slight change in the order today in that I will make an opening statement, and then Congressman Smith will have some opening remarks, and then we will hear briefly from Mr. Robertson, Deputy Administrator representing Bonneville Power Administration for an announcement. And then, because I believe that will perhaps be reflected in subsequent testimony, or subsequent testimony we may want to reflect on that, and then we will go to the panels as scheduled.

It is about a year ago, we were in the midst of the Bonneville Task Force hearings, a number of which we did in the Pacific Northwest. In fact, it would have been my preference to do this hearing in the Northwest, but given the exigency of the schedule, that wasn't possible and I felt the hearing was very timely and important, given the speed with which BPA is moving to implement what would be the most far-reaching changes in the system of distributing Northwest power and in the relationships among the customer groups since the Northwest Power Act of 1980.

There is some controversy over what the immediate threat is to Bonneville regarding their future competitiveness and how they might best respond to that. The key to me is that we want to get this right. Certainly there are time pressures, and we must look at those.

On the other hand, the last time the region got into a panic over time pressures, that being the panic generated by the notices of insufficiency, promulgated by BPA to the region, we put ourselves into the largest financial disaster in the history of the Pacific Northwest, and we are still paying for it, and we will be paying for it, most of us in this room, until the day we die. That episode was called WPPSS.

So I want to make certain that in rearranging relationships in the Northwest, we do it well. To me, you know, the best public policy is made in the public view.

Perhaps I am prejudiced as an Oregonian. I was a local official. I dealt with the open meetings law and we had to do the most sensitive things always in a public forum. And even if we finally could find something like a personnel matter that required a closed session, the reporters could still come in the room and they could challenge whether or not that was truly appropriate as a closed-door meeting.

I am concerned that much of the basis for the Bonneville Power Administration's new policies has been formulated essentially behind closed doors. Yes, there have been customer working groups and other things, but there has not been broad public involvement, in part because of the complexity of the matters, but in part because of the relationships that exist between particular customer groups and the Bonneville Power Administration, the ins and the outs, the haves and have-nots, the winners, the losers.

So I think it is entirely appropriate, despite some testimony submitted to this committee, that Congress, the policymakers, shed some light on what is going on and attempt to help the region, that is the people of the region, every person in the region, determine the equities in what is being proposed. We have allegations by some customers, an analysis by the non-DSI industrials, that there would be a massive shift of burden under this new tiered rate proposal, increasing costs to the public utilities of up to \$300 million a year. Who wins, who loses? Is that good public policy? Will that get us to the energy future we want in the Northwest? Those are questions that we need to examine today.

I am pleased that we have a good slate of witnesses to come before us, and we have a number of issues to develop. The committee had a rather extensive series of questions it asked to have addressed.

I have read the testimony that was submitted as of 5:00 o'clock yesterday. As the witnesses testify, I would prefer that they summarize, go to points in response to other testimony, and do as best as possible to make their testimony relevant, knowing that what you have written has been read and any other written responses that you might provide will be read, and will be incorporated into the entire record.

This is an extraordinarily important time for our region. It is a time of change, and, as in any time of change, people are jockeying for position. I don't expect anybody, no matter what interests they represent, to come in and want to give away their interests.

I don't expect private utilities to want to give big advantage to the public or to make some changes that would give big advantage to private, or one industrial group to want to give advantage to another. Certainly you should all be strong advocates for the interests that you represent. I understand that. I appreciate that. I am an advocate myself.

But I am an advocate for the future of the entire Pacific Northwest and all the ratepayers. I want to balance those interests fairly and equitably as we balanced them I think with great wisdom and after great controversy in the Northwest Power Act.

I am concerned that what is being proposed here will unbalance that act and in ways that we don't yet understand, and that is what this hearing is about. We want to understand it. We want to lay it out. We want everybody to have an opportunity to comment on it. We want to decide as a region that it is fair and equitable and the best way to go forward to a stable energy future for everyone who lives in the Pacific Northwest, particularly for our children. That is why we are here today.

So I thank everybody for trekking across the country. I do it a lot. I know it is not fun or easy. And I look forward to your testimony.

[Prepared statement of Mr. DeFazio follows:]

The Remarks of the Honorable Peter DeFazio
For a Hearing of
The Subcommittee on Oversight and Investigations
August 9, 1994

Last year at this time, the Task Force on the Bonneville Power Administration was in the midst of a series of hearings considering the extraordinary challenges facing BPA. We then spent many months working on a report containing my conclusions after that oversight exercise. The report and its relationship to the changes now being proposed by Bonneville in its Draft Strategic Business Plan is the subject of this hearing.

BPA is moving to implement the most far-reaching changes considered by the agency since the passage of the Northwest Power Act in 1980. I've heard an increasing number of concerns that Bonneville is moving too hastily -- that the agency has so many processes underway, it is virtually impossible to keep up with them all or understand the implications of the sum of the changes now underway.

BPA claims that its haste is driven by the competitive threats unleashed by an increasingly deregulated utility marketplace and cheap natural gas. We can all agree that Bonneville faces unprecedented competitive challenges. But we seem to have some disagreement on the immediacy and the magnitude of those threats. We'll hear more about that during this hearing.

BPA is first and foremost a public agency with a mandate from the public it serves. The public deserves to fully understand the implications of the profound changes underway at BPA before those changes are set in place.

That's why I am pleased to be able to share a letter I just received from BPA Administrator Randy Hardy. In answer to my written request -- and the requests of a growing number of Bonneville's customers -- Randy has decided to delay the start of a rate case intended to design and implement a tiered wholesale electric rate. His revised schedule would commence a rate case on January 9, instead of October 15.

That's good news and I congratulate BPA for its flexibility. As we will hear later today, BPA's tiered rate proposal could cause a huge shift in costs between customer groups, placing as much as \$300 million a year in new costs on growing public utilities like EWEB or the Springfield Utility Board in my district, or the utilities serving Tacoma and Seattle in Washington State.

Though I'm pleased that Bonneville has slowed the pace a bit on tiered rates, I am dubious about the agency's plans to complete the complex task of negotiating new power sales contracts within the next four months. The current contracts

between BPA and its utility and DSI customers expire in 2001. Some of the most significant issues facing Bonneville and the regions' electric ratepayers will be resolved in the new contracts, including the region's relationship to the aluminum industry and the nature of the integrated resource planning requirement now being negotiated with BPA's public utility customers.

I understand and sympathize with the customers' desire for planning certainty. But I am strongly of the opinion that BPA must resolve these issues openly and only after consideration of a range of alternatives. To that end, I am urging Bonneville to prepare an environmental impact statement to guide the development of its new long term power sales contracts. An EIS will lay out options for BPA and its customers, and analyze the likely outcomes. That's the kind of information the region needs in order to understand and ultimately endorse BPA's new direction.

Among the changes proposed by Bonneville is the reinvention of its conservation programs. It is far from clear whether BPA's reinvention will accomplish the region's energy conservation goals. BPA's current conservation programs delivered a record 52 megawatts of conservation last year at a cost of only 23 mills per kilowatt-hour. The burden of proof is on Bonneville to show that its new approach will deliver the energy efficiency savings called for by the Power Planning Council. I remain unconvinced.

The tradition of publicly-owned and operated utilities is particularly strong in the Pacific Northwest. Public power offers its ratepayers economical electric power and responsive service. A public utility is, by definition, devoted entirely to the interests of its ratepayers. I am a strong believer in public power.

BPA was created to market the power from the federal hydroelectric projects on the Columbia River. In its sale of power, it is directed by law to give "preference and priority" to publicly-owned utilities. BPA's Business Plan seems to violate that very basic directive in a number of respects. We'll talk about the future of public preference during today's hearing.

And finally, the Task Force report contained a number of proposed cost savings. Some of the most significant are found in the management of the Washington Public Power Supply System's single operating nuclear reactor. Mr. William Council, the managing director of WPPSS, took issue with those recommendations. He's here today to make his case.

We will not be considering the changes proposed by BPA in its fish and wildlife programs during this hearing, though that issue may be the subject of a future hearing. Generally, I share BPA's interest in making its fish and wildlife obligations more predictable, but am concerned about any proposal that seeks to

place an arbitrarily defined cap on BPA's fish and wildlife obligations.

As I said, BPA is first and foremost a public agency with a public purpose. We all support BPA's goal of maintaining its competitive position, of becoming less bureaucratic and more efficient. But not at the cost of sacrificing its mandates to promote efficient energy use and rebuild the Columbia River's salmon runs. Those mandates should not be seen as a drag on Bonneville's ability to do business, but as the reason Bonneville is in business in the first place.

The Task Force's report stated: "The Northwest Power Act sought to encourage conservation and efficient energy use and promote the development of renewable energy resources, thus assuring the Northwest an adequate, efficient and economical supply of power. The goals of the Act remain sound. In the final analysis, these goals are the yardstick by which Bonneville's new Marketing and Business Plans should be measured."

This hearing seeks to measure BPA's Business Plan against that yardstick.

Mr. DEFAZIO. I will defer now to Congressman Smith and then we will hear from Mr. Robertson. Bob?

STATEMENT OF HON. ROBERT F. (BOB) SMITH

Mr. SMITH. Thank you very much. You are certainly correct.

This hearing comes at a very crucial time, especially for Bonneville Power Administration. It seems to me exacerbating this whole issue has been the idea that for too many people that BPA is a bottomless pit for every social program that comes along. They spend \$1 billion trying to save fish, currently \$1 million a day, and it seems as though there is no breakthrough in that issue.

But I want to compliment what I believe Bonneville Power Administration is doing currently in reorganization and trying to bring the agency into a competitive world. There is no question in anybody's mind that it wasn't the Government that did it, or it wasn't hearings that did it, it was the need to be competitive, and Bonneville is reaching out, attempting to reorganize and attempting to compete, and I take my hat off to them for that. I would hope in the future that they would not be so soft-headed and soft-minded as to accept every brainless idea that comes down the road about how to correct either the salmon runs or the issues on the whole Columbia River.

But of course many say that it is still not enough, Bonneville must do more. Of course these are the same people that have bought into the Andy Kerr logic that we must go beyond \$1 million a day in spending money for fish and of course to save the salmon, we must eliminate the real villains.

Now, who are those real villains? Well, to those that know, the real villains are the direct service industries who operate from Bonneville energy, so-called corporate agriculture, quote—underline corporate agriculture, and of course included in this is the aluminum industry. These are the people that are responsible for the loss of our salmon, and, Mr. Chairman, you probably know—I am not sure you do—that there is one huge aluminum company in my district. It is called Northwest Aluminum. Brett Wilcox is here.

This huge corporate structure has a little notch business in the aluminum area in the country. They employ 470 people at a decent wage in The Dalles, Oregon, and when we talk about the villain, make sure we include this huge octopus, this giant industry that is housed in The Dalles, orchestrated and engineered by basically one person and his employees who are part of the whole program and has been tremendously successful.

Well, I think that we can still support an affordable and environmentally-responsible energy package for Bonneville, and at the same time support 40,000 direct and indirect jobs in our area associated with the DSIs in the Northwest. While eliminating an industry that pumps about \$2 billion annually into the Northwest economy is not going to bring the salmon back, but it could bring us a recession to the Pacific Northwest.

And I mentioned this corporate agriculture that has been charged with demonizing the waters of the Columbia River, the facts are that on the Washington side about 1.5 percent of the Columbia River water is used for agriculture, and on the Oregon side, about 1 percent of the water is used for agriculture. So if we wiped

out this corporate agriculture, which by the way is not corporate at all. These are mom and pop farms. There may be a corporation or two along the river, but for the most part, they are just family farmers using a very small amount of water and trying to make a living and providing the cheapest food in the world to the people of America.

So I suppose we should get rid of them. That would help a lot, I know. And then, you know, we go to the whole question of the DSI's and those who are producing in the Pacific Northwest.

So I don't have a problem standing up for the people who produce, and there is no question that we have made some horrible mistakes in the past and BPA has, and is attempting to be the perfect environmental and conservation-oriented organization, and it has cost billions of dollars and it hasn't worked.

So rather than point fingers at each other and eliminate industry and agriculture, and aluminum, maybe we better look inside and see what we have done wrong on the other side of the ledger, that is attempting to be politically perfect environmentally, and in the area of conservation.

I look forward to these hearings, Mr. Chairman, because I think there is a defense that can be raised and will be raised today against those who believe that we ought to chop out 13 dams and therefore the economy of the Northwest to satisfy what some believe is the salvation of the salmon.

Thank you.

[The prepared statement of Mr. Smith follows:]

**STATEMENT OF CONGRESSMAN ROBERT F. (BOB) SMITH
OVERSIGHT AND INVESTIGATIONS SUBCOMMITTEE
HEARING ON "BPA AT A CROSSROADS"
AUGUST 9, 1994**

Mr. Chairman,

This hearing comes at a crucial time for the Bonneville Power Administration. This agency that for too long has been the bottomless pit for every social program that comes along. They have spent one billion dollars on saving fish. But yet some say that's still not enough.

These are the same people that have bought into Andy Kerr's logic that we must go beyond spending one million a day for fish. They say that to save the salmon we must eliminate the real villains -- the direct service industries and irrigated agriculture.

I wasn't aware until recently that the 470 people working at the aluminum plant in my district were putting Northwest ratepayers at risk. The truth is, they are not. Nevertheless, some are trying to exploit this issue even though they know it makes absolutely no sense.

I think you can still support affordable and environmentally responsible energy path for Bonneville and still support the 40,000 direct and indirect jobs associated with the Direct Service Industries in the Northwest. Eliminating an industry that pumps \$2 billion annually into the Northwest economy is not going to bring back the salmon. But it may bring back a recession in the Northwest.

Or what about irrigated agriculture. We have heard about the so-called "corporate irrigators" who want to gut the Northwest Power Act. Who are these people? The irrigators I know are family farmers in places like Umatilla and Morrow County. These small operations in these two counties inject \$400 million into Oregon's economy and they are not the least bit interested in gutting the Northwest Power Act. They are too busy trying to scratch out a living.

So I don't have any problem standing up for these people even if some others won't. The problem is not the people who create jobs in the Northwest, it's the people in the Northwest who think Bonneville is a cash register.

The problem is that some people have confused cutting the fat at Bonneville and cutting the heart out of the Northwest economy.

Mr. Chairman, I look forward to the testimony we will hear today.

Mr. DEFAZIO. I thank the gentleman.

Mr. Allard, do you have an opening statement?

Mr. ALLARD. Mr. Chairman, I don't have an opening statement. Thank you.

Mr. DEFAZIO. Okay. Thank you.

With that, Mr. Robertson is recognized out of order for some very brief remarks.

STATEMENT OF JACK S. ROBERTSON, DEPUTY ADMINISTRATOR, BONNEVILLE POWER ADMINISTRATION, DEPARTMENT OF ENERGY, PORTLAND, OR

Mr. ROBERTSON. Thank you, Mr. Chairman. I am Jack Robertson, Deputy Administrator of Bonneville.

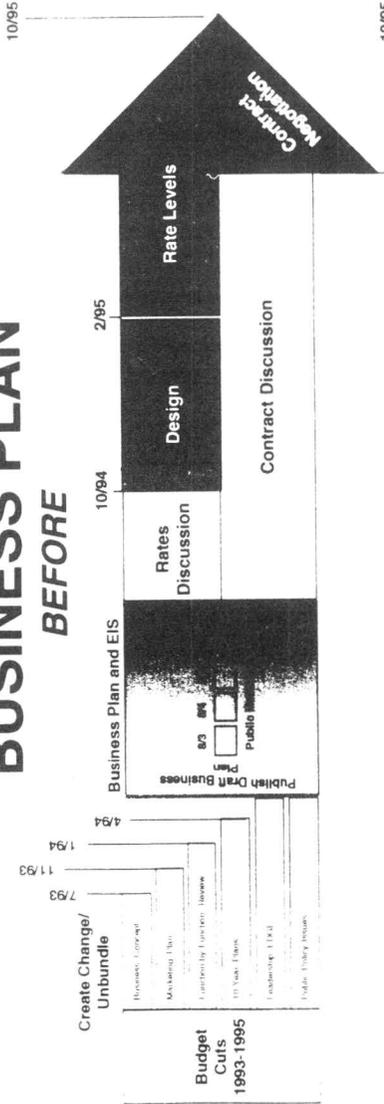
We thought we would at least lead off here with a change of schedule which we thought was significant and would perhaps lay the context clearer for the hearing. Last month we received from you a letter indicating your concern about the fact that we were in fact proceeding on a schedule that seemed to you to be too quick based on the issues you felt were at stake. You had indicated to me personally, I think and to others, that you felt there was a growing customer and stakeholder concern in the region that this schedule was in fact causing people concern because of the compression of time around it.

In the wake of that letter, and in conversations with you, we did a customer survey and talked to stakeholder groups, as well, to verify that in trying to shape our public involvement program to be responsive to as many concerns as we could. We look forward to congressional reviews like this. We look forward to open debate. We think that will definitely result in a better product in the end. We take a lot of pride in our public involvement responsiveness.

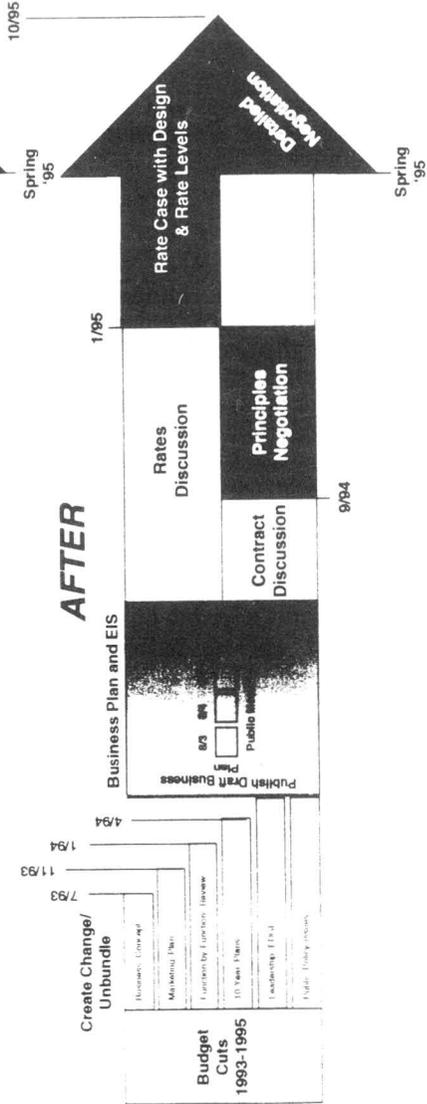
What you see here is, quickly, a before and after chart, I think you have a copy of this in your packet. If you don't, we can get it to you. The chart simply on the top is the before chart. This is before we had a conversation. We were planning on finishing our public involvement process at around the end of August with three public hearings. We have blowups of this.

[The charts follows:]

BUSINESS PLAN BEFORE

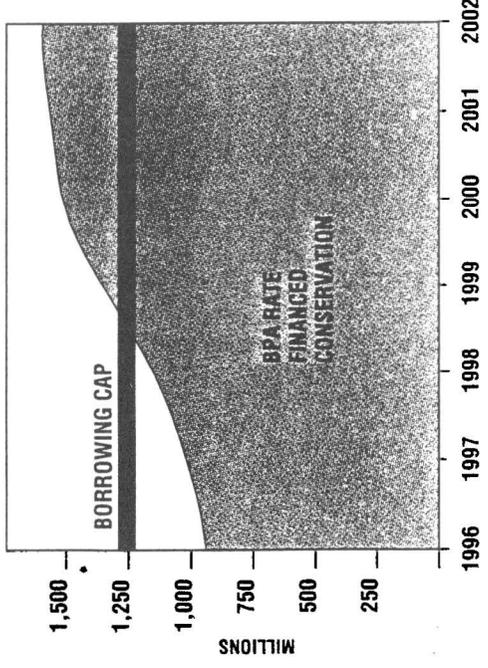


AFTER

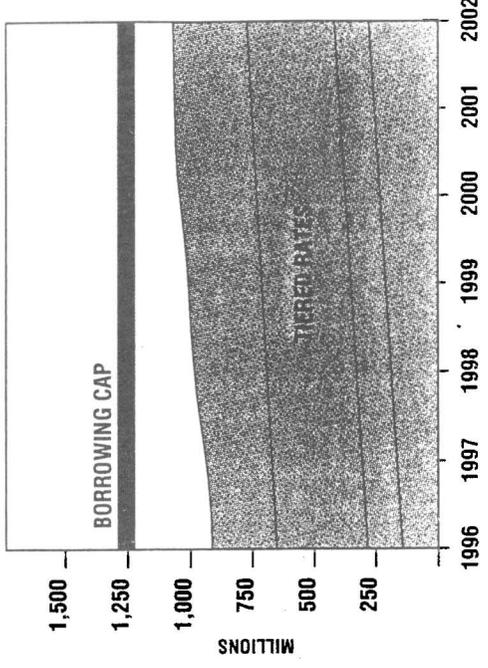


Conservation Objectives

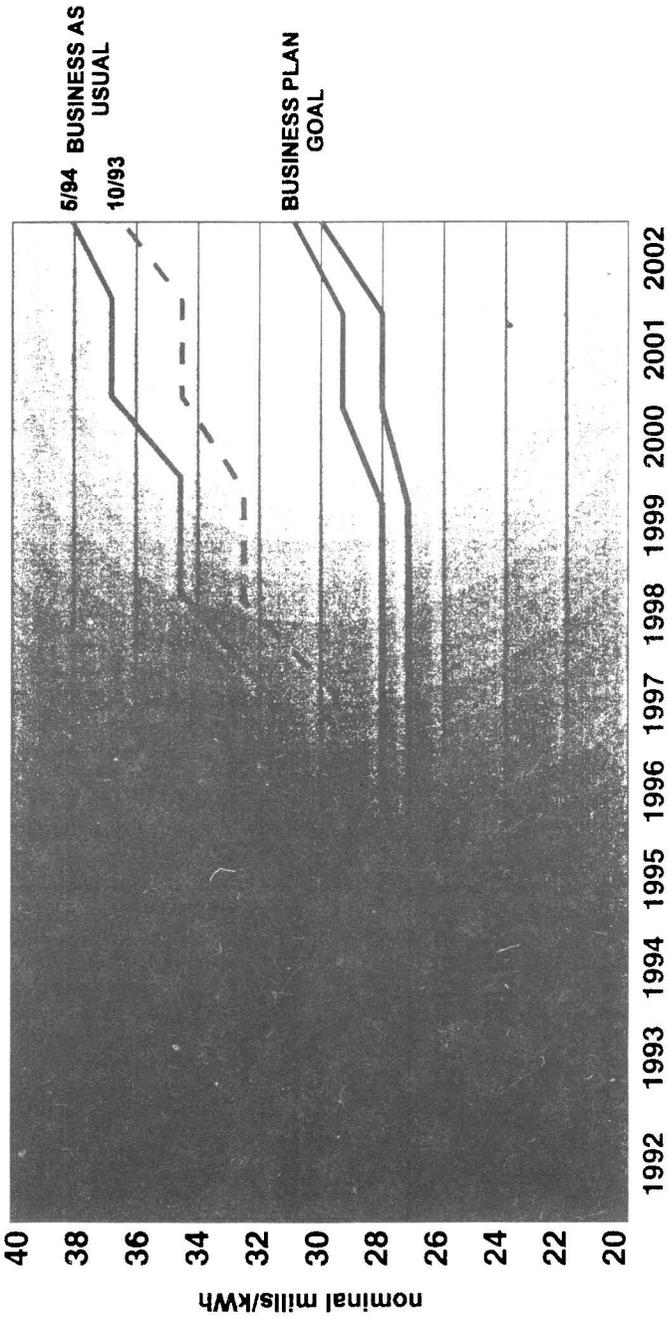
**Without
Business Plan**



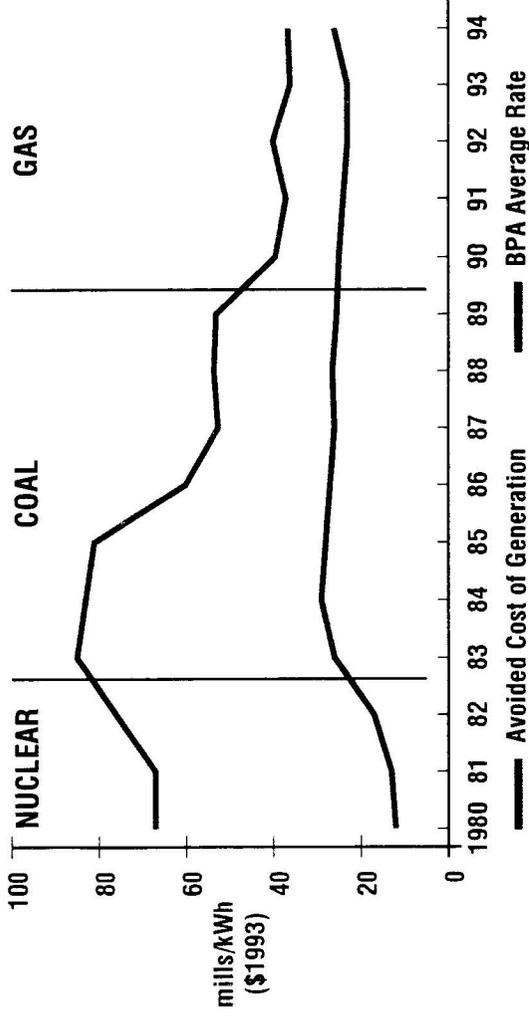
**With
Business Plan**



Rate Comparison



Avoided Cost of Generation vs. BPA Average Rate



NUCLEAR: based on actual cost of Washington Public Power Supply System
 COAL: based on studies by Kaiser Engineers Power Corporation, among others
 GAS: based on studies by Fluor Daniel Incorporated, among others

Mr. DEFAZIO. You are dealing with an aging panel here.

Mr. ROBERTSON. What you and folks in the region wanted, was to put it as simply as possible and as quickly as possible. You needed more time for a discussion about the impact on tiered rates and discuss how those tiered rates might effect various customer classes. You needed to get more information from us before we entered into that debate more seriously—about the potential impact by customer group. The customers also needed to have more information on principles associated with contracts negotiations that are preceding in parallel with the rate case.

To be brief, what you see in the after arrow is a substantial expansion of the window of discussion, the rates discussion. At the top of the after arrow, you can see the window of discussion has opened quite large and now extends to January, 1995. At that point the darkness takes over, that is when the rate case begins and the ex parte window comes down. That was a concern I know of the committee as well.

So, we have tried to push that rates discussion period out. We will provide further information through a tiered rates model to the committee and to others in the region in the next 30 days.

[The information follows:]

The tiered rates impact model is still under development. Technical work is being done by BPA and our customer representatives. We will provide the model to the Committee upon completion.

Mr. ROBERTSON. You can see that the contract discussion which was simply a discussion pointed to the top arrow before our conversations with the customers, beginning with contract negotiations in the spring, now involves principal negotiations on the contracts, begins in parallel and ends around January 1, as well. We think that will marry up the concerns of the customers for more information and begin to make basic principles known in the contracts prior to entering the rate case when a number of principles are translated into different rates.

Fundamentally we have expanded the public involvement process into September. I think that is not enough for some folks, but given the rate schedules we are on and the need to get done by October 1 of next year, we are deeply pushing the Bonneville staff, which is in a transformation of its own.

So to make it brief, we tried to respond to our customers. We have met with the customers and others. We did a pretty good job of moving quickly, and I think we have opened a discussion. There will be plenty of opportunity for interactive debate in the course of the next two or three months.

Mr. DEFAZIO. If I could briefly summarize. The immediate concern which I expressed, that is, not fully understanding the potential impact between customers groups, which has been a growing concern in the region, and then there are other concerns to be expressed during the hearing, that during this time period, there would be latitude for adjustment in the tiering proposal, more analysis on those disparate impact that will be made available to all of the customers and the public in the Pacific Northwest so that we fully understand what we are entering into.

Mr. ROBERTSON. Yes. We expect to provide a tiered rate impact model which is jointly developed by the customers and us later this month. It should begin to be the basis of the information you need.

Mr. DEFAZIO. You think later this month you can have that.

Mr. ROBERTSON. That is what our objective is. We will get it done in plenty of time. The window now gives us the opportunity to iterate on that.

Mr. DEFAZIO. Okay. I appreciate that. I think it is a good step on the part of BPA. The only unfortunate part of your testimony was where you said the darkness takes over on January 1st, but we will let that go by.

Mr. ROBERTSON. Some people see it that way.

Mr. DEFAZIO. Well, you know, there is a problem when we get into the rate setting in terms of the, you know, the restrictions of the ex parte contacts, and you know, when people want to raise policy concerns, it is very difficult, and I understand you are also looking at ways to modify and your attorneys are reviewing ways in which you could have a more open process during the rate making; is that correct?

Mr. ROBERTSON. Yes.

Mr. DEFAZIO. Okay. Thanks.

Mr. ROBERTSON. Thank you.

Mr. DEFAZIO. We will return to the regular order now and have the first panel. It is a rather large—oh, wait a minute. Sorry. We start with a small panel, but of high quality. I skipped to part two there, Angus, sorry. Angus Duncan, council member, Northwest Power Planning Council for the State of Oregon.

**STATEMENT OF ANGUS DUNCAN, COUNCIL MEMBER,
NORTHWEST POWER PLANNING COUNCIL, STATE OF OREGON**

Mr. DUNCAN. Mr. Chairman, thank you. Mr. Smith, good morning, nice to be here in this historic room.

Mr. Chairman, my name is Angus Duncan. I am here today representing the Northwest Power Council to offer the council's testimony on the report of the Task Force on BPA and on Bonneville's draft strategic business plan. You have our written testimony and I just have a few remarks here to add.

The council emphatically supports the stated intention of the draft business plan, which is to steer Bonneville through the competitive challenges it faces to successfully achieve its fundamental legislative plan dates. There is also much within the business plan that the council supports, including actions that were called for in the council's 1991 power plan.

There are also elements that the council believes must be developed more fully before they are decided and implemented. I discussed these principally in the written testimony.

This morning I would like to focus on four challenges for Bonneville that the council perceives in this plan.

The first has to do with Bonneville's response to the newly competitive energy markets. Bonneville begins with a significant competitive advantage in this region, the Pacific Northwest. The council staff analysis has suggested that Bonneville's wholesale power is today between 16 and 30 percent less expensive than power sold

by other Northwest utilities, Bonneville's initial competitors in the emerging wholesale power markets.

We believe with prudent business choices that Bonneville should be able to maintain that edge into the foreseeable future. As it adjusts to the competitive marketplace, Bonneville must be selective in choosing the markets where it will compete; it must husband the Federal base system, maximize its efficiency and cost advantages. Some of the methods that Bonneville proposes for maintaining its competitive position, such as tiered rates, are proposals that the council set forth in the 1991 power plan. It is gratifying to see them emphasized in the business plan, and we are working with Bonneville on the process of implementing those ideas.

Second, Bonneville has a balance beam to walk here between the competitive pressures of the marketplace and the agency's identity as a public agency with public interest responsibilities. This is more than simply compliance with the law, which is the obligation of any private company. Bonneville is the steward of a valuable regional power system and of the rivers that underlie that system, and these are rivers that have environmental, aesthetic, and cultural as well as economic significance, including most particularly, rights reserved by Indian tribes through treaties with the United States.

Bonneville's challenge is to remain a competitive wholesale supplier of power products and services while fully implementing the intent of Congress in the Northwest Power Act and the council's regional power plan and regional fish plan; that collective intent, particularly, to acquire all cost-effective conservation, to develop new renewable technologies and to protect, mitigate and enhance fish and wildlife in the Columbia River basin.

The biggest unknown affecting Bonneville's competitive position, aside from whether it can complete its internal efficiency measures, is the impact of fish and wildlife expenditures, particularly the impact of river operations that may be required to protect threatened salmon stocks. No one can guarantee that there will not be further impact to the hydro system, but the council, working with Bonneville and other parties in the region to look for the most cost-effective ways to use that system while protecting the fish, including, for example, more cost-effective and less hazardous means of spillage of fish through the dams.

The council's third concern is that Bonneville recognizes which elements of the business plan are right for implementation, organizational structures. More efficient and delegated decision-making are two examples, and which need further work within the region. Reinvention of conservation, some aspects of the tiered rate proposal, treatment of fish and wildlife obligations are examples of policy choices with far-reaching consequences that should be neither delayed needlessly, nor rushed to fit a predetermined business plan schedule.

Finally, Bonneville must prepare to compete long-term as well as near-term. With its present edge in wholesale power costs, Bonneville is better positioned than any other regional facility to invest retained earnings in tomorrow's technologies and information systems where this can be done through collaborative efforts, through EPRI, through the National Labs, the regional collaboratives. Bon-

neville should exploit such opportunities to make the dollars go further. The same fashion, cost-effective investments in conservation today will pay dividends in regional competitiveness down the road. But if the cost advantage is applied only to keep rates down today, the region will lose an enormous opportunity for the future.

In conclusion, the council finds much to support in the business plan. We are concerned that undertaking changes in haste or with only short-term competitiveness foremost in mind would not serve the region well. We agree that Bonneville faces competitive challenges, but we believe that through thoughtful management, Bonneville can make these challenges work to its advantage and the region's.

Thank you, Mr. Chairman. I will be happy to answer any questions.

[Prepared statement of Mr. Duncan follows:]

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August 6, 1994

**Testimony of the
Northwest Power Planning Council
before the
Subcommittee on Oversight and Investigations
Committee on Natural Resources
U.S. House of Representatives
on
the report of the
Task Force on the Bonneville Power Administration
"BPA at the Crossroads"**

Good morning, Mr. Chairman and members of the Committee. My name is Angus Duncan, and I am one of two Oregon members of the Northwest Power Planning Council. I am pleased to be here today to offer the Council's testimony on "Bonneville at the Crossroads," the report of the Task Force on the Bonneville Power Administration, and on the consistency of Bonneville's Draft Strategic Business Plan with the recommendations of Sections II and IV of the Task Force report.

Our comments are organized to address 1) goals of the Business Plan, 2) the major policy changes that Bonneville is proposing to help achieve those goals, 3) some observations and concerns regarding the adequacy and maturity of some of the policies proposed in the Business Plan to achieve the goals of the Northwest Power Act, 4) some observations about the implications of the proposals in the Business Plan for the distribution of costs and risks in region, and 5) some observations regarding the rationale for the changes being proposed by Bonneville and Bonneville's characterization of that rationale. The good news is that the Council believes that Bonneville is now a competitive power supplier and can, with skillful management, remain so in the future. We briefly address fish and wildlife issues raised in the Business Plan. We look forward to future opportunities to comment further.

We note at the outset that many of the features of the Business Plan are features that the Council has supported for some time. For example, the Council called for examination of multi-tiered wholesale rates in the 1991 Power Plan. We have been encouraging greater decentralization of conservation implementation.

The Council has also been actively encouraging approaches to conservation implementation that reduce the cost to the utility system. We are pleased to see these initiatives reflected in the Business Plan.

There is one overriding comment. The goal we all have is that Bonneville remain competitive and fulfill its obligations under the Power Act today and in the future. To accomplish this, Bonneville must remain clear about its fundamental purpose and nature. It is a public agency with broad and long-term public purposes as well as narrower and shorter-term commercial purposes. Bonneville will inevitably face pressures to sacrifice investment for the long term, such as conservation, in favor of short run rate advantages. The intent of the Business Plan must be to make Bonneville business-like in the execution of both its public and private purposes. It must not be to make Bonneville into a business for which public purposes are secondary to its commercial purposes. It is not yet clear that the Business Plan has fully succeeded in walking this fine but essential line. The Council and others in the region are prepared to continue to work with Bonneville in this important task.

Goals of the Draft Strategic Business Plan

The Council clearly supports the stated intention of the Draft Business Plan, which is "to steer BPA through the competitive challenges it faces to successfully achieve its fundamental legislative mandates."¹ A Bonneville that is more effective, more efficient and more responsive to its customers *and* the citizens of the region will be a better Bonneville. It will be a Bonneville better able to fulfill the goals of the Northwest Power Act and Bonneville's other organic legislation. The Council believes that Bonneville is sincere in this aim, and many aspects of the Business Plan should move Bonneville in those directions.

Proposals in the Business Plan also should contribute to reducing the "hassle factor" many experience in doing business with Bonneville. For example, it is a very positive step to organize marketing efforts along customer-segment lines and direct account executives to learn about and represent within Bonneville the problems facing individual customers.

Much of the Business Plan is aimed at instituting the organizational structures, management objectives and accountabilities and changes in internal culture that are necessary for a more effective, efficient and responsive organization. Bonneville should move ahead quickly to implement these aspects of the Business Plan. However, there are other aspects that cause the Council some concern, such as certain aspects of the agency's proposed reinvention of conservation, certain aspects of the tiered-rates proposal and the treatment of fish and wildlife obligations. The Council believes these need further development before implementation, and I will discuss them in more detail later in my testimony.

¹ Bonneville Power Administration *Draft Strategic Business Plan*, June 1994, p. 32

Major policy changes

In attempting to respond to Bonneville's competitive challenges, the Business Plan proposes several key changes in the way Bonneville offers and prices its products and services. Primary among these is tiered wholesale rates, unbundling of products and charging market prices for some of those products. Through these mechanisms, and others, Bonneville proposes to both increase revenues and cut costs. These changes are essential to Bonneville's effort to close the "revenue gap" -- the projected gap between planned revenue requirements and an assumed goal for rates. Tiered rates, for example, are a rationale for Bonneville moving to direct customer financing of conservation and thus reducing Bonneville's costs and borrowing requirements. Charging market prices for some unbundled products is intended to raise more revenue than was possible when sold as part of a package.

There are aspects of these changes that the Council supports, such as the economic efficiency signal Bonneville would send to its customers by adopting tiered rates. Tiered rates should provide a better economic signal to customers of the cost of new resources. They will reduce, but not eliminate, the lost margin experienced by utilities as the result of investments in energy conservation.² Tiered rates will also subject Bonneville to the discipline of the competitive wholesale markets in their acquisition of new resources. Tiered rates should contribute to greater economic efficiency of the regional power system. This is why the Council's 1991 Power Plan called for Bonneville and its customers to investigate and implement wholesale rate designs if necessary to achieve the conservation goals of the plan, that give individual wholesale customers price signals based on avoided costs. A multi-tiered wholesale rate, with the last tier set at avoided cost, could be appropriate.

Bonneville also would give its customers a clear view of the value of its service if some of its products are unbundled and if Bonneville charges market prices for them. This also should result in greater economic efficiency in the use of these products. From that standpoint, the Council supports these changes.

However, if the goals of economic efficiency are to be met, it will be essential that Bonneville be consistent in its application of market principles in pricing its products. For example, the second tier must be priced at the market level or it would not provide an accurate signal, and it would undercut the incentive for customer development of conservation. There are at least two ways in which the second tier might not be market-priced. The first is that Bonneville would use the low cost of some of the federal base system resources to hold down the price of tier 2. The second could occur if, as we expect, new resources added to the second tier are more expensive than the resources already in that tier. If the costs of these resources are just averaged in with those of the resources already

² By "lost margin" we mean the difference between revenues lost and the power costs avoided.

in the second tier, the resulting melded price would be less than the cost of new resources. Thus, tiered rates no longer would send the appropriate market signal. Both of these conditions should be avoided.

Pricing of other products must follow the same principles. For example, unless the pricing of transmission services sends customers a signal about the incremental costs associated with serving incremental loads, customers will not be seeing the true benefits or costs of their decisions to implement or not implement conservation or other new resources. It will not be easy to implement incremental pricing in transmission. However, if Bonneville is to be true to market principles, it must price transmission in way that sends a clear signal of the incremental cost, whether it is wheeling its own power or that of competitors.

Will the policy changes be sufficient to fulfill Bonneville's responsibilities?

As noted above, the Business Plan proposes relying on market mechanisms to a large extent to achieve its commercial and public purposes. While the Council supports many of these means from the standpoint of economic efficiency, there is reason to question whether they are adequate to achieve all of Bonneville's public purposes. In at least one instance, conservation, the Business Plan proposes a mechanism to give assurances that those public purposes will be met. Unfortunately, it is not clear that the proposed mechanism is or can be sufficiently developed in the time frame of the Business Plan. In other areas, no backup mechanism is considered. The Council seriously questions whether Bonneville can move forward on all issues in the Business Plan at this time. Some, such as internal efficiency and organizational improvements, should proceed immediately. Others need more time for development. The Business Plan should recognize this fact and provide place holders for these issues. Three of these are particularly important to the Council. They are conservation reinvention; environmental considerations of power resources and development of renewable resources; and fish and wildlife reinvention. Although not actually a part of the Business Plan, we believe the government corporation legislation is in the same category. Here is a brief discussion of each:

Conservation Reinvention -- Conservation is the foremost area where the Council is concerned about the adequacy of the means proposed in the Business Plan. The existing system of Bonneville-funded, locally implemented conservation is on track to meet Bonneville's share of the regional goal of 1,500 average megawatts by the beginning of the next decade. In 1993, this system delivered approximately 52 average megawatts at a cost to the utility system of 23 mills per kilowatt hour. This far exceeded Bonneville's target for the fiscal year of 39 average megawatts, and it was nearly double the amount of conservation the agency acquired the previous year. The life-cycle cost of this conservation was significantly less than the cost of new generating resources.

Nonetheless, there are concerns about the current conservation system. For example, there are concerns about the impacts on Bonneville's rates, fixed

costs and borrowing requirements.³ Many believe there are significant inefficiencies in Bonneville's administration of conservation. There are also perceptions of inequities in the distribution of conservation costs and benefits -- primarily that customers whose loads are not growing are contributing to the conservation of those whose loads are. As a consequence, Bonneville is proposing to "reinvent" conservation delivery.

The reinvented conservation proposed in the Business Plan consists of:

- Tiered wholesale rates to encourage customer utility funding of conservation;
- Elimination of regional conservation funding to the utilities;
- Offering capital to utilities that choose not to raise capital for conservation. That capital, interest and possibly a Bonneville service fee would be recovered through a Bonneville "energy service charge" to the utility;
- Sale of demand-side management services by Bonneville to utilities and possibly others; and
- Some level of regionally funded support for "market transformation ventures" -- activities intended to change the standard practice in a market for electricity-using facilities and equipment, thereby reducing the cost of efficiency improvements.⁴

There are several reasons why the Business Plan's model of reinvented conservation may not be successful in meeting the cost-effective conservation targets in the Council's plan.

First, all else being equal, most of Bonneville's customer utilities will see greater rate impacts from conservation with the reinvented model than with the current model. This is largely because the reinvented model does not share the costs of conservation with all of Bonneville's customers as is currently the case. The rate increase for many utilities will be small -- 1 to 3 percent. Some utilities could see rate increases of as much as 5 to 6 percent under the reinvented conservation proposal.⁵ In their concern about retail competition -- undoubtedly heightened by Bonneville's focus on competition -- some utilities may be reluctant to commit to greater rate impacts. There are mechanisms available to mitigate

³ Bonneville's draft analysis indicates that continued Bonneville funding of conservation would add approximately 1.5 mills per kilowatt hour to Bonneville's rates between 1996 and 2003.

⁴ An example would be activities like manufacturer incentives, that create a large market for efficient equipment, bring down its cost and ultimately make it possible to establish or improve energy efficiency standards for that equipment. Another would be training for architects and engineers to promote energy-efficient design, construction and operation practices. Research and demonstration activities are also important to transforming markets.

⁵ Draft analysis by Bonneville Power Administration.

those impacts, such as greater use of municipal financing for conservation and alternative incentive structures. However, these mechanisms are also available under the current system of conservation financing.

The second reason that the Business Plan's model of reinvented conservation acquisition may not be successful is that the tiered rate system will not provide a mechanism to give conservation credit for its environmental benefits compared to conventional generation technologies. Unless Bonneville's potential wholesale competitors give consideration to environmental effects, Bonneville will be forced to price second-tier power at a rate that does not reflect environmental considerations. The Power Act's 10-percent credit for conservation finds no place in the tiered rate system.

Third, unless Bonneville incorporates incremental pricing for transmission products, the benefits of avoided transmission investment attributable to conservation will not be captured.

Fourth, the reinvented model also assumes significant savings from utility adoption of tiered retail rates and resulting retail customer conservation and fuel switching. The Council believes this price response will be quite modest. Moreover, if utilities do have a greater concern about their retail rates, there seems to be little reason to believe they are interested in sending a higher rate signal to their customers.

Fifth, the reinvented model proposes using Bonneville's borrowing authority to provide loans to utility customers for their implementation of conservation. It may be important to have such a source of capital available. It is not clear, however, that Bonneville has the legal authority to use its borrowing authority in that way and its borrowing authority is limited.

Finally, Bonneville proposes to sell its demand-side management services to utilities. It is unclear how successful Bonneville can or should be in this enterprise. By selling demand-side services, Bonneville would compete directly with private businesses that offer the same services. It is probably worth noting that energy service companies like these have not been particularly successful in the Pacific Northwest.

Conservation Reinvention Principles -- Reinventing conservation is a challenging and possibly risky proposition. Clearly, the current system of acquiring conservation must be considered successful if Bonneville doubled its acquisition from Fiscal Year 1992 to Fiscal Year 1993 and did so at extremely competitive costs. Moving away from this successful system should be done cautiously. To Bonneville's credit, it has consistently maintained its commitment to achieving the Council's conservation goals. However, for many of the reasons noted above, there are many who have concerns about whether the reinvented conservation model is adequate to meet the cost-effective conservation goals of the Power Act.

For this reason, Bonneville included principles in the Business Plan intended to assure that the conservation would, in fact, be achieved. Those principles are:

- *Overall goal* -- meeting the Council's regional target for all cost-effective conservation savings.
- *Strategies*
 - Regionally supported market transformation activities. Programs and funding levels determined through a collaborative process.
 - Customer-funded efficiency programs consistent with:
 - An integrated resource planning (IRP) commitment in power sales contracts. Integrated resource plans are to be developed by Bonneville's customers using "existing IRP criteria confirmed by a consultative process;
 - A collaboratively developed mechanism to track and provide confidence in conservation accomplishments; and
 - A performance accountability mechanism to be developed collaboratively to reward good performance and/or penalize poor performance.
 - BPA demand-side products and services with:
 - Transition to reinvented conservation on mutually (Bonneville and customers) acceptable schedule and terms; and
 - Bonneville commitment to a "mid-course correction" if necessary, for example, to take steps to ensure that the conservation goals are met.

There are many positive aspects to these principles. Integrated resource planning is good business planning. Done well, integrated resource planning should result in better resource decisions and should help utilities avoid or mitigate risks. This is the reason the Council is working to develop a utility-scale planning model. This would make it relatively easy for individual utilities and utility consortia to use the data and analytical techniques the Council develops in its' planning process in doing their own integrated resource plans.

Similarly, tracking requirements are essential if utilities are to know whether they are spending their customers' dollars effectively. Accountability should be valued by all customers to assure that no one is attempting to secure short-run advantage to the detriment of its neighbors and the region's long-term interests. For example, some are concerned that one utility might forego

investment in conservation to secure a temporary rate advantage over its neighbors.

These integrated resource planning, tracking and accountability mechanisms will be successful, however, only to the extent that Bonneville's customers are willing to accept responsibility for the wise use of the region's federal resources along with the benefits of those resources. In addition, Bonneville must be willing to hold customers accountable when they fail to live up to that responsibility. Sharing in the benefits of the federal Columbia River Power System should also mean sharing in meeting the goals of the Northwest Power Act.

Similarly, market transformation activities hold promise of delivering conservation resources at lower cost to the delivery system. However, these must be more than token efforts. If there are efficiencies to be gained from coordinated, centralized action, Bonneville and its customers must be willing to commit to making them happen. And, if there is the possibility that a mid-course correction will be required, the region must be assured that there is a plan in place and the capability to carry it out exists.

Bonneville and its customers, the Council and others have been working hard to further develop the conservation reinvention principles in ways that are effective and not burdensome to those involved. At this point, however, there is not consensus. This issue must be resolved before the Council can fully support this part of the Business Plan. The Business Plan schedule must not be allowed to override resolution of these issues.

Alternative Ways of Reinventing Conservation -- The Business Plan offers only one option for reinventing conservation. It may be a good option if the reinvention principles can be made to work. However, the Council believes there are also other options that could achieve most of the same ends with perhaps greater certainty. Given the challenge and the risks of conservation reinvention, the region deserves a more thorough exploration of the options. One alternative that deserves analysis includes:

- Continued regional funding of conservation at a significant level, but with utilities paying directly a higher portion of the cost. This would reduce Bonneville's costs and borrowing requirements and reduce the perceived inequities in the distribution of conservation costs and benefits.
- A cost-sharing formula that varies the customer's contribution as a function of load growth and the share of the customer's load served by Bonneville. Utilities with high load growth and/or partial reliance on Bonneville would support more of the conservation cost directly. This would further reduce the perceived inequities.

- Increased reliance on the utilities' municipal bonding capability to finance conservation with Bonneville payment of the regional share of the debt service. This would reduce both the cost of conservation and the pressure on Bonneville's borrowing.
- Increased flexibility for utility implementation. Many utilities can do an excellent job of designing and operating programs for their service territories and may be able to be more cost-effective in their conservation delivery.
- A significant focus on market transformation opportunities. Bonneville can be the catalyst for securing low cost savings.
- Vigorous efforts to reduce Bonneville's overhead. This must be pursued with any alternative.

Such a model would significantly reduce the rate impacts and the perceived inequities in the current conservation model. It also would reduce Bonneville's share of the cost of conservation as well as the pressure on Bonneville's fixed costs and borrowing authority. At the same time, it would preserve much of the benefit of regionally shared costs of conservation development. It should be analyzed.

Environmental Considerations and Renewable Resource Development --

The Business Plan includes very little regarding consideration of environmental costs and benefits and less on the development of renewable resources. These two issues are linked because it is essential to give renewable resources and conservation credit for their environmental benefits if they are to compete fairly with conventional generating alternatives. It is worth noting that the Draft Environmental Impact Statement for the Business Plan concludes that the "market driven" Bonneville has smaller environmental effects than the status quo.⁶ This conclusion rests on assumptions about price-induced conservation and fuel switching, Bonneville load loss and customer development of generating resources. These assumptions are clearly open to question. Bonneville's approach to the environment must be more than simply minimizing the risk that Bonneville someday might face regulation of an environmental impact not regulated today. The Business Plan must address this issue if it is to be effective in carrying out the goals of the Power Act.

Fish and Wildlife Reintervention -- Although not a topic of this hearing, it is important that you know that there is not consensus about the proposals for fish and wildlife reintervention contained in the Business Plan. As in the case of conservation reintervention, Bonneville should move ahead with other portions of the Business Plan while working to resolve the issues associated with fish and wildlife reintervention.

⁶ Bonneville Power Administration, Op Cit. pp 219-224.

Government Corporation -- The question of the government corporation legislation was not addressed in the business plan. The Council clearly supports the goals of administrative efficiency that the legislation is intended to produce. At present, however, there is not consensus in the region regarding other aspects of this legislation. Bonneville should try to achieve the administrative efficiencies it can without legislation while working to achieve regional consensus about this legislation.

Issues Not Developed in the Business Plan

The Business Plan is relatively silent on a number of issues that are at least as critical to Bonneville's business success as conservation reinvention. These include the nature of Bonneville's business relationship with the Direct Service Industries, including the variable rate and the quality and value of the reserves provided by the DSIs; the irrigation discount; and the costs of the Washington Public Power Supply System. The Business Plan proposes a formula for application of tiered rates to the DSIs but provides no details. The question of irrigation rates is not raised at all, nor is the issue of oversight of the Washington Public Power Supply System. Because these issues are critical to Bonneville's business success, we believe the Business Plan should at least lay out a process through which they will be addressed.

Distribution of Cost and Risk

The proposals in the Business Plan will have significant effects on the distribution of costs and risks between customers. Such distribution effects are typically not the Council's concern. The Council believes it is essential, however, that the region fully understand those effects.

The primary distribution effect is from the introduction of tiered rates. Tiered rates largely abandon the concept of regional sharing in the cost and risk of new resource development. Instead, tiered rates imply that costs and risks are born entirely by those requiring new resources. The beneficiaries of this policy change are primarily those whose loads are not growing. This includes some utilities and the direct service industries. There has been one estimate that the cost of that shift to the preference customers is as much as \$200 million annually by the year 2004.⁷

As noted earlier, principles of economic efficiency support a move in this direction. At the same time, however, this represents a significant departure from the principles that have guided regional development in the past. One can argue that today's new resources -- natural gas-fired combustion turbines -- are much less costly and risky than those contemplated when the concept of regional sharing of costs and risks was adopted. They are not risk-free, however. If the

⁷ Association of Public Agency Customers, April 20, 1994.

region is going to move away from this principle, it should do so consciously. We do not believe the Business Plan is as clear about this change as it needs to be.

Unbundling Bonneville's products and charging market prices for some of them will also affect distribution of costs among customers. Perhaps the primary example is the unbundling and market pricing of power shaping services. Because most customer loads are not constant, most require shaping services to match resources to loads. Because Bonneville controls much of the region's hydropower generating capacity, Bonneville is in the best position to provide shaping services. Shaping services are currently part of the bundled Priority Firm service. In the proposed system, those having greater need for shaping services would pay more. Those with relatively flat loads would pay less.

Moves toward unbundling and charging market prices for products like shaping services are consistent with principles of economic efficiency. However, Bonneville has not indicated what it would charge for these services or how it would set rates for the direct service industries, whose loads are essentially flat, in relation to the rates charged to the industrial customers of Bonneville's public utility customers. As a result, it is impossible to calculate the distribution effects of these changes. Without more information from Bonneville, the region is not in position to support or reject this element of the Business Plan.

Finally, we should be clear about the intergenerational effects of the changes being proposed in the Business Plan. The Business Plan portrays a shift to almost total reliance on market mechanisms. Market mechanisms do some things extremely well. They require efficient operation and spur innovation in meeting customer needs. These are positive elements, and the region should make appropriate use of market mechanisms to foster efficiency and innovation. Markets typically do not, however, take a long-term view. Markets typically do not account for environmental impacts unless forced by regulation or tax policies.

The Power Act, in contrast, intended that the region invest for the future as well as for the present. The Act intended that we consider the environment in more than purely a business risk-management sense. The Business Plan, as currently constructed, may well have the effect of shifting costs to future generations -- avoiding near-term investment in conservation and renewables while incurring future fuel costs. It may also have the effect of shifting costs to the environment. The Council believes these effects need to be explored further before the Business Plan is finalized. Bonneville is arguably in the best position of any utility in the Northwest to be competitive in the short run and to make the necessary investments -- in conservation, renewables, the transmission system, information systems and people -- that will insure that it is competitive in the long run as well.

Bonneville's Competitiveness -- Is the Glass Half Empty or More than Half Full?

Mr. Chairman, I will conclude by addressing a subject I mentioned at the beginning of my testimony -- the question of Bonneville's competitiveness. Bonneville's concern about competitiveness motivates most of the changes proposed in the Business Plan. I want to emphasize that the Council believes Bonneville is subject to competition at the wholesale level. The Council further believes that Bonneville needs to recognize these competitive pressures and respond to them. Some significant changes in the way Bonneville does business are necessary.

The Council also recognizes the difficulty of leveraging change in a large organization in the face of internal and external inertia and outright opposition. The degree of support for change seems to vary in proportion to the size of the perceived threat. For Bonneville, the threat is competition. Unfortunately, the Council believes that Bonneville may have overstated this competitive threat in the interest of bolstering arguments in favor of changes called for in the Business Plan.

The Council believes that Bonneville's glass is not half-empty and draining fast, as the introduction to the Business Plan would have us believe. Rather, the Council thinks Bonneville's glass is more than half-full. Bonneville's competitive advantage has been eroded and it does face significant risks. It is, however, still in a good competitive position, and careful management can maintain and build on that position.

The Council is somewhat concerned that Bonneville may have been so successful at telling the bad news in its Business Plan that it may undercut its competitive position -- in essence, creating a self-fulfilling prophecy of uncompetitiveness. Candor with customers and the public can help Bonneville. Overreaction can hurt.

I will briefly discuss three key issues that Bonneville raises as evidence of its eroding competitive position. These are competition from natural gas-fired turbines, certain risks and the possibility of load losses.

Competition from Gas-fired Combustion Turbines -- Bonneville has compared the cost of its power to that from a natural gas-fired combustion turbine to indicate how perilous its competitive position has become. There is no denying that increases in Bonneville's rates and continued low gas prices have seriously eroded the agency's competitive position. Bonneville's rate increases are primarily the legacy of ill-advised investments in nuclear power in the 1970s. Bonneville continues to finance nuclear plants that were never completed. Those are sunk costs that cannot be avoided. They are, however, perhaps illustrative of the need for caution when you think you know what the future will be like.

The other side of the equation has been driven by low gas prices and improved combustion turbine technology. To assess how much erosion has occurred, the Council staff analyzed public information on bids received by Snohomish County Public Utility District (Everett, Washington) in response to its recent request for proposals. In this analysis, the costs of proposed gas-fired combined cycle combustion turbine projects were adjusted for consistency and compared with projections of Bonneville's rates from the 1993 rate case.

For this analysis, staff considered 20-year bid energy price streams for 15 proposals. All but one would be placed in service in 1998. The selection of bids was limited to plants proposed to be financed using municipal bonding. This type of financing is available to many of Bonneville's customers and would likely provide the least costly financing for this type of project.

Bonneville Priority Firm (PF) rates currently provide a full service power product, delivered to the customer utility. To fairly compare bid prices with forecast Bonneville PF rates, the bid prices were adjusted to account for interconnection, shaping, capacity and other services included in the PF rate. Because the market prices for these services are not available at present, Bonneville system cost adjustments from the 1993 Billing Credits program were used to estimate the shaping and capacity prices that would be incurred by a utility seeking to integrate power from a gas turbine into its system. Depending on what Bonneville eventually charges for these services, the results might be somewhat different. The sample of bids analyzed was limited to plants that would be located within the utility's service territory or that clearly included transmission costs in the bid price. Representative substation interconnection costs were added to each bid price. In total, these adjustments added an average of approximately 7 mills per kilowatt-hour to the 20 year levelized nominal bid prices.

Some of the Snohomish bids appear not be based on actual natural gas prices. However, several bids, falling within the average to high price range, appear to be credible proposals. These bids have levelized nominal prices that are 16 to 34 percent higher than the November 1993 medium forecast of Bonneville's PF rate. The adjusted first year (1998) prices of the proposed projects are from 6 to 28 percent higher than the 1998 medium forecast PF rate.

The low end of the credible proposals beat Bonneville's highest rate forecast, but not until about the year 2008. Bonneville's high rate forecast includes a number of very substantial risk assumptions:

- A \$200 million increase in costs due to risks, which are not specified;
- Increased costs for new resources;
- Medium-high load growth; and
- A loss of 250 additional megawatts of firm energy lost as the result of fish mitigation requirements.

Any of Bonneville's competitors will face its own set of risks as well.

Snohomish did receive bids that might pose a competitive threat today. However, we cannot assess the quality of those bids with the information available -- what kinds of gas supply terms these bids contain or the quality of the gas supply contracts. Depending on what happens in the gas market, they might turn out to be very good deals or very bad ones. In general, staff believes this demonstrates that Bonneville remains a very competitive wholesale supplier. While clearly the gap has narrowed, Bonneville is likely to still be the best deal in town.

Bonneville Risks -- Bonneville is uniquely subject to a number of risks that could drive up its rates. One is the risk of unilateral changes in the terms of Bonneville's debt repayment to the U.S. Treasury. Legislation to contain that risk recently has been introduced by Congressman DeFazio and Senator Hatfield. The Council supports that legislation in concept.

The other major risk facing Bonneville is the potential cost of salmon recovery measures. There is the very real potential of additional salmon recovery costs, and the Council by no means wishes to understate those risks. The Council is committed to fulfilling the fish and wildlife obligations of the Power Act and the Endangered Species Act as cost-effectively as possible.

We would take issue with the way in which Bonneville portrays fish and wildlife costs. On page 15, the Business Plan presents a plot of fish and wildlife costs, including foregone power revenues and replacement power costs.⁸ The chart appears to portray exponential growth in the costs but at no point suggests that a significant part of the costs in 1993 and 1994 is related to drought conditions and would not be experienced in normal or wet years. Portraying these costs in this way has the effect of falsely confirming the worst fears of Bonneville's customers. Bonneville's risks of increased fish and wildlife costs are real, but the risk of failing to rebuild declining populations of fish and wildlife in the Columbia Basin are as great or greater. It is unlikely that costs would increase exponentially year to year. It is incumbent upon Bonneville and the Council to provide the customers with realistic estimates of the bounds on future fish and wild-life related rate impacts.

We think it is important to take a broad view in salmon rebuilding efforts in the Columbia River Basin and not focus narrowly on stocks that are being protected under the Endangered Species Act. Yet the region's response to fish and wildlife problems sometime seem to be driven by that one law. The ESA imposes a recovery planning process that is something like emergency surgery. To attack a problem that is so wide-ranging, the region needs a broad approach -- a holistic health care plan rather than emergency surgery to aid specific stocks.

⁸ Bonneville Power Administration, Op Cit.

Bonneville's fish and wildlife activities respond to at least four important legal mandates. The first is the Northwest Power Act, which requires Bonneville to protect, mitigate and enhance fish and wildlife of the Columbia River Basin impacted by hydroelectric dams -- all fish and wildlife, not just those being protected under the Endangered Species Act. The second, of course, is the Endangered Species Act. The third is our nation's responsibility to Columbia Basin Indian tribes under the treaties of 1855. The fourth is our nation's obligations to rebuild naturally spawning salmon runs under the U.S./Canada Pacific Salmon Treaty of 1985.

Efforts on all these fronts can and should proceed simultaneously and in a coordinated way. None of these mandates is less important than any other. They all aim to protect and enhance fish and wildlife populations in the Columbia River Basin, albeit to different levels. The Council and Bonneville must discharge these obligations: the Council in developing the region's fish and wildlife program; and Bonneville in implementing the actions assigned in a full and timely fashion.

Probability of Loss of Load -- It is important to distinguish between losing existing load and losing load growth. With tiered rates, Bonneville is putting itself in a competitive market for load growth. There is every reason to expect that some or many customers may choose to meet all or part of their load growth from sources other than Bonneville. This should not pose a particular problem to Bonneville.

There are several scenarios in which Bonneville could lose existing load. A customer, whether utility or industry, may choose to develop or purchase resources to offset its Bonneville purchases. A direct service industry or a large customer of one of Bonneville's utility customers may go out of business or leave the region. Or, retail competition may result in retail customers of Bonneville losing load to a competitor -- other electricity suppliers or suppliers of other fuels. While all of these are possible or even likely to some degree, it is highly unlikely that the cumulative loss of load would reach anything like "death spiral" proportions. The first tier of a tiered rate system will be protected from some of the costs that drive up rates. That should help maintain Bonneville's competitiveness for a large portion of its existing load. Counteracting the effects of loss of load is the over 200 average megawatts per year of load growth the region is experiencing as well as a competitive but vigorous West Coast market for power.

Some Bonneville customers will choose to acquire resources to displace power from Bonneville. In the past, some utilities chose to limit their dependence on Bonneville when the economics of doing so were much less favorable than they are today. As the earlier analysis shows, the Council thinks that, particularly with tiered rates, the economics will continue to favor serving existing load with purchases from Bonneville, we expect some utilities or DSIs will choose to displace some of their Bonneville load. We do not expect rampant defection.

Similarly, it is likely that some of Bonneville's direct service customers and large industries that buy power from Bonneville customer utilities may cease or significantly decrease operations, for a variety of reasons. These industries are engaged in competitive world markets, and their margins are slim. Clearly, Bonneville and its customers should try to maintain these loads as long as it is economically advantageous to do so. But it may not be possible or even desirable to maintain all those loads no matter what.

Retail wheeling might have an impact on Bonneville's load. In theory, some Bonneville customer utilities could lose load to retail competitors if their distribution lines were opened to all. However, we will have the opportunity to see whether this happens first in California and elsewhere in nation where retail power rates are significantly above the cost of new resources. It is not at all clear that California and others will act affirmatively on retail wheeling. Conditions favoring retail wheeling do not exist currently in most of the Northwest. Our region's embedded costs are low. There will be some niches where retail competition will be present, most likely in the form of competition from other Northwest suppliers. But it will be niches not whole markets. Retail wheeling in the Northwest would require affirmative action by state legislatures, regulatory commissions or local utility commissions. Given that it will be hard to find a significant overall economic benefit in this region from retail wheeling, the Council does not expect a large impact.⁹

With respect to competition from other fuels, particularly natural gas, most of that competition is in the residential sector. A benefit of tiered wholesale rates is that Bonneville's customers will see more directly the costs of trying to retain loads that would be more economically served by other fuels. Utilities can expect to see continued space and water heating load lost to natural gas. However, this will lead to greater fuel efficiency overall and in most instances will be more than offset by other load growth.

Overall, the Council sees the possibility of possible of load losses totaling as much as several hundred megawatts. We believe wholesale load losses in the thousands of megawatts are unlikely. If there is load loss in reasonable amounts, the Council believes Bonneville could sell the power at rates very similar to those it would have charged prior to the load loss. Markets for this power are both inside and outside the region. If callback provisions relating to public and regional preference prevent Bonneville from entering into contract sales that recover adequate revenues, congressional action should be considered to modify those requirements. This would be in the best interest of customers inside and outside the region.

⁹ For a critique of the savings associated with retail competition see, Kahn, Alfred E., "Lets Play Fair with Utility Rates," *Wall Street Journal*, July __, 1994.

Conclusion

In conclusion, the Council finds much to support in the Business Plan. We applaud the emphasis on greater efficiency, effectiveness and responsiveness to customers and other constituencies. Similarly, in principle the Council supports aspects of the move toward greater use of market mechanisms -- tiered rates, unbundled products and market pricing. These moves, if applied consistently, should lead to greater economic efficiency.

However, the Council is concerned that, for a number of reasons, these market mechanisms will not be sufficient to insure the development of all cost-effective conservation. Conservation reinvention principles outlined in the Business Plan could provide the necessary assurances, if they can be satisfactorily implemented. At present there remain significant disagreements among the various parties. These disagreements must be satisfactorily resolved before the Council can support this aspect of the Business Plan. The same can be said about fish and wildlife reinvention.

The Council is also concerned that environmental considerations and Bonneville's role in fostering the development of renewable resources are not adequately dealt with in the Business Plan. The issues here lie largely outside market considerations and must be dealt with in other ways.

The Council notes that there are significant distribution issues inherent in the proposals in the Business Plan. Tiered rates, while positive from the standpoint of economic efficiency, result in a significant departure from the concept of regional sharing of costs and risks of growth. The net effect is that customers with growing loads bear all the costs of that growth. Similarly, unbundled products and market pricing for some of those products will result in a redistribution of costs from the current system. However, without knowledge of what Bonneville will charge for these products and precisely how the products will be defined, it is not possible to assess the magnitude of the redistribution.

More fundamentally, the increased reliance on market mechanisms described in the Business Plan has the potential for transfers of costs and risks to future generations and to the environment. This is a result of the generally short-term perspective of competitive markets and the fact that environmental considerations are typically external to the market. In part, the Power Act was enacted to overcome such market flaws. The Business Plan needs to tell the region how Bonneville intends to deal with the potential for such market flaws in the future.

The Business Plan is relatively silent on a number of issues that are at least as critical to Bonneville's business success as conservation reinvention. These include the nature of Bonneville's business relationship with the Direct Service Industries, including the variable rate and the quality and value of the reserves provided by the DSIs; the irrigation discount; and the costs of the Washington

Public Power Supply System. Because these issues are critical to Bonneville's business construct, we believe the Business Plan should at least lay out a process through which they will be addressed.

Finally, with respect to Bonneville's competitive position, the Council believes Bonneville faces competitive threats, but that these threats can be managed. Overall, while Bonneville's competitive position certainly has worsened, it is still strong. Bonneville will experience some load loss but is unlikely to experience load losses that would lead to a death spiral. If the call-back provisions of public and regional preference prove to be significant impediments to marketing any surplus power at competitive rates, congressional action to modify those provisions should be considered.

Thank you again for the opportunity to testify here today. I would be happy to answer any questions.

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Mr. DEFAZIO. I thank the gentleman for staying within his allotted time. We are going to do an agreement with Representative Smith. We are going to take 10-minute question rounds, so if you can give us the light on 10 minutes, since there is only the two of us at the moment.

There is obviously a question, which I couldn't have submitted to you in writing, which would be to respond to BPA's new schedule, and I guess generally and if we can keep your answers as brief as possible, sort of respond to it generally in terms of addressing some of the concerns you have raised.

Secondly, do you believe in particular, you know, when they are now talking about having the contracts negotiated by the first of the year before we enter into the rate-making, my understanding is there are two cases which have been brought previously against BPA in terms of contracts where it was found that an EIS was necessary. Do you think an EIS would be necessary, and few think it would be necessary, do you think that the so-called EIS that accompanied the business plan would be adequate or could be modified to meet those requirements?

Mr. DUNCAN. Mr. Chairman, I am going to pass a little bit on the question of the EIS, just taking these in reverse order. But I would be happy to have our general counsel review that issue and give you a response back.

Mr. DEFAZIO. I would appreciate that.

Mr. DUNCAN. I certainly expect that if there are significant changes that are still to be made in the business plan and the schedule permits those changes, that an EIS has to be comprehensive enough to include those, and there are still substantial uncompleted portions of this business plan in our estimation. We have some aspirations for completing some of that unfinished business, and the Bonneville's proposed extended review period may allow us some additional margin of time for doing that, particularly the discussions on conservation reinvention which we participated in intensely over the summer still have a ways to go, but it is not impossible for those to be concluded satisfactorily within the schedule that Jack described today. And if that happened, then we would hope that that agreement, and those understandings, could be reflected in the business plan and in the EIS, but we are not there yet.

Mr. DEFAZIO. Okay.

Mr. DUNCAN. We would also, I think, appreciate the additional time for public review. We are trying to squeeze our oversight responsibilities over the business plan in with a major, main-stem rulemaking and a new power plan, and we are, frankly, having difficulty making those time ends meet. So this is going to be of assistance to us, too.

Mr. DEFAZIO. Was the time line on the new plan from the council?

Mr. DUNCAN. The power plan will be adopted sometime next year.

Mr. DEFAZIO. Okay. In your testimony, page 5, the bottom of the page you refer to the reinvented model of conservation and talk about the fact that since we would no longer be sharing conservation costs among all customers, that there would be a rate increase

for some. You discuss a small rate increase, one at 3 percent and some utilities could see rate increases at 5 to 6 percent under the reinvented conservation proposal. You refer to a draft analysis by the BPA. They didn't see fit to provide that to me or to the committee or to make us aware of that despite repeated contacts. So perhaps you could—is that a 5 to 6 percent retail or wholesale rate increase?

Mr. DUNCAN. That would have been a—the analysis led to a retail rate impact. That is the rate impact that affects those retail utilities competitiveness, and so the analysis was done on the basis of retail impacts.

Mr. DEFAZIO. Okay. Do you think it is a—I mean do you think the analysis is adequate? Do you think the impact might be greater, or do you have any way of commenting—it was a draft analysis, I guess?

Mr. DUNCAN. Yes. It is a first cut—well, it is more than a first cut, but it is certainly far from complete, because a lot of pieces of the business plan and of conservation reinvention and the allocation of distribution of cost and benefits is incomplete. So it is an interim indication.

But what it suggests is that in order to accomplish the kind of conservation that the power plan envisions, some utilities under the decentralized model that Bonneville is describing are going to be dealing with retail rate increases, and that is not a reason that they will not do conservation, but it certainly will be a disincentive that is going to be weighed in the process. The more retail competitiveness pressure they feel, the more visible that rate impact is going to be. We have to weigh that.

Mr. DEFAZIO. I understand that. And particularly if we are looking at retail.

Mr. DUNCAN. Yes.

Mr. DEFAZIO. Retail tiered rates, which BPA seems to assume in its analysis. We had a very unfortunate experience with that in Springfield in 1982, in fact. We had riots in the streets or a demonstration at least and burning of electric bills. But let's go beyond that.

Also, you are saying here there is no 10 percent credit for conservation. Well, before I get to that, one thing that has concerned me all along, and a question I put to BPA that has never been satisfactorily answered, is if we send this message through the tiering down to the individual utilities and if the rate impact would be in this 5 to 6 percent range, and if the threat to BPA is that there is going to be all this wholesale power out there basically unlimited, because of it being provided by new producers, independent power producers with long-term, stable extraordinarily cheap contracts, wouldn't my option as a local utility be to say, hey, why do I want to mess around with this conservation stuff and induce a rate increase when I can go out and get this really spiffy firm, cheap IPP power for less?

Isn't that a concern? BPA tells me they will control that through the transmission system; on the other hand, they tell me that they are losing control of the transmission system.

Mr. DUNCAN. I don't think the transmission system is going to be an element of control, a tool of control in this case. I guess if

I can step back from your question a little bit, Mr. Chairman, it is my perspective, and this is from spending 10 years on the private side in the utility business, as well as my time on the council, that in this competitive marketplace, utilities are going to have to figure out how to compete, not just on the basis of a kilowatt hour, because a kilowatt hour is a pretty undifferentiated product. Anyone can sell you one.

And if that is all you are selling, then you are going to compete just on the basis of the cost of it, and some utilities are going to find it very difficult, especially smaller ones, to compete in that respect. Utilities which are smart about positioning themselves for a competitive retail marketplace are going to have to think about ways to add value to that kilowatt hour, and in only a limited number of ways I guess that I can see right now. This is reliability, that that is kind of a negative value added. It is only when that doesn't appear that that becomes a significant marketplace factor and you lose on it.

What is a positive, highly visible marketplace value added factor is if you can help your customer use the power more efficiently. And it is my belief that utilities which are going to compete successfully are ones that do figure out how to add that value to their kilowatt hour that they sell to their customer.

The problem is that near term there is an enormous amount of psychology that says, no, we just have to compete on rates. And the concern I think that the council broadly has is the potential for sacrificing long-term competitiveness, which is what we will evolve to with utilities competing on the basis of service and value added, not just rates; sacrificing that for short-term competitiveness, where they may well be at a disadvantage unless they start cutting costs which are front loaded, capital-intensive. What are those?

Well, those are conservation and renewable technologies. And they are also investments in environmental protection, investments that don't pay off until substantially down the road. So the concern is that the long-range competitiveness of the region broadly, the economic viability of the region, and the competitiveness of individual utilities is going to be adversely affected by this emphasis on being short-term rate competitive.

Mr. DEFAZIO. Okay. And certainly if we are looking at the free market which many espouse here, there are other things that are going to come into effect now. I mean in some cases you can build customer loyalty for your local utility. I mean all of the things that play into private market.

Not everybody has rushed to one of these new alternate phone providers because many say they know AT&T or they know this or that, they will stick with it, even if there is a marginal cost saving. I mean there are going to be a whole host of factors. BPA does recognize that in terms of their customer service reps for the utilities and then obviously utilities are going to have to somehow recognize that more with their individual customers, if we ever get to retail wheeling.

We only have a minute left in this round, so I will try and phrase a brief question that you can answer briefly.

Well, why don't I—at this point I am going to save until the next round. I am going to defer now to Congressman Smith for his round and then I will get back to you.

Mr. SMITH. Good morning, Mr. Duncan. How is your daddy?

Mr. DUNCAN. Pretty good, what we see of him.

Mr. SMITH. Good. Slip him the grip for me, will you?

Mr. DUNCAN. I will.

Mr. SMITH. Thank you. I understand you have been a proponent of drawdowns, even though the core draft system's configuration study says there is no biological benefit to drawing down these reservoirs unless you draw them all the way down to the mud at a cost of \$5 billion. It is my understanding that the Power Council paid Hersa Engineering to shadow the Corps' work; they came up with the same findings. How can you continue to push this plan on the face of the evidence that it does salmon no good biologically?

Mr. DUNCAN. Congressman, to be fair, I think you would also have to characterize me as a proponent of transportation, since the language in the Council's rule, which I wrote substantial portions of, said that there are a number of tools we have to reserve for salmon recovery. One is drawdown, another is transportation, a third I would add would be spill, and that those ought to be analyzed technically and objectively and not as, you know, ideological issues that you support or oppose.

So as far as I am concerned, all of those measures are still on the table; they continue to be analyzed. We have also had reported—we have also had a recent report from National Marine Fisheries that raises some major questions about the efficacy of transportation, and the Council is going to do its own analysis on all of those measures in our current main-stem rulemaking.

The Corps' analysis, in particular, relies heavily on their computed benefits of transporting fish in barges to argue that there is no biological benefit to allowing the fish to go down the river through a drawdown procedure. I think we have some serious questions about the accuracy of those assumptions of transportation benefits for fish, which the HARS report incidentally also raised and supported.

So I wish there were an easy answer to your question that said drawdown is good or drawdown is bad. I think even the Corps will acknowledge, as they did when I asked them about it, that their conclusion with respect to biological benefits was based on their assumptions about transportation benefits, and if you call those into question, then you get a different conclusion from their analysis.

Mr. SMITH. So you want to continue to use drawdown as one of the alternatives to work on as well as spill and conservation, even though you have two authorities that say drawdown doesn't work?

Mr. DUNCAN. Well, let me clarify, Congressman. What we are going to do is to continue to have those as alternatives in our rulemaking, and the Council will conclude, I expect, by November or December of this year, you know, which of those or which combination of those, and which configuration of them, you know, ought to be in the Council's salmon recovery plan. So we have not specified that, for example, lower granite should be drawn down and it should be drawn down to thus and such a level. That is on the table and it is open for discussion in the Council's rulemaking.

Mr. SMITH. Well, I am not going to ask about the spill experience, because that was a catastrophe, I understand. So maybe you are back to your only one left, transportation, which you support, I hear.

Let me ask you about, in your testimony I couldn't determine your position on the variable rate and the irrigation discount. What is your position?

Mr. DUNCAN. Congressman, the Council hasn't specifically considered those and taken a Council position, so I have to differentiate between a Council position and my answer to your question. I have been a supporter—supporter is not the right word, but I have argued that the variable rate made economic sense when Bonneville and the direct service industrial customers negotiated it and agreed to it in the 1980s, and I still feel like that was a correct decision and one that was on balance good for the region.

Mr. SMITH. In 1980?

Mr. DUNCAN. In the 1980s, that is correct. That was a time in which we had a substantial surplus of power in the region, and this was a reasonable way to make sure that we could continue to use that and have a means of amortizing the cost. We don't have that surplus in the region any more, and I have considerable difficulty in justifying continuing that variable rate in the 1990s. But it made sense at the time.

Mr. SMITH. You mean if you don't continue the variable rate, then you are going to put somebody out of business, so we are going to have more energy?

Mr. DUNCAN. No, I am not proposing putting anybody out of business. What I am proposing to do actually is to, what I propose to do would be to let the market work with respect to the DSI's purchasing power from Bonneville, and with respect to the region purchasing interruptible benefits and system flexibility from the DSIs. If it turns out we can work an arrangement where both the region and the DSIs benefit from new contracts, that is what we ought to execute.

If it turns out that we can, for example, buy reserves or flexibility less expensively somewhere else, then I see no reason for paying more for that flexibility and those reserves by buying them from the DSIs. So my proposition would be to let the DSIs, the other customers of Bonneville and other parties, compete to provide those kinds of benefits to the region.

Mr. SMITH. What about the irrigation discount?

Mr. DUNCAN. I think that ought to be on the table, as well.

Mr. SMITH. In other words, you, in both of these situations, you want to change what has been historically the case since the agreement in 1980?

Mr. DUNCAN. Yes.

Mr. SMITH. And the reason is because we don't have enough—we don't have a surplus of energy; is that the reason?

Mr. DUNCAN. That is the beginning of the reason. The other part of the reason is that we are in a much more competitive marketplace, and customers of Bonneville, you know, by executing special deals, can thereby render Bonneville less competitive in the marketplace.

Mr. SMITH. I asked Mr. Hardy about these issues during our last hearing, and I want to reiterate for the record his answers. I was asking him about what the impact was with respect to irrigation discounting, and his answer was about half of 1 percent.

Then on the question of the variable rate, I asked him if they had lost any money, and I am reading from his quote to me. He said, quote, "I guess the point I would make, Congressman Smith, is that in five or six years, since the variable rate was initiated, we have about broken even."

Then he went on to say that when aluminum prices were high, they received more money, \$1 per pound, and basically we have lost that. The aluminum price has plunged and he says we are about even. However, quote, the rate has probably kept on line some plants that otherwise would have gone off line. In that sense, we are probably in a net sense ahead for having instituted the rate and the quote.

Do you have any concern about aluminum plants going off line?

Mr. DUNCAN. I do have some concern about aluminum plants going off line, particularly if they went off line precipitously and left us with a big chunk of power, we would then have to sell at dumb prices, yes, absolutely. And I find nothing to disagree with in Mr. Hardy's statement about the variable rate, retrospectively.

Mr. SMITH. And the question of impact from the irrigation rate, one-half of 1 percent probably is going to change the world in your view?

Mr. DUNCAN. I am reminded of Senator Dirkson's comment about 100 million here and 100 million there and pretty soon it adds up.

Mr. SMITH. I never thought you would ever mention that.

Mr. DUNCAN. I am not above a mercenary comment.

Mr. SMITH. Well, let me ask you about what you think—do you believe that DSIs are subsidized?

Mr. DUNCAN. No. I—well, I think that gets back to my answer about the variable rate. A lot of people will point to that and call that a subsidy for the DSIs. I don't regard it as that. I regarded it at the time and do still as a reasonable business deal between a willing buyer and a willing seller.

Mr. SMITH. Thank you.

Mr. DEFAZIO. Okay. I thank the gentleman. We are being so good here about staying within our time.

Mr. SMITH. Yes. I was on yellow.

Mr. DEFAZIO. Yes. That is great. Unusual in a congressional hearing. Since we are in this area, let me just—I am a little puzzled by something, which is the 7(c)(2) process that BPA goes through, and I am not sure whether you are going to be able to totally explain it or not; Jack certainly can, he is an expert on it.

Mr. DUNCAN. He probably has a chart.

Mr. DEFAZIO. But you know, just from the last rate case document, they come up with what they say is a cost of service total for the aluminum companies, and they say it is 1.324414 million. No, those are thousands. Even in Washington we have trouble with numbers that big. And then after we go through all of the exercise and the adjustments, we come out with a 7(c)(2) delta or that is a theoretical loss of \$357,999,000.

Now, I guess I don't know what that all means, because if—why BPA goes through this exercise, why we come up with a number and we say that this is the division between cost of service and revenues received. You referred to or alluded to the proprietary study, the secret study that was done that shows the net benefit, which I assume included some of the assumptions about aluminum plants going off line, which I am not allowed to see, no one in the public is allowed to see, no one except the aluminum companies and BPA is allowed to see; I assume the Council has not been privy to that study; is that correct?

Mr. DUNCAN. I haven't been privy to that study, I am not aware that our staff has.

Mr. DEFAZIO. That was a two-year total, I am sorry, on the 7(c)(2). So some of the staff has seen the proprietary study?

Mr. DUNCAN. I don't know. I am unaware of it.

Mr. DEFAZIO. Because it is hard to—we will hear it referred to in subsequent testimony; it is just difficult for me to have a group representing strongly their own interests and their own profits come in and say to me we have a study that shows that we are a net benefit to the region and to have BPA who has always had a very close relationship with a number of companies come in and say we have a study that shows a net benefit to the region, but you can't see it. It is hard for a public policymaker.

Mr. DUNCAN. Again, my way of testing that would be to allow the market to test it by seeing whether we could attract those same benefits from other providers at the same or a lower cost.

Mr. DEFAZIO. So you are referring in particular to say values of reserve.

Mr. DUNCAN. Values of reserve, exactly.

Mr. DEFAZIO. I understand that some of the industrial customers would like to bid on providing reserves to BPA—has the Council been contacted by other customers that would like to be included in that process?

Mr. DUNCAN. I think some industrial customers might well be interested in bidding on it. I think some of the utilities might be interested in and willing to bid on it.

Mr. DEFAZIO. I think—I mean since we are getting so free-market oriented here, I think that is a great idea and I would assume that we would open that process up fully.

Mr. DUNCAN. And that would be the best possible way I think to test this benefit, rather than either restore the aluminum companies or Bonneville, my, of the three of us, having to take that on faith.

Mr. DEFAZIO. Well, and the good thing about that is we no longer have to argue over the assumptions which I can go into at great length, you know, the 1982 assumptions and the, you know, the turbines and the interest rates, but we could put all of that argument aside and just say, fine, we are going to do a free market process here, anybody who wants to provide this sort of interruptability can bid. The aluminum companies could do it individually. Some aluminum companies might, rather than acting as a cartel and bidding as a group, which generally defies, you know, my sense of law and free competition in the United States, they could do it individually.

Mr. DUNCAN. I would expect some would be able to make considerably more competitive bids than others, and that would be just fine.

Mr. DEFAZIO. And I assume then the ratepayers would probably come out ahead, or other ratepayers, as good.

Mr. DUNCAN. Yes.

Mr. DEFAZIO. Well, let's get to a couple of other points here. And this is—I don't want to go into this too long, but I share this concern with the Council and I just would like you to—where you talk about the threat of competition and you say the Council believes that Bonneville may have overstated this competitive threat in the interest of bolstering arguments in favor of changes called for in the business plan. Now, is that a position of the Council or is that you?

Mr. DUNCAN. Council staff has done the analysis that is reflected in our written testimony. And I think that there is a general feeling on the Council, although I can't say that we have taken a vote on this or taken a Council position on it, that while it is important for Bonneville to signify, you know, to its own—to its customers and its own employees, that times have changed and the company has—the agency has to be more efficient and competitive, there comes a point at which you start overstating the potential for you to become noncompetitive.

In the business plan, for example, and in a number of the other documents Bonneville has provided to the region, there is a chart in there that shows fish and wildlife costs. And it basically shows those costs shooting through the roof. And in fact, there is nothing technically wrong with that chart, because fish costs have gone up, and in the last two or three drought years, it has been a very expensive proposition. But the inference you draw from the chart is that those costs are going to increase exponentially.

Well, if you have customers who already are concerned about dealing with you and impose a, say, 2 or 3 percent discount on their willingness to deal with you, and you start undermining your competitive position even further by stating that you do have fish and wildlife costs and they are uncontrolled and they are shooting out of site exponentially, chances are that customer's discount is going to go up from 2 or 3 percent to 4 or 5 or 6 percent, and is not going to end up making Bonneville more competitive.

Mr. DEFAZIO. Sure. So basically we are talking about a free market lesson for BPA here, which is you want to get customer confidence, I think that is something that BPA has to pay some attention to. My understanding is there have been some rather extraordinary presentations by BPA on this issue, particularly to Mr. Lovelin's group which seem to engender a great deal of fear.

I guess I would like to just underline the point you made about drought. You know, if we are in a cycle—this is a permanent cycle, we have really big problems in the Northwest beyond just our hydroelectric system, I mean with the potential for our forests or rangelands or anything else. I mean if we don't get back to more than what we consider normal meteorological conditions, we've got some real adjusting to do. But that is the key in terms of the last couple of years.

Mr. DUNCAN. But even if we continue, even if worst case were concluded and we would continue in this kind of serious drought situation, the line doesn't keep going up, you know. It levels off at a very difficult and high level, and we have got to do everything we can to bring it down.

Mr. DEFAZIO. Right. There is a limit to the system, no matter how much you want to tweak it, no matter how much you are an advocate of drawdown or anything else, there is a limit to the system, a realistic limit, particularly when you have to figure there is another year coming.

Mr. DUNCAN. Yes. One of the reasons, for example, that we could continue to examine drawdown as an option is that at some point that extra acre foot of water does become exponentially more expensive and starts to impact refill for both fish and power, and you have to look at ways of using the same water more efficiently, because there isn't more.

Mr. DEFAZIO. Right. On page 10, issues not developed in the business plan, you raised three major points and you might expand on those briefly. That is, the business plan proposes a formula for application of tiered rates but the question of irrigation rates, is not raised at all.

I might disagree with you somewhat. It seems to me with either the DEIS or the business plan they mention something about summer rates, which is a vague reference to me for irrigators, but it would be a change in the system. So I believe it was referenced. And these issues are critical to Bonneville's business success and business plan process. Do you want to expand on that any?

Mr. DUNCAN. I think the point we were trying to make there is that there are a lot of issues out there that have to be addressed in a—an early and deliberate way. We are not going to be able to squeeze all of them into the business plan, given the schedule that it is—that it is on. It was a way, if anything, of underlying the fact that important issues have to be given the time to work themselves out.

Some of them are not in the business plan because they are going to take longer to work out. One of them is not in the business plan because it is going to rely on the Congress to move on it or not, and that is the issue of incorporation. And the point to describing those is that those are also issues that Bonneville is going to have to take up if it is going to thoroughly examine its competitiveness and render itself as competitive as possible.

But they're not going—not going to be addressed in this current business plan, as far as we can tell.

Mr. DEFAZIO. Let me get one more question in quickly before this round ends. I will have a couple more questions the next time.

How much of BPA's projected load loss, according to the Council, is due to customers choosing to meet load growth independent of BPA? For instance, they talk about Clark, 250 megawatt cogent project. I keep asking BPA, have you received a notice from Clark yet? Have you received a notice from Clark or Snohomish that they no longer wish to purchase that power? Because I understand you have to give a two-year notice. There has been no notice.

Are they anticipating load growth or are they actually, do you think, going to say to BPA, No, we will take 250 megawatts less two years hence?

Mr. DUNCAN. I think that the Council's staff analysis and judgment, which I share, is that, as in the past, some utilities have chosen to meet their own load growth partially, and they will continue to do so for a variety of reasons that have to do with diversity of supply, reliability, not just price. I would not necessarily expect Clark and Snohomish would or wouldn't conclude these negotiations. But I am not under any illusions about some utilities choosing to meet some of their load growth and conceivably some of their load through their own resources. Historically, they always have. EWEB has its own resources, Seattle has its own resources. A lot of utilities are partially reliant customers of Bonneville.

So I think the point the Council was trying to make there is that will continue, but that is not the origin of a death spiral for Bonneville. And that the potential loss of future load for Bonneville, if that is how one wants to characterize it, is in the hundreds of megawatts, not the thousands of megawatts; and that there are a variety of other reasons than just wholesale rates why that is going to take place.

Mr. DEFAZIO. Okay. Thank you, gentlemen.

Mr. Smith.

Mr. SMITH. Your statement here regarding the intent of the business plan, you say, must be to make Bonneville businesslike in the execution of both its public and private purposes. Must not be made—it must not be to make Bonneville into a business for which public purposes are secondary to its commercial purposes.

Question—are 470 jobs in The Dalles a social concern to Bonneville?

Mr. DUNCAN. Jack is going to have to answer that directly. Do I think they should be a social concern for Bonneville? Yes.

Mr. SMITH. Good. So do I. You and Mr. DeFazio were agreeing with each other to go to a strictly bidding kind of a program and allowing people to bid on extra energy, wherever they might get it, and it sounded like the Adam Smith purity.

Mr. DUNCAN. No. That was—

Mr. DEFAZIO. It was specifically in connection, if I can interrupt, with the value of reserves and not all new resources. It is one particular benefit that is provided for one industry or company.

Mr. SMITH. Thank you for the clarification, Mr. Smith.

Mr. DeFazio.

Mr. DEFAZIO. Even if he is a relative, I am not that much of an advocate.

Mr. SMITH. I am sure you are not an advocate. The question that I have is simply that in that decision-making process and in the business plan, do you or do you not believe there ought to be a cost benefit kind of analysis with respect to how you handle those kinds of reserves? The point again being that pure—pure competition is one question.

Another question, if Bonneville Power Administration has to have a social half of its body, it can't be so competitive that it drives an aluminum plant out of production in The Dalles just to maintain the competitiveness of Bonneville.

Mr. DUNCAN. Well, Congressman, I also don't want to be in the position of—of advocating a pure rate competitiveness test in the instance of DSIs when I am arguing that that shouldn't be the beginning and end of wisdom in Bonneville's dealings elsewhere in its business world. So, yes, I think there are other considerations, and ought to be, besides simply which—which supplier can provide the least expensive reserves to Bonneville. And considerations, for example, such as building and maintaining a long-term business relationship and, therefore, for a long-term reliability of those reserves is a consideration—ought to be in any business dealing. It was in contract negotiations that I had when I was on the private side.

So if your question is, should this be entirely driven in some abstract world of who can undercut the next competitor by one dollar, no, I am not advocating that at all. But I am advocating opening this up to competition with multiple issues, not just the ultimate dollar cost being a part of that competition.

Mr. SMITH. I think I should not retreat. We are beginning to agree, and that is dangerous.

Thank you.

Mr. DEFAZIO. I thought you agreed with his dad on a lot of things.

Mr. SMITH. His dad had a heavy gavel. I was never asked whether I agreed or not.

Mr. DEFAZIO. And—

Mr. DUNCAN. And I paid for those sins.

Mr. DEFAZIO. Actually, I just saw him. He was here a couple of weeks ago for his class reunion. There are three people, I think, or four left that were in his class. It is fun to see him. He always starts by introducing himself to me as if I don't remember him. I always remember him.

On page 16 of your testimony, second paragraph, at the end of the paragraph, you talk about retail wheeling. There is a lot of hysteria about retail wheeling; there have been a lot of questions about what the legislation adopted by Congress and what Congress intends in terms of wheeling. The California PUC has seemed to back down after threats of litigation from some of their major utilities.

BPA made some assumptions about load losses due to retail wheeling. Do you want to briefly address that?

Mr. DUNCAN. Yes. I think it was appropriate for Bonneville to do an analysis that bounded its likely future with best and worst cases. And, here, I am speaking again for myself, not the Council, because they haven't spoken to the issue of retail wheeling.

But at least what I see of the bold start and pretty immediate slowdown at the California PUC is—is that while retail competition is certainly coming to the utility industry, it is probably not going to arrive the day after tomorrow in all of its form and substance, and that there is time for both utilities to adjust their competitive strategies and, more important from our perspective—our institutional perspective, time for the Congress and State legislatures, public utility commissions and the Council to try to figure out how we protect some of those long-term values that were embedded in the Northwest Power Act, and at the same time, reap the benefits. And

I think, on balance, there will be benefits of a more competitive energy and utility marketplace.

So the short answer to your question is now, retail wheeling is not going to be here in full form immediately; and I guess it is my belief that utilities need to be expeditious but deliberate in figuring out how they are going to respond to it.

The impulse is to respond to it by being able to compete on rates, and that impulse tends to be fed by, particularly, gas companies and IPPs that want to open up and do business in the Northwest and will put a lot of pressure on Northwest utilities to think in those short-term—that short-term frame of reference.

Mr. DEFAZIO. Sure.

Mr. DUNCAN. I think we have a longer period of time to make those adjustments until then.

Mr. DEFAZIO. You made a good case early in the day about the alternate providers. So I subscribed to some Podunk alternate provider, and what I got when I tried to dial long distance was, there was no availability. So one would want to be a little cautious about signing up with an IPP, lest you turn on your heat one day in the winter and they say, sorry, we are out.

It is—there are going to be some really major questions. Is Oregon, Washington, Idaho or Montana, the service territory of BPA, are any of them currently considering rules regarding retail wheeling?

Mr. DUNCAN. I am not aware of any that are. I think, Congressman, that what we will find over the next 10, 15 years is a sharp differentiation in the marketplace and that there will be some customers whose business operations lend themselves to buying big chunks of cheap power that will be looking for those. But there will be a lot of smaller ones.

Mr. DEFAZIO. I understand that. In fact, that has been, at times, one of the unfortunate impacts on the telephone.

Mr. DUNCAN. Right.

Mr. DEFAZIO. When you cherry-pick and pick off the big cost centers, but then who wants to provide the rural electric? That is always the case and that is something that is going to have to be looked at as a package by the regulatory commissions. We will have later testimony basically questioning one of the suggestions made by the task force which had to do with the issue of regional preference.

One scenario BPA has spun out is that we are going to be left with this power and we won't have anybody who wants to buy it at a decent rate. And, in particular, we can't market it outside the region because we have to have the call-back provisions. And the response of the task force was, well, if you could come into a permanent surplus power situation, and given the new marketplace, there is a good rate which can be obtained—in fact, SMUD was in here testifying on another issue; their avoided cost is 37 mills, so they'd be thrilled to be able to bid at about, you know, somewhere in the 30 mill range, I am sure, to buy some long-term power from BPA.

So the task force suggested if there is not a—a firm market in the region, or market at a good price, that we should look outside

the region. And apparently either you or the Council—and if you could clarify that, agreed that there might be some benefits to this.

Mr. DUNCAN. Yes. The Council hasn't taken a position on it, but certainly if Bonneville is sitting on surplus power that it can't market internally and can't market externally because of constraints, removing those constraints pretty much has to be on the table. And I think that the Council would support removing them.

I found it instructive, Mr. Chairman, to sit in a—an advisory committee meeting over at Bonneville a few months ago when one of Bonneville's public customers was complaining about the lack of competitiveness, and that he was just thinking of taking his business elsewhere. And a major private utility representative, who was also sitting in the room, offered out of hand to take his consignment of Bonneville power at his price, straight across, no questions asked. No regional preference problems there, either.

But the deal was not consummated.

Mr. DEFAZIO. Okay. And we will hear from Judy Lamson later, in her testimony on page 5, she refers to Puget Sound Power and Light recently purchasing 500 megawatts of power from new resources at 42 mills. So again, there may be markets within the region. It will be interesting to explore that question in a little more depth.

Two other quick things. Integrated Resource Plans—would you care—I mean, there has been some controversy over how we should do IRPs. There now seems to be agreement in the public power community that it would be desirable to develop them. The question then becomes enforceability.

Mr. DUNCAN. And it is a question that we are still discussing within this energy conservation group that is meeting at Bonneville, between public interest groups, the Council and others. I expect that most of Bonneville's customers, you know, will do some kind of an IRP because it only makes business sense.

I think there is some concern about the assumptions that customers will select, in doing their IRPs, and whether those will reflect the goals of the regional act. And all of that is obviously still under discussion. Where, at least, I am coming down right now is a willingness to focus on the region's contribution, rather than proposing a structure that involves policing every single customer of Bonneville. I don't think that is especially productive. I don't think that is required by the Act.

But what is, I think, essential and productive is that there be a tracking mechanism so that—so that we know whether those IRPs are in fact producing the conservation returns that are consistent with the regional act. And, as yet, we don't have agreement on some sort of credible structure for tracking conservation contributions, utility by utility, and being able to accumulate those and report them to the region.

Mr. DEFAZIO. Okay. The Act, as I recall, gives some price preference or difference for conservation, 10 percent.

Mr. DUNCAN. Yes.

Mr. DEFAZIO. Do you think we should be tracking that as we do all IRPs, or do you think the IRPs should be free-market-cost based?

Mr. DUNCAN. I—I guess the fundamental rule that I think ought to be observed is that those who are partaking of this public value, the river and the electricity that it generates, have reciprocal obligations back to the region. That river doesn't belong to any one economic user group; it belongs to all of us. And there is an obligation to use its production as efficiently as possible.

Mr. DEFAZIO. Okay. In applying the—well, no.

Mr. DUNCAN. And the Power Act sets the terms for its use. It includes a 10 percent benefit for conservation.

Mr. DEFAZIO. Sure. Okay. I think—I will see if Mr. Smith has more questions, now that he has found something he can disagree with you over. I will defer back to Bob.

Mr. SMITH. I think I found something.

Mr. DUNCAN. It is a relief to me, too.

Mr. SMITH. Should utilities who get the benefit of conservation savings bear their cost?

Mr. DUNCAN. Yes. And they do now.

Mr. SMITH. That means that—that means that you believe all that the utilities are bearing equitably the cost of conservation?

Mr. DUNCAN. Well, equity is a hard thing, and I—

Mr. SMITH. Evenly.

Mr. DUNCAN. What?

Mr. SMITH. Try evenly.

Mr. DUNCAN. No.

Mr. SMITH. Let me give you an example.

Seattle City Light pays Bonneville \$40 million a year and gets four million back. That is not true of many other utilities in the Northwest; is that correct?

Mr. DUNCAN. That is correct, yes.

Mr. SMITH. So which utilities benefit and which do not?

Mr. DUNCAN. Well, Congressman, certainly Seattle benefits and EWEB benefits.

Mr. SMITH. An urban area, right?

Mr. DUNCAN. It is an urban area with substantial load growth.

Mr. SMITH. I assume EWEB benefits.

Mr. DUNCAN. Yes.

Mr. SMITH. What about Pacific Power and Light?

Mr. DUNCAN. Pacific Power and Light, probably fits under the regional exchange.

Mr. SMITH. Would you agree that—therefore, that in the new business plan, whoever receives conservation benefits ought to pay for them?

Mr. DUNCAN. Well, Congressman, if we are to continue to be a region and distribute costs and benefits of the system on a regional basis, then there will inevitably be some inequities. Some areas will grow faster and some slower. If we simply decide to divide up the hydro production of the Columbia River and allocate a chunk to each utility, I am sure some would perceive that as a more equitable solution. I don't.

Mr. SMITH. I think the point is, you are pressing Bonneville towards conservation.

Mr. DUNCAN. Yes.

Mr. SMITH. That may be a bona fide public response from your point of view.

My question is, should one utility benefit over another when you are stressing conservation? If one utility does a terrific job of putting forth conservation, why shouldn't they benefit from it?

Mr. DUNCAN. Well, they do benefit from it.

Mr. SMITH. I'm talking in terms of region.

Mr. DUNCAN. And so does the region.

Mr. SMITH. But you just admitted to me that there were some inequities.

Mr. DUNCAN. There are. I admitted there is unevenness.

Mr. SMITH. Pardon?

Mr. DUNCAN. Unevenness. There are lots of inequities in the region.

Mr. SMITH. Unevenness?

Mr. DUNCAN. Yes.

Mr. SMITH. So you are saying that utilities that are primarily in residential areas benefit and those utilities which probably have more commercial activity don't. Is that a fair statement?

Mr. DUNCAN. No, because we have—we have substantial commercial and industrial conservation programs, and those will also have benefits.

Mr. SMITH. I think I will leave you with that ambiguity. But I think I am right, and I will go into this in more depth. And I think we will have some testimony about which utilities benefit from conservation and which do not and why. And maybe the Pacific Northwest Council ought to take a look at that unevenness.

Mr. DUNCAN. Yes. I hope we will, and we are. And one of the reasons that I have supported decentralizing conservation programs and some costs of conservation is to try to get a closer match between costs and benefits. But I still believe that we—and the law describes us as a region where those costs and benefits have to be construed regionally, as well as utility by utility.

Mr. SMITH. Well, somebody makes a decision, obviously. And you are in a position of advisory over Bonneville Power Administration. Somebody makes the decision where to transfer these credits.

Mr. DUNCAN. Yes. And I have made—some of my staff are really uneasy, but I have been supporting a movement toward more closely aligning those costs and benefits at the utility level.

Mr. SMITH. I yield back to Mr. DeFazio.

Mr. DEFAZIO. One quick point on that. My understanding is, we had a record year for regional acquisition of conservation. Last year, was it 53 megawatts?

Mr. DUNCAN. Yes.

Mr. DEFAZIO. 23 mills?

Mr. DUNCAN. Pretty cheap.

Mr. DEFAZIO. Is there any other resource out there we could buy for 23 mills?

Mr. DUNCAN. Not that I am aware of.

Mr. DEFAZIO. So BPA avoided having to acquire 53 megawatts of something that would have cost considerably more than 23 mills. I haven't questioned them recently; a year ago during the February-March time period, my recollection is they were purchasing power close to 30 mills.

Mr. DUNCAN. Somewhere between 30 and 40.

Mr. DEFAZIO. Right. So right now, the way we are acquiring conservation benefits, everybody in the region, because we are acquiring a resource that is so cheap that, you know, it far outstrips anything anybody could require individually and BPA doesn't have to acquire something more expensive and crank it into the rate base and charge everybody more.

Mr. DUNCAN. That is right. The disadvantage and the reason it is an issue in the first place, that two—2.3 cents is a life-cycle cost, but most of those costs are front-loaded and so they put near-term upper pressure on rates, long-term downward pressure on rates. And that is the dichotomy that we are trying to resolve.

Mr. DEFAZIO. Yes. You avoid transmission.

Mr. DUNCAN. Yes.

Mr. DEFAZIO. I mean, there are a number of immediate savings.

Mr. DUNCAN. Yes.

Mr. DEFAZIO. If transmission is going to become a great new functional commodity that BPA is marketing to everybody, then we want to free up as much of it as possible so we can market as many of those parts as possible because we are making so much money doing it?

Mr. DUNCAN. Yes.

Mr. DEFAZIO. Thank you. Call the next panel. Thank you for your excellent testimony.

The next panel will come up. As they are getting arranged, I am going to step out. We will—why don't we take about two minutes here, right? There are certain things that don't—yes, two minutes for the next panel. You don't have to sit down right now. You can stretch, whatever. I am serious.

[Recess.]

PANEL CONSISTING OF K.C. GOLDEN, EXECUTIVE DIRECTOR, NORTHWEST CONSERVATION ACT COALITION, SEATTLE, WA; KEN CANON, MANAGING DIRECTOR, ASSOCIATION OF PUBLIC AGENCY CUSTOMERS, PORTLAND, OR; BRETT WILCOX, PRESIDENT, NORTHWEST ALUMINUM CO., THE DALLES, OR, ACCOMPANIED BY KEN PETERSON, JR., CHIEF EXECUTIVE OFFICER, COLUMBIA ALUMINUM CORP., VANCOUVER, WA; C. CLARK LEONE, MANAGER, PUBLIC POWER COUNCIL, PORTLAND, OR; DANIEL C. SCOTT, COMMISSIONER, MASON COUNTY PUD NO. 1, ON BEHALF OF THE ALUMINUM INFORMATION PROJECT UTILITIES, SHELTON, WA; DAVID E. PIPER, GENERAL MANAGER, PACIFIC NORTHWEST GENERATING COOPERATIVE, PORTLAND, OR; AND, JUDY LAMSON, POLICY SPECIALIST, WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, OLYMPIA, WA

Mr. DEFAZIO. Okay. I thank the panel for their indulgence. I got ambushed on the way to the corner of the building there and had to answer a few questions.

The next panel, rather extensive panel—I apologize for the crowded conditions. This is not the Ways and Means Committee, but you each have a microphone and some water. What I would like you to do is watch the lights and stick to your five minutes. And as I said earlier, any departure from prepared remarks or prepared testimony is always welcomed because I have read the testi-

mony but it is your five minutes. We will go in the order provided for on the sheet. Mr. Golden will be first.

STATEMENT OF K.C. GOLDEN

Mr. GOLDEN. Thank you, Mr. Chairman, Mr. Smith, for inviting our comments on your excellent report.

I first wanted to reaffirm that the Earth is not flat. Those of us who have looked at the evidence and concluded, like the task force concluded and as the power planning council indicated this morning, that Bonneville is not in imminent danger of massive load loss, have been accused by some of burying our heads in the sand and ignoring the new competitive realities of the electric utility industry. I am here to say we are acutely aware of those realities. We stand ready, willing and able to help Bonneville accommodate and adapt to those realities and fulfill its mission in view of those realities.

Having said that, you still have seen no credible case made for an imminent massive load loss or a death spiral. I think the task force's conclusion on that subject was correct, and I think the testimony today of the Washington Utilities and Transportation Commission will put to rest any fear that there is any present or foreseeable lack of demand for the output of the Columbia River system. The Earth is not flat but the sky is not falling.

Second, I wanted to indicate that the draft business plan's conservation reinvention departs quite markedly under Congress's direction, under the regional act and this task force's recommendation to acquire all cost-effective conservation. Quite apart from the reinvented conservation program will meet its goals, it starts by aiming to deliver annual savings in every year after 1996, significantly lower than the Power Planning Council's annual targets and Bonneville's own 1992 targets from its conservation implementation plans.

That is what happens if it works. And I think that the task force's grave concerns about whether it will in fact work are very well placed. I want to reaffirm that we are ready and able to help Bonneville adapt to new realities. Tier grades was, after all, I suppose it is time to admit it, our initiative. We have worked very hard to help Bonneville develop a conservation approach that conforms to this task force's recommendations and the Senate appropriations language. As the Council indicated, Mr. Duncan indicated, we have a long way to go.

In the effort to move that discussion forward, I have included in my written statement a discussion paper called Rethinking Conservation, Reinvention Revisited that I think incorporates much of what is useful, insightful information in the conservation reinvention proposal, while preserving the essential features of a successful existing system, a system that is producing the only cost-effective resource that Bonneville has ever delivered in significant quantities. I hope that that proposal addresses some of the concerns that Mr. Smith raised this morning about equity.

I guess I want to conclude by just thanking you all for redirecting Bonneville toward the crucial mission, the central mission of Bonneville, which is defined in the purposes of the regional act. BPA assertions to the contrary notwithstanding, this discus-

sion is about ends, not just means. The business plan treats commercial success as Bonneville's primary goal and the Act's purposes as the statutory constraints among which Bonneville must now begin on its way to that Holy Grail of commercial success.

I think the business plan treats the regional act and its purposes as a cost of doing business. We think it is the reason for doing business. It is not a penalty that handicaps Bonneville relative to its competitors. It is the prize that sets Bonneville above its competitors as an uniquely valuable regional institution that provides a lot more than kilowatt hours. We think the regional act was a promotion from the role of simply commodity broker to the role of steward of the Columbia River's bounty and advocate for a brighter energy future for Bonneville. I think it is time for Bonneville to accept that promotion.

I think Bonneville is eminently capable of rising to the occasion and accepting that promotion, but not if it keeps thinking of itself as a competitively challenged business. I would urge Bonneville leaders and this task force to think of it instead as a public service organization with the unique ability and the enormous resources to provide affordable energy service, environmental integrity and sustainable economic development opportunities to the nine million citizens in the Northwest.

Thank you again for your continuing, persistent and very insightful oversight.

Mr. DEFAZIO. I thank the gentleman for being so brief.

[Prepared statement of Mr. Golden follows:]

Statement of K.C. Golden
on behalf of the
Northwest Conservation Act Coalition
before the

House Committee on Natural Resources
Task Force on the Bonneville Power Administration

August 9, 1994

Thank you Mr. Chairman and members of the Task Force for soliciting our comments on your report. On behalf of the Northwest Conservation Act Coalition and its 70 member organizations, I want to extend our sincere appreciation for both the quality and the persistence of this Task Force's oversight activities. Your continued diligence is the region's greatest hope for realizing the bright promise of an economically and environmentally sound energy future that Congress articulated in the Northwest Conservation Act of 1980.

Let me begin by congratulating you for the thorough and insightful analysis you provided in "BPA at a Crossroads." We particularly appreciate its clear focus on the enormous public policy implications of BPA's "competitiveness project" and its unwavering insistence on putting the public interest first. The analysis and recommendations in Section II are particularly compelling, and we support them wholeheartedly.

We particularly support your proposition at the beginning of recommendation 9: "Those who benefit from the power provided by the Columbia River hydroelectric system bear a responsibility to further the efficiency goals of the Act." We believe integrated resource planning will result in more sensible resource acquisitions, but we wish to emphasize that 130 individual IRPs do not sum into a plan for the prudent management of the Federal Base System. That plan can only be developed regionally, by the Council. We are still a region; we'll still be a region with tiered rates; and we're better off because we are a region. Since the Council's Plan is the best hope for coordinated management that maximizes the benefits of the FBS, all who share those benefits should be required to implement the Plan - and in particular, to achieve its conservation targets - as a condition of service. The relative ease with which BPA and the region's utilities surpassed the Council's targets last year - notwithstanding severe budget constraints - should put to rest any fear that the Council's goals are unreasonably ambitious.

Section II of the Report reaffirms the region's priorities and begins to straighten the record on BPA's competitive prospects. Section IV offers an impressive list of costs incurred for reasons having little to do with BPA's core mission - costs that should be eliminated before BPA even contemplates curtailing the efficiency and fish recovery programs that lie at the heart of its statutory mission. We note that these costs are significantly understated, because they rely on conservative WPPSS estimates of mothballing costs, and because they do not take account of the full range of subsidies to the DSIs. The miscalculation of the value of reserves provided by the DSIs (approximately \$40 million annually) represents less than a quarter of the annual difference between the cost that BPA incurs to serve DSI loads and the revenues collected from them during the last two-year rate period. We find it conspicuous that BPA makes frequent (and often inflated) reference to the

costs of fish and conservation programs as principle drivers behind its alleged loss of competitiveness, yet almost never publicly reveals (let alone bemoans) the unproductive nuclear costs and industrial subsidies that clearly represent the agency's most serious financial liabilities.

BPA's Draft Business Plan is patently inconsistent with the Task Force's recommendations. It uses different assumptions, arrives at diametrically opposed prescriptions, and only grudgingly acknowledges the report's clear admonition to fulfill the mission that Congress articulated in the Regional Act. Two inconsistencies are particularly noteworthy.

First, despite the Report's well-founded conclusion that BPA is not in imminent danger of massive load loss, the draft business plan is crafted in large part as a response to the specter of the death spiral. To the extent that BPA's actual competitive prospects are analyzed in the draft business plan and accompanying environmental impact statement, the evidence suggests that significant load losses are exceedingly unlikely. BPA's rates remain substantially lower than the cost of alternative resources. The hypothetical "30 mill combustion turbine" to which some observers compare BPA rates is not an appropriate comparison, for at least four reasons:

- 1) Cost estimates as low as 30 mills/kwh assume full baseload operation, while purchases from BPA are seasonal and diurnal in nature. Typical utilities have annual load factors on BPA of around 50%. If the fixed costs of a combustion turbine costing 30 mills/kwh at full baseload operation are spread over a 50% annual load factor, the cost of energy produced rises to over 40 mills/kwh, over a third higher than the comparable BPA rate.
- 2) Line losses incurred during generation and distribution generally add about 5 mills/kwh to the cost of power from a combustion turbine.
- 3) The Northwest Conservation Act requires BPA to give a 10% preference to energy efficiency, in part to reflect the environmental impacts of generating resources. Substituting the quantified estimates of the air impacts associated with burning gas (and occasionally oil) in combustion turbines used by most states which quantify these impacts would probably yield an estimate higher than 10%.
- 4) The economic and environmental risks of the existing system are now well-known and captured in BPA rates. The economic and environmental risks associated with combustion turbines are only beginning to emerge.

Taken together, these factors drive the cost of a "30 mill" combustion turbine to near 50 mills, or almost twice the current BPA preference rate.

The testimony of the Washington Utilities and Transportation Commission, which regulates Washington's investor-owned utilities, clearly shows that the market value of BPA's power is significantly greater than the revenues BPA collects from many of its customers. There is not now, nor will there be in the foreseeable future, any shortage in demand for the output of the Columbia River System.

Furthermore, BPA's proposed "market-driven" alternative will not significantly reduce projected load losses. Given the extraordinary lengths to which BPA proposes to go to protect its competitiveness, we find it remarkable that BPA has not documented a significant problem, and that its proposed solution has very little effect. In concurrence with preliminary Power Council analysis, the Task Force concluded that BPA is wise to undertake cost control measures, but that it faces no imminent threat to its competitiveness. We hope that the Task Force will work with the Council to develop a more definitive analysis of this important issue.

Second, the draft business plan departs radically from the Task Force's recommendations on energy conservation. The draft and accompanying DEIS directly and disingenuously link BPA's investments in cost-effective energy efficiency with its hypothetical loss of competitiveness. Based on this spurious link, BPA proposes to replace its successful conservation investment program with an alternative that even Randy Hardy describes as "a high risk" strategy.

Conservation is the most economical energy resource available to the region, but it is not free. BPA cannot fulfill the Regional Act's and this Task Force's directive to "acquire" conservation while pursuing the draft business plan's goal of making conservation a net revenue producer. Even if BPA's proposed conservation reinvention worked, it would, by BPA's own estimates, produce annual conservation savings significantly lower than the Council's targets and the planned savings under BPA's 1992 Conservation Implementation Plan. The draft business plan aims for underachievement.

We have been working with BPA and its customers to devise a program under which the customers would assume much of the responsibility for making the efficiency investments that BPA proposes to drop. The Senate Appropriations language that stipulates the terms under which this transfer of responsibility would be acceptable form the framework for these discussions. Although we remain gravely concerned about the implications of dramatic reductions in regional conservation investment, we are working in good faith to develop a system which meets the standard set forth in the Senate Appropriations language. Independent verification of energy efficiency achievements and a meaningful, performance-based accountability mechanism are, as the Senate language suggests, critical features of any credible alternative to a system that is presently performing well. They are,

in fact, crucial features of any effective regional conservation effort, "reinvented" or otherwise.

While BPA's proposed conservation "reinvention" is in many respects antithetical to the Task Force's findings and recommendations, it contains one crucially important initiative. BPA has accurately concluded that if the region's energy efficiency goals are going to be reached, all who share in the benefits of the Federal Base System must assume responsibility for reaching them. To his credit, Randy Hardy has endorsed this concept vocally. It remains for BPA to develop a system which accurately aligns the allocation of Federal Base System benefits with beneficiaries' performance in maximizing the value of those benefits to the present and future citizens of the region. In negotiating new Power Sales Contracts, BPA has a golden opportunity to develop such a system. The renegotiation of these contracts represents the unique moment at which BPA can ensure that those who enjoy the fruits of the federal investment in the Columbia River System bear the responsibility for maximizing the system's productivity. These contracts allocate what is arguably the region's most valuable public resource. Therefore, they must contain provisions which allow third parties to pursue and protect the vital public interest in efficient use of the FBS as a condition of service.

The attached discussion paper, "Conservation Reinvention Revisited," is an effort to incorporate the useful insights of BPA's proposal into a more comprehensive system that preserves most of what is working in the existing model. While we are pleased with results of last year's conservation effort, we are by no means complacent. We offer "Conservation Reinvention Revisited" in the spirit of building on BPA's singular success in delivering cost-effective energy savings to the regional grid.

In many crucial and substantive respects, the draft business plan departs from this Task Force's direction. These inconsistencies represent more than a disagreement about strategy. Contrary to BPA's assertions, the draft business plan is not merely about means. While it nods dutifully to the Regional Act's directives, it does not embrace them as BPA's core mission. It treats Congress' direction as a series of statutory constraints through which BPA must navigate, not, as the Task Force report recommends, as "the yardstick by which Bonneville's new Marketing and Business Plans should be measured."

The most disturbing part of BPA's "reinvention" to those of us who believe passionately in BPA's public service mission is that when BPA leaders talk about what separates the agency from a business, they talk as if their public service mission makes them somehow less than a business, a business with a competitive albatross around its neck.

The draft business plan treats the Regional Act as a bothersome cost of doing business. We're saying that the Act is the reason for doing business. The draft business plan focuses primarily on commercial success and looks at the

Regional Act's mission as an impediment to that success. We're saying that the Regional Act's mission is the definition of success. The Act is not a penalty that handicaps BPA relative to its competitors, it's the prize that sets BPA above its competitors as a uniquely valuable institution that serves the region with a great deal more than kilowatt hours.

We've heard Bonneville leaders say recently that what's at stake in the reinvention is BPA's very survival, as if that was the most important goal we can imagine. It is not.

An economically and environmentally affordable energy future; healthy Northwest ecosystems; democratic control of the region's energy and natural resource decisions; efficient use of our precious endowment of inexpensive hydropower; affordable basic energy service for all; far-sighted stewardship of the Columbia River's bounty: these goals are far more important to the people of the region than BPA's commercial fortunes.

BPA appropriately maintains that these goals are intertwined - that without commercial success, BPA won't be able to accomplish any of the Regional Act's purposes. We agree that they are related, but we would describe the relationship somewhat differently: Unless BPA devotes itself as passionately to these goals as it has to "competitiveness," there is no reason for it to exist as a public entity.

The Regional Act defined a crucial job for BPA to do and this Task Force has compellingly reaffirmed the importance of that job. The Act wasn't a punishment; it was a promotion from the role of a commodity broker to the role of steward of the Columbia River's bounty and advocate for a brighter energy future. BPA can and must accept the promotion that Congress gave it in 1980 and that you have offered once again in "BPA at a crossroads."

Bonneville is capable of rising to the occasion, but not if it keeps thinking of itself as a competitively-challenged business. Instead of looking of BPA as a business with a monkey on its back, we'd urge you to think of it as a public interest organization, like NCAC, with an ambitious mission, and unlike NCAC, with an enormous revenue-producing endowment.

Think of it, not as a business, not as a government agency, but as a committed team of public interest advocates with the unique ability and enormous resources to provide affordable energy service, environmental integrity, healthy fisheries, and sustainable economic development opportunities for 9 million people.

We plan to submit more detailed written responses to your pre-hearing questions in the near future. Thank you for your continuing deliberations and oversight, and for the opportunity to participate.

ATTACHMENT TO TESTIMONY OF K.C. GOLDEN
House Natural Resources Committee, BPA Task Force
August 9, 1994

NCAC Discussion Draft

RETHINKING CONSERVATION "REINVENTION"

BPA's proposed conservation "reinvention" begins from the premise that regional acquisition of saved energy is a failed model. Citing competitive threats and customers' unwillingness to "embrace conservation as a resource," BPA proposes to induce conservation through a combination of a modest short-term marginal cost signal at the wholesale level, targeted marketed transformation activities, and a DSM product line that BPA would sell to customers.

Many of us who have been instrumental in building the Northwest's successful energy efficiency programs see the situation somewhat differently. Last year's conservation performance (135 megawatts saved regionally, and over 50 megawatts saved on the BPA system) clearly reaffirmed the proposition that energy efficiency can be acquired as a resource on a large scale. Conservation is, in fact, the only resource that BPA has ever acquired cost-effectively in significant quantities. Last year's success prompted the U.S. Senate to observe, in its FY 95 Energy and Water Appropriations report (103-291), "[The] combination of regional funding and locally tailored programs achieved impressive savings at a modest cost in 1993." The recently-completed work of the House Natural Resource Committee's BPA Task Force confirms that conservation is not exerting significant upward pressure on BPA rates, and that BPA can remain competitive without reducing its conservation investments.

Based on the dramatic recent success of the region's conservation effort, the region and BPA have much to be proud of, but no reason to be complacent. Continuing efforts to improve the efficiency and effectiveness with which we deliver saved energy to the regional grid are clearly in order. However, effective reform should build on success, rather than scrapping a highly successful approach and starting over. NCAC embraces innovation, but we are wary of "reinvention" that dismantles first and reinvents later. In the spirit of building on success, we offer the following thoughts on how to improve the region's conservation performance.

Premises and principles

While we believe that BPA's conservation "reinvention" approach is founded on some unsound premises, we acknowledge and support BPA's effort to rise to the enormous challenges posed by industry restructuring. In view of those challenges, and in view of the urgent necessity to make the most of the Columbia River's increasingly constrained output, we begin from the following premises:

• We are still a region; we'll still be a region after tiered rates; and we're better off because we're a region. Sound management of the Columbia River System is fundamentally a regional enterprise. It cannot be accomplished as the sum of the independent activities of BPA's more than 130 wholesale customers. Tiered wholesale rates will help to communicate the economic consequences of action or inaction at the margin, but it will not eliminate regional interdependence. Our ability to manage the system

autonomously on behalf of the region's citizens depends on our performance in managing the system wisely. Maximizing the productivity of the federal investment in the region's power system is our collective challenge. It is also an enormous opportunity, an opportunity that the Regional Act urges us to seize in its first purpose:

"to encourage, through the unique opportunity provided by the Federal Columbia River Power System - conservation and efficiency in the use of electric power, and the development of renewable resources within the Pacific Northwest." (PL 96-501, Section 2.(1))

We begin from the premise that as the operator of the world's largest coordinated hydropower system and transmission grid, BPA has an unparalleled capacity to make efficiency investments, offset lost revenues by marketing saved energy, and increase the value of the FBS by maximizing the energy services it produces.

• **The primary goal is to minimize the total, life-cycle cost of providing energy services, while avoiding unacceptable rate impacts.** The region's considerable experience in developing conservation suggests that the resource can be acquired effectively with only modest rate impacts. BPA's estimates of the impact of continued conservation investment on wholesale rates (approximately 1.2 mills over the 10 year period) is well within any reasonable assessment of what is possible and acceptable in an increasingly competitive wholesale power market. Furthermore, because of its considerable marketing advantages, BPA is in the best position to minimize rate impacts by marketing the conserved product. We strongly support BPA's efforts to eliminate unnecessary costs and subsidies. As the BPA Task Force report concluded, Bonneville can maintain its status as the wholesale power provider of choice while sustaining necessary levels of energy efficiency investment.

• **Marginal cost pricing is good economic policy, not a panacea.** Regional and national experience demonstrates conclusively that economically efficient pricing increases the effectiveness of conservation programs, but in no way eliminates the need for them. As the BPA Task Force concluded, "[A] tiered rate - by itself - is not likely to provide an incentive sufficient to cause utilities to make substantial direct investments in conservation..." Persistent market barriers remain, leading to chronic failure to capture cost-effective energy savings even in places where retail rates are two or three times higher than they are in the Northwest. Energy efficiency is the cheapest resource available, but it isn't free. There is no substitute for investment. The 20 mill difference between the likely Tier 2 rate and the Council's estimate of the regional avoided cost is a partial measure of the opportunities to reduce the region's energy bill that will not be captured by individual utilities responding to a tiered wholesale rate.

• **BPA and electric utilities generally will continue to play a uniquely valuable role in the increasingly competitive power industry.** Unlike any of their emerging competitors, electric utilities are singularly equipped to provide customer services that are likely to become more valuable as the market diversifies. Electric utilities have a pronounced competitive edge in providing increasingly important products such as energy portfolio management, risk mitigation, and efficient energy service. Because it manages one of the region's most important economic and environmental assets, Bonneville has an especially crucial role in maximizing the value of those assets to the region as a whole - a role that no other existing entity or combination of entities can play.

• **BPA is wise to get in front of industry changes, but it should not panic.** BPA remains, by a significant margin, the lowest cost wholesale power supplier in the West. Competitive challenges are real, but BPA is not in imminent danger of massive load

loss. BPA can and should reduce costs in many areas where it is now either inefficient or where it is incurring large costs that are not directly related to its core mission, as defined in the purposes of the Regional Act. It can do this deliberately and soberly, without reducing conservation investments. The earth is not flat, but the sky is not falling.

"Reinvention" insights

We start from somewhat different premises, but we applaud some of the key insights of BPA's conservation "reinvention" effort.

- **Long-term conservation success requires local initiative.** Energy efficiency efforts must respond not only to regional needs, but to the challenges and opportunities of local communities and the utilities that serve them. Without sacrificing regional conservation performance, local utilities should have greater discretion to implement efficiency efforts in the manner that responds best to unique local circumstances. And while the region should encourage creative adaptations to local needs, local utilities should accept responsibility for delivering the regionally cost-effective conservation that is available in their service territories. As a region, we need to be firmly accountable -- not to some arbitrary outside authority, but to each other - for the wise management of our most valuable collective asset: the Columbia River System.

- **Real and perceived inequities in the distribution of conservation expenditures need to be addressed.** We note that, compared to other resource acquisition payments, conservation payments are distributed relatively evenly throughout the region. We would not expect those payments to be distributed perfectly evenly unless the resource were distributed perfectly evenly. Nevertheless, with the introduction of tiered rates, we should reexamine the distribution of conservation funding, both among retail utilities and between retail utilities and BPA.

- **BPA and its customers can and should reduce conservation overhead.** BPA and the region's utilities are presently delivering conservation cost-effectively, but we can do better. Efficiency programs are still saddled with some unnecessary costs and administrative burdens. Some overhead is of course necessary to ensure solid evaluation and performance. But duplication, second-guessing, and overprocessing can be significantly reduced.

- **We should focus on performance and reward it.** Our ability to manage the Columbia River System autonomously and keep its benefits in the region depends on our performance in managing the system prudently and efficiently. Therefore, distribution of the system's benefits within the region should be at least in part performance-based rather than entirely entitlement-based.

From here to there: steps toward improved conservation performance

Starting from somewhat different premises and sharing many of the same goals, we would like to sketch out some of the features of an improved approach to regional conservation. Our intent is to preserve the best of what we have built over the last decade, while incorporating some of the key insights of BPA's conservation "reinvention." Again, these features assume that we are better off building on success rather than starting over.

- 1) **Adjust conservation cost-sharing to more closely reflect utilities' resource needs and reliance on BPA.** This will address equity concerns and adjust for growth while more closely approximating actual costs and benefits of conservation for the regional system.
- 2) **Increase retail utilities' proportion of overall conservation investment relative to BPA's to reflect the increased local value of conservation in a tiered rates environment. Do not diminish aggregate conservation investment as long as cost-effective conservation opportunities remain.** This preserves BPA's indispensable role as the primary regional conservation investor, while bringing more of the costs and rewards to the local level. Safeguards will be necessary to ensure that aggregate conservation investment is sufficient to capture all cost-effective savings.
- 3) **Reduce the total cost of energy efficiency programs by capitalizing on the customers' access to favorable tax-exempt financing.** Third party financing agreements - in which BPA backs locally-issued debt - have been successfully pioneered by a few utilities. These agreements reduce pressure on BPA's financial relationship with the federal government and reduce the cost of conservation by lowering financing costs. This approach should be used more widely.
- 4) **Reduce the unit cost of saved energy and ensure that conservation targets do not become caps by preserving the budget flexibility to take advantage of unanticipated opportunities between rate cases.** While exceeding annual targets, the region missed significant opportunities to capture cost-effective conservation this year due to budget constraints. The cost per unit of saved energy can be reduced significantly by ensuring that fully operational programs reach all willing participants. Reducing backlogs and reducing the waiting period for successful programs will lower unit costs by allowing fixed costs to be spread over a larger number of kilowatt hours and by encouraging greater participation.
- 5) **Continue the trend toward providing increased local flexibility in program implementation.** Energy Smart Design is a good working example of a regional program that offers enormous local discretion in implementation. We should continue to investigate approaches in which the utility delivers an agreed-upon quantity of savings and is free to achieve that level with maximum local discretion.
- 6) **Forge a clear, contractual link between efficiency performance and allocation of FBS benefits to wholesale customers.** Current tiered rates proposals allocate FBS benefits exclusively on an entitlement basis. However, our ability to control the benefits of the regional system will be based on our collective performance, and the size of those benefits is in part a function of efficiency achievement. Therefore, our allocation of those benefits should be based, at least in part, on customers' independently evaluated efficiency performance. BPA has a statutory responsibility to achieve regional

conservation goals, but the implementing agencies must share that responsibility. To maximize the total value of the system to the region, a significant portion of its value should be reserved for allocation to those customers who enhance the system's value by delivering saved energy.

7) Develop and implement an ambitious market transformation program that uses BPA's formidable market leverage to institutionalize efficiency in technology development, construction practices, building operations, and industrial processes. BPA has appropriately recognized its ability to "push" efficient products through the distribution chain, as well as "pull" them through from the end-user. The full range of methods to capture efficiencies at lower cost by intervening earlier in the research, development, production and distribution phases should be employed. This should both expand the total conservation resource (by bringing in measures that would not have been cost-effective if they had been acquired through end-use incentives), and lower the cost of acquiring the resource overall (by intervening earlier, when smaller investments can have a bigger impact).

8) Identify and remove barriers that constrain BPA's ability to reap the full market value of its efficiency investments on behalf of the region's consumers. Lost revenue remains one of the principal deterrents to utility-sponsored energy efficiency initiatives. BPA's formidable marketing advantages should allow it to offset lost revenue by marketing saved energy at or near its full market value. Legal and institutional barriers to such marketing should be re-examined and, if possible, removed. Bonneville's capacity to eliminate or substantially mitigate lost revenue impacts is vastly superior to that of its customers.

We offer this alternative approach in the spirit of regional cooperation, a spirit that has enabled us to deliver impressive energy efficiency results in recent years. We offer it with a keen recognition that the industry is changing rapidly and in ways that challenge us to improve conservation delivery systems.

However, we are also deeply concerned about the rapid erosion of a conservation infrastructure that took a decade to build and delivered admirable results last year. This infrastructure has already begun to contract significantly, because of a widespread perception that BPA's "reinvention" will entail significant and rapid net reductions in energy efficiency investment. Virtually all of the energy service leaders in the private sector have significantly reduced their workforces or left the region altogether in the last year.

Only a year ago, the Regional Conservation Acquisition Task Force and others were working feverishly to ensure that private firms and educational institutions would quickly develop a qualified work force to meet the healthy demand for energy efficiency services. One of the principal obstacles to that effort was the perception that utility investment commitments are unreliable, and that BPA could suddenly ramp down its programs, as it did in 1984. Now, BPA is proposing to do just that. Ironically, Bonneville also proposes to pick up much of the slack by developing its own energy service marketing apparatus. That apparatus exists now in the private sector. BPA should utilize it, not supplant it.

We remain eager to explore even better ways of delivering the enormous benefits of energy efficiency to Northwest consumers. But we believe firmly that a credible effort to do a better job begins from a strong appreciation of how much we have accomplished, as well as a keen awareness of how much remains to be done.

Mr. DEFAZIO. Mr. Canon.

STATEMENT OF KEN CANON

Mr. CANON. Thank you, Mr. Chairman, Mr. Smith. I represent a group called the Association of Public Agency Customers. It is a group of large industries that buy their full requirements essentially from public agencies.

I guess our view is that competition does exist for Bonneville, regardless of the current number, as far as rates. I think the question is of a competitive Bonneville future.

We believe that utility customers aren't waiting for Bonneville potentially to become uncompetitive. I know that my industrial members certainly aren't waiting. They are moving to diversify, and we expect that to happen and continue to put pressure on Bonneville, as well.

For many, Bonneville's uncertainties are viewed as larger or at least equal to new resource uncertainties, those new resource uncertainties being mostly gas costs and supply. Those are issues that industries are very familiar with, and utilities are becoming more familiar with, and they feel like they can deal with those contractually.

We believe that Bonneville is properly concerned about loss of revenues and the ability to fund their responsibilities into the future. Our analysis shows that Bonneville is likely to become in the realm of uncompetitive by the end of this decade. What that shows—again, our rate analysis shows a series of double-digit rate increases facing Bonneville if it continues on the status quo.

Obviously, Bonneville has undertaken a number of steps—cutting costs, unbundling products and services, transmission access, program retooling and tiered rates; we support some of those. I think for many of them it is much too early to tell.

We do have a number of concerns. First of all is adequate information and evaluation, as we go through this process, making sure that we have the time to respond to that. We are mindful of Bonneville's schedule and are willing to work within that schedule, but I think it behooves everyone to make sure that there are no surprises; and we need to be better in asking Bonneville—making our requests to Bonneville on information.

Bonneville needs to be very good about responding. We want to see real, overall cost improvements, not just a shift of costs from Bonneville to the utilities or from the DSIs to the utilities. I think the measure that we are looking at is Bonneville's costs plus utilities costs are lower than what you would imagine a Bonneville status quo cost to be. And unbundled products and services, as mentioned earlier, I think that there will be a number of my member industrial customers who are interested in potentially offering reserves to Bonneville, as well as the DSIs and the utilities.

I think fundamentally, as we go through this process, the question is a question of Bonneville's continued role in the region and whether or not this region is in fact a region anymore. Regardless of the assumptions that went into the regional act, it seems it is going to be a great challenge for all of us to determine whether, as we go through this process, we don't actually set up a situation

which pits one group against another group in a way that literally tears the region apart.

We do give credit to Bonneville, a large Federal agency, for recognizing that its position today does not guarantee its future and for taking bold steps, both internally and externally, to improve its chances in the future. We certainly don't agree with everything in the business plan, and we will have many intense discussions with all of the parties sitting here at the table today on these subjects. However, now that we have a draft business plan, we at least have a target to shoot at, and we believe it as an important first step.

Thank you.

Mr. DEFAZIO. I thank the gentleman.

[Prepared statement of Mr. Canon follows:]

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Managing Director
Ken Canon

**Testimony of Ken Canon, Managing Director of the
Association of Public Agency Customers**

To

**The Subcommittee on Oversight and Investigation of the
House Committee on Natural Resources**

August 9, 1994

The Association of Public Agency Customers (APAC) is a group of large Northwest industries who purchase electric energy from Northwest public agencies (municipals, rural electric cooperatives, and public or peoples utility districts). Since its formation in 1981, APAC has represented its membership in every BPA rate proceeding. APAC was formed out of the recognition that BPA rates have a profound impact on the rates charged by the local public agency. APAC's industrial members need an adequate, reliable and competitive power supply in order to survive in an increasingly competitive global economy.

The Regional Act was based on the assumption that BPA would operate as the center of a coordinated, regional power system. Events since the passage of the Regional Act have forced BPA and the region to question that assumption. Changes in technology, institutional relationships, business organization, and future assumptions have combined to place BPA's centralized role at risk. Without significant changes, BPA is likely to become just one of many participants in a vastly more open and fluid regional power system. BPA's new role may be focused more on coordination through its operation of the regional high voltage transmission grid, rather than its current position as a primary funding source. If, however, BPA is to continue as the central focus of regional electric energy policy and activity, it must strive to improve its competitive position.

Achievement of the purposes of the Regional Act (cost effective resource development) is closely intertwined with the need for BPA to keep rates - both short term and long term - at competitive levels. As a high fixed cost utility system, BPA risks losing more than it might gain by raising rates in the short term on the promise of lower rates in some distant future. The challenge facing BPA is to strike an acceptable balance.

Load loss only serves to deprive BPA of the very revenues needed to fund its responsibilities.

We are concerned that BPA is on a path that will place it (and those that rely on it) in an uncompetitive position in the near future. Two countervailing factors support this concern. First, under the status quo, BPA is projected to need a series of double digit rate increases in order to meet an increasing revenue requirement. Second, other utilities and independent power producers are aggressively moving forward to lower costs and limit rate increases. Our view is that the competitive crossover point for BPA will occur near the end of this decade. However, APAC members, and/or the utilities that serve them, are not waiting for this to occur. They are actively exploring means to reduce their reliance on BPA through their own resource acquisitions or through power purchase arrangements. Establishing a more diverse power supply is viewed as a prudent option given the challenges facing BPA. At the same time, we are working closely with our utilities, BPA and others in an effort to help transform BPA into a competitive, customer-responsive organization.

In its draft Business Plan, BPA seeks to address its competitive position by designing a tiered wholesale rate structure, by unbundling its products and services and by reinventing conservation and fish and wildlife programs. In addition, BPA is restructuring its workforce in order to be more market and customer oriented. We support BPA's intent to unbundle its products and services, to provide greater transmission access, to seek more cost effective means to acquire conservation and to achieve more measurable results from its considerable fish and wildlife annual investments. However, we are not convinced that tiered rates are necessary to achieve these laudable goals. We are concerned that tiered rates as proposed in BPA's draft Business Plan only formalize the split between BPA customers that are expecting growth and those that are expecting little or no growth. This may have unintended negative consequences for future regional action. Regional action is not aided by a system that pits growing public agency customers versus non growing public agency customers and Direct Service Industries in an ongoing regional battle over the diminishing capability of the Columbia River hydro power system.

We have only begun to understand the nuances involved in establishing a workable and fair tiered rate system. We believe that it is much too early to either endorse or oppose a tiered rate structure. The question that we continue to try to sort out is, "How are we better off with a tiered rate system as compared to some other non status quo system?" That determination can only be made following a much clearer definition of what a tiered rate system actually involves, how it specifically affects the

different customer groups, and whether it actually provides a more competitive electric utility system as opposed to simply shifting costs from BPA to its utility customers.

Never the less, we do have two concerns regarding tiered rates as proposed by BPA. The first regards the treatment of the Direct Service Industries. We understand the competitive plight confronting the DSIs. We face the same competitive pressures but without the safety net of a rate that varies with the price of the commodities produced by the APAC membership. High load factor industries (whether DSIs or APAC members) provide real benefits to the efficient use of a power system. However, any tiered rate proposal adopted by BPA must treat the DSIs in the manner contemplated under the Regional Act. Even though there are limits to DSI growth, the DSIs (in exchange for long term contracts) committed to paying for a share of BPA's load growth. This commitment must be reflected in any tiered rate system adopted by BPA. In addition, it must be recognized that the DSIs are not the only industries in the region that may be willing to provide reserves for the power system. An examination of the need for reserves, the options to provide the reserves and the pricing of reserves may reveal other entities willing to provide reserves at a competitive price.

Our other concern with the tiered rate proposal involves the treatment of industries that have "Contracted For, Committed To" (CFCT) amounts under the New Large Single Load (NLSL) provisions of the Regional Act. In the Regional Act, only one tiered rate provision was adopted, the New Large Single Load provision. This growth penalty could be avoided if the industry could demonstrate that it had a contract or commitment from its utility for an amount of power in excess of its current usage. A number of industries in the region have documented their CFCT amounts and their utilities have entered those as an exhibit to their Power Sales contract. We believe that BPA must continue to recognize these CFCT amounts in any Tier 1 allocation.

Answer to the specific questions posed by the Subcommittee:

Questions 1, 2 and 3

Over the past decade BPA's competitive position has eroded sharply due to other competitive power supply options and BPA's own cost pressures. We continue to support BPA's efforts to gain Government Corporation status as one means to implement greater internal efficiencies. However, assumptions of ever-increasing fish, wildlife and other nonrevenue producing investments, continued internal cost increases, uncertainty caused by BPA's political nature and significant customer dissatisfaction are leading BPA's customers to examine other resource options.

If BPA were to continue the status quo, we believe they will

become uncompetitive by the end of the decade. However, BPA's customers will not wait to take alternative actions. If BPA is unable to convince its customers in the next several years that it can significantly change the way it does business, then BPA could face the beginning of a death spiral. Even moderate load loss could impact BPA's financial viability. Significant BPA change would include controlling its costs, limiting the scope of its activities to those that are at the core of its business and those that it does best, and utilizing the flexibility of the hydro system in partnership with its customers in order to provide resources economically.

Question 4.

It is much too early to determine the effectiveness of BPA's attempt to restructure its operations in an effort to be more customer oriented. However, we certainly support BPA's efforts. Recognition of the "hassle factor" problem is an important first step in correcting the problem.

Question 5.

Under the tiered rates structure proposed in BPA's draft Business Plan, it appears that approximately \$200 million to \$300 million in costs will be shifted to preference customers. These costs will be shifted from the DSIs, from a residential exchange buyout on the order of \$200 million a year and from contracts that have rates based on BPA's Average System Costs. These cost shifts come primarily from shifted responsibilities for resource development and the loss of the DSI top-quartile market.

Question 6.

We believe that most utilities, and certainly the larger ones, will continue conservation efforts with or without tiered rates. Tiered rates may reduce some efforts at some of the slower growing utilities. Freed of the limitations and requirements imposed with many BPA conservation programs, we believe that utilities are in the best position to develop locale-specific conservation activities. To the extent utilities are investing their own customer funds, we believe they will be motivated to develop innovative means to achieve more conservation at a lower cost.

Question 7.

None at this time. To the extent that BPA proposes to act as a backstop from the very beginning of the conservation reinvention, what motivation would exist for utilities to go forward on their own? Just delay and the entire program would revert back to the existing status quo with all the utilities sending money to BPA, BPA processing the money and skimming off a

not inconsequential amount for as overheads and program administration, and then disproportionately reallocating the remaining money back to the very utilities that sent it in originally.

Question 8.

No.

Question 9.

BPA and the region's utilities need to focus on treating conservation as a resource, not as a social program. As a resource, BPA and the region's utilities should have spent the past 13 years focused on acquiring the least costly, most effective conservation first. This would minimize rate impacts, reduce the need for new BPA Treasury borrowing authority, while still meeting the region's conservation goals. The same approach should be used now.

Question 10.

Based on what we have seen to date, we do not support this concept. The advantage of public power is local control over the local consumer owned utility. To agree to this principle could possibly mean removing much of a utility's discretion to respond to unique local needs and situations. It would also mean assuming that all utilities would act in bad faith and therefore all need an affirmative requirement in their power sales contracts. We are unwilling to make that assumption. Our reaction to this principle is highly dependent on the specifics of the proposal.

Question 11.

Renewable resources will continue to compete with natural gas-fired resources. BPA's unbundling of products and services, and greater transmission access could allow more utilities to diversify their resource portfolio through the integration of renewable resources.

Question 12

Establish the DSI price equal to what an all-requirements industrial customer would pay by adjusting the weights of the DSI's Tier 1 and Tier 2 prices to accomplish that goal.

Question 14

BPA has recently revised its schedule to accommodate a greater focus on the power sales contracts to initiate this process. The customers must be more explicit regarding their

specific information and data needs and BPA must be more responsive to developing this information in a timely fashion. BPA cannot keep the endpoint of its schedule fixed while pushing back the front end of the schedule. Each BPA customer must go into the tiered rates process with their eyes open regarding the specific financial impacts of each proposal. We are concerned that the current schedule compresses the process, but we are willing to try to work within these constraints.

Question 15

The DSI's load pattern is beneficial to the power system. So, also, are the loads of some retail customers in the region. Opportunities extended to the DSIs in recognition of their beneficial load patterns should also be offered to other retail customers that can provide the same beneficial load patterns.

Question 16

Congress should make no changes to regional preference.

Mr. DEFAZIO. I notice a couple of people are standing in the back. The committee has no objection if they want to take a couple of the seats over here at the end of the dais. But if they like standing, they can do that, too. I thought this was interesting enough that you could sit down and stay awake, but maybe other people don't, so—yes, I know.

I am wondering when—the House has just gone out. Just listening to the bells.

Okay, Mr. Wilcox is next.

STATEMENT OF BRETT WILCOX

Mr. WILCOX. Thank you. I am Brett Wilcox, President of Northwest Aluminum Company in The Dalles. With me is Ken Peterson, CEO of Columbia Aluminum Corporation.

Bonneville faces a real and immediate challenge. This problem is both cyclical and structural. BPA is going through a cycle when its own costs have risen dramatically and may make it uncompetitive unless future increases are controlled.

In contrast, BPA's competitors, especially gas-fired generators, face historically low fuel and other costs. While BPA's still have some cost advantage, it clearly would be imprudent to bet the agency on the hope that BPA's costs will come down and that natural gas prices will go up. It is essential that BPA take action now so it can remain competitive, regardless of uncontrollable future cycles.

It would be a mistake for anyone to believe that BPA's problem is just cyclically low natural gas prices. The fundamental problem is the way BPA's business is structured. BPA's historic practice of selling highly bundled power products has resulted in many customers paying for services they do not use, while other customers pay less than the cost they impose on the system.

For example, bundled rates give customers an artificial incentive to develop their own combustion turbines because they can operate their own resources at minimum cost and shift the costly shaping and load falling services to BPA. The current structure places BPA at the inherent disadvantage of providing an entire fruit basket of services while competitors just have to provide basic apples. The proposed business plan fosters apples-to-apples competition.

A second structural problem is BPA's ability to respond to rapidly changing markets as quickly and economically as its competitors. BPA simply cannot afford to be outmaneuvered by competitors who are more and more market focussed and customer oriented.

The proposed business plan streamlines BPA and reduces the hassle factor dealing with the government bureaucracy. While the draft business plan provides a good map, it can only be implemented through into contracts and rates. We support BPA's ambitious but necessary schedule which was announced today to resolve these issues by October, 1995. These contract and rate issues can and should be resolved by compromise within the region. None of these issues requires a change in Bonneville's existing statutory guidance.

One key issue is conservation reinvention. We support tiered rates because price signals can be a more effective and economical way to meet the region's conservation goals than bureaucratic pro-

grams and cash incentives. Contrary to some claims, BPA is not risking regional conservation goals by trying an unproven approach. BPA will maintain its strong conservation effort but replace grants with loans recovered through energy service charges. This approach follows the proven and highly successful energy finance conservation program pioneered by Pacific Power.

The last issue I want to put to rest is the assertion that the DSIs are subsidized through the value reserve credit and valuable reserve rate. Neither is a subsidy. Both hold down other customers' rates. I would personally support your idea to seek reserves from anyone through competitive bids.

BPA enjoys substantial rights to restrict service to the DSIs when necessary to protect service to its other firm power customers in the region. These rights range from stability reserves, which allow BPA to interrupt 100 percent of the load for brief periods, to top quartile reserves under which BPA restricted 25 percent of each DSI load almost continuously over the last two years, principally to avoid purchasing high-cost energy. While DSI rates are adjusted, provides some compensation for these restrictional rights, bottom line, BPA charges the DSIs higher rates for interruptable service than it charges utilities for firm service. In my book, that is not a subsidy.

The variable rate paid by BPA's aluminum smelters links the power cost to the price of aluminum. If prices fall, the rate is discounted, but only to a point that is still above the price BPA can obtain in other markets. If aluminum prices rise, smelters pay a premium.

The claim by NCAC that variable rates could cost regional rate-payers more than \$300 million is just plain wrong. BPA has calculated that as of March, the variable rate has improved revenues by \$52 million. The DSIs estimate that over its entire life, the rate will add about \$50 million to BPA's revenues. My written testimony contains a more detailed explanation of these and other issues.

Thank you for the opportunity to testify and respond.

Mr. DEFAZIO. Thank you, gentlemen.

[Prepared statement of Messrs. Wilcox and Peterson follow:]

TESTIMONY OF BRETT WILCOX
PRESIDENT OF
NORTHWEST ALUMINUM COMPANY
BEFORE THE HOUSE NATURAL RESOURCES COMMITTEE

My name is Brett Wilcox. I am the President of Northwest Aluminum Company, located in The Dalles, Oregon, which is a direct service customer of the Bonneville Power Administration. My company, and my employees, want BPA to remain a competitive supplier of power. For this reason, Northwest Aluminum and BPA's other direct service industrial customers support the proposal in BPA's Strategic Business Plan to restructure and streamline its business so it can meet the challenges of the new competitive marketplace for electricity. The electric power business is undergoing rapid and accelerating change towards increased competition, particularly in the wholesale power and transmission markets. BPA must be allowed to respond to this new competitive market if it is to maintain its position as the power supplier of choice in the Pacific Northwest.

Today I would like to make several important points in response to your Task Force's Report.

First, BPA does not need two years to reposition itself in the market, nor does it have the luxury. Competitive forces are driving BPA's customers into the arms of competitors even as we convene here.

Second, utilities are prepared and motivated to pursue conservation vigorously under tiered rates -- and without BPA's heavy overhead costs.

Third, the DSIs should be treated no differently under new contracts and rates than other customer groups, as provided by the Northwest Power Act.

Fourth, the Task Force's Report concludes erroneously that the DSIs enjoy subsidies. To the contrary, the DSIs are paying more than the costs of serving them, and I'll explain how.

Fifth, the Variable Rate is one of the most successful sales implements ever adopted by BPA. It has produced great benefits for BPA and its customers, and has been emulated by other utilities that serve such loads elsewhere.

And finally, I will address the real subsidies in BPA's rates and explain why disposing of Regional Preference is a bad idea and, in any case, futile.

The Competitive Environment

I have closely followed, and participated in, the development of BPA's Strategic Marketing Plan and its Strategic Business Plan. BPA accurately identifies many of the factors which have created a more competitive market for electricity, including open transmission access, the falling cost of gas fired generation, increases in BPA's costs and uncertainty about future increases in these costs, and the large number of well-financed new entrants into wholesale power generation markets.

All of these factors have eroded the competitive advantage that BPA enjoyed for decades due to its low-cost federal hydropower base. In my judgment, however, none of these factors represents the single largest threat to BPA's ability to perform in the marketplace. The federal hydro system is still capable of producing low cost energy products which customers will need as power markets evolve.

The real threat to BPA lies in potential barriers, imposed from outside the marketplace, on BPA's ability to respond to the market by changing as quickly and economically as its competitors. BPA's historic cost advantage over alternative suppliers has been significantly reduced such that BPA has little, if any, margin for error. If BPA's competitors react more quickly to occupy product niches which are opened as markets evolve and to move out of product niches that become unprofitable, then BPA will steadily loose market share. As a utility with fixed costs making up most of its total costs, BPA cannot afford to be outmaneuvered systematically by more market-responsive competitors. Therefore, BPA must have the capability to change rapidly in response to market forces.

Northwest Aluminum supports BPA's Business Plan because it represents reasonable change where change is clearly needed. Without these changes, the inexorable upward pressure on BPA's overall costs, and its customers' perception that this pressure will continue, would seriously impair BPA's competitive position. In the eyes of its customers, BPA's Business Plan is an important first step to address and slow these pressures. Further, implementation of the Business Plan will streamline BPA and by more clearly defining responsibilities will reduce the bureaucratic "hassle factor" that has characterized BPA's past. The Business Plan must be implemented without delay because the competitive pressures BPA faces are real, and delay in reacting to them would, in itself, send BPA's customers a signal that BPA has become an inflexible and unreliable supplier in a changing market.

I recognize that BPA has unique responsibilities arising from its use of the Columbia River System and its status as a federal agency. But the fulfillment of these public responsibilities depends on BPA's ability to meet the basic commercial needs of its customers. If BPA fails in that enterprise, then there will be no funds for the discharge of its public responsibilities.

Contracts and Rates

Many of BPA's initiatives will require new contracts with its customers and revised rates. BPA recognizes that timing is the key issue to the success of its Business Plan and proposes an ambitious, but necessary, schedule to address and resolve these contract and rate issues by October 1995. I also believe that the success of BPA's Business Plan requires that this deadline be met.

These contract and rate issues can and should be resolved by negotiation and compromise within the region. A regional solution will balance the many interests affected by BPA and it will be sufficiently flexible to allow for future changes as they are needed. None of the outstanding issues requires any additional statutory guidance for BPA. Excessive Congressional oversight could detract from the ability and willingness of regional parties to act in a timely fashion. Instead of compromising their differences through good faith negotiations in the region, parties would be encouraged continually to return to Washington for political solutions to their business problems. BPA must be free to pursue market-based solutions to market problems. BPA cannot possibly respond to rapidly changing market conditions if it must negotiate with its customers and potential competitors before Congress.

Tiered Rates

BPA has identified the adoption of tiered rates as a key element in reinventing conservation. In fact, the initial impetus for tiered rates came from the conservation community. I support tiered rates because the price signals provided by tiered rates can be effective and economical means to reach the region's conservation goals when coupled with strong utility support for achieving all cost effective conservation. I do not agree that tiered rates should be coupled with continued cash incentives to utilities sponsoring conservation. One important reason for substituting tiered rates for cash incentives is the high cost and hassle factor inherent in policing the use of incentives. Tiered rates allow customers to reap directly, through lower power bills from BPA, the rewards of conservation without the bureaucratic overlay of the current system.

I will not propose any alternatives for the implementation of BPA's tiered rate principles because those changes are currently being worked out among interested parties in the region in BPA's tiered rates workshops. I expect a consensus to develop in that process. I do not expect the consensus proposal to treat the DSIs any differently than other BPA customer groups. The DSIs should have the same incentives to conserve as other customers and should not suffer discrimination regarding the adequacy of their power supply.

The DSIs Are Not Subsidized by Other Customers

The Task Force's Report contends that the DSIs are subsidized by other customers due to the value of reserve (VOR) credit in their Industrial Power rate and due to the Variable Rate for aluminum smelters. Neither of these provisions is a subsidy -- to the contrary, both provisions benefit BPA's customers generally and serve to hold down other customers' rates.

The BPA rates applicable to the DSIs, including the VOR credit and the VI rate, recover the full cost of serving the DSIs' loads.

VOR Credit. BPA enjoys substantial contractual rights to restrict service to the DSIs when necessary to protect service to its other firm power customers in the region. These restriction rights range from the "stability reserves" by which BPA can interrupt up to 100% of a DSI's load for brief periods in the event of equipment outages (e.g., several DSIs were restricted this spring when the L.A. earthquake disrupted transmission of power sales from California to the Northwest), to top quartile restrictions which BPA has used for economic reasons (e.g., BPA has restricted 25% of each DSI's load almost continuously since August 1992 for economic reasons while it is purchasing to serve its other firm loads). Even though the DSIs' rates are adjusted to provide some compensation to the DSIs for these interruption rights, BPA charges the DSIs higher rates for interruptible service than it charges utilities for firm service. In my book, that is not a subsidy.

The VOR credit is part of a comprehensive rate package known as the Industrial Power ("IP") - Priority Firm ("PF") Rate Link. This link was established in 1987, based on BPA's 1985 rate case results, to quantify the net of adjustments required under the Regional Act to BPA's PF rate to derive the IP rate. The individual adjustments are a "typical retail margin," a "character of service adjustment" for top quartile interruptions, and the VOR credit. The sum of these adjustments produced a surcharge of approximately 1.5% to be added to the firm power rate applicable to BPA's public utility customers to develop the DSIs' interruptible power rate. After the 1985 rate case, parties requested BPA to extend the 1985 methodology through 1990, and later through 1996. BPA adopted the link after expressly finding that the link would in aggregate track the net of the individual components if they were recalculated in each future rate case. The Federal Energy Regulatory Commission approved the methodology twice. The link has been used by BPA in each subsequent rate case by escalating the 1985 net mark-up by the rate of inflation.

NCAC now argues that one element of the link -- the portion of the VOR credit associated with forced outage reserves -- would be substantially lower if it were recalculated today. NCAC is mistaken about the amount of the VOR credit. The VOR forced outage component of the VOR credit compensates the DSIs for the value of certain contractual restriction rights that were negotiated in 1981. By virtue of BPA's forced outage restriction rights, BPA was able to avoid in 1981 purchasing over 1200 megawatts of combustion turbines to back up its system. The primary savings to BPA was the carrying costs on long term debt BPA would have had to incur in 1981 to acquire the turbines. Therefore, it was appropriate for BPA to base the VOR credit on those savings. The DSIs receive only one-half of the savings and BPA's other customers receive the remaining savings through lower rates. Moreover, NCAC is simply incorrect about the amount of reserves the DSIs provide. BPA negotiated the amount and duration of its rights to restrict 1600 megawatts of DSI load to provide the 1288 megawatts of capacity reserves it concluded were needed to back up all of BPA's operating resources.

NCAC is also incorrect about the effect of recalculation of the VOR credit, which would require repeal of the comprehensive IP-PF Link. Most elements of the IP-PF Link would be more favorable to the DSIs if recalculated today based on current circumstances. First, the VOR credit gave the DSIs only token compensation for stability reserves, which are provided by an automatic load shedding device at DSI plants, and which save BPA hundreds of millions of dollars in transmission system upgrades that BPA would otherwise need to obtain the same level of transmission reliability. Second, the character of service adjustment for top quartile restrictions was based on conditions in 1986 and 1987 during which BPA's surplus of firm power made top quartile restriction highly improbable. If applied to the current deficit condition, the downward adjustment to the DSI rates would be twice as large. Finally, by escalating the net mark-up, the IP-PF Link overstates the actual increases in retail margins. If all elements of the IP-PF Link were recalculated using the 1985 methodology, I would expect the DSIs' rate to be reduced by a modest amount. NCAC's attempt to criticize a single component of the link in isolation is self-serving and inappropriate.

The Variable Rate. The Variable Industrial ("VI") rate paid by BPA's aluminum smelter customers links the DSIs' power cost to the worldwide price of aluminum. BPA adopted this rate in 1986 to enhance its overall net revenues and thereby keep rates to other customers lower than they would be without the VI rate. If aluminum prices fall, the smelters' power price is discounted; but even the low end of the VI rate is designed to remain above the price BPA could obtain for the power in other markets or the value of reducing BPA's power purchases. When aluminum prices rise, the smelters pay a premium on their power price and BPA gets more revenues from sales to the DSIs than it would at the standard IP rate. As a secondary goal, BPA designed the VI rate to produce an average rate equal to the IP rate, if possible.

The claim by NCAC that the VI rate "could cost regional ratepayers more than \$300 million by June 1996" is just wrong. This number represents the difference between charging the DSIs the IP rate and the VI rate for the same amount of power over a 10-year period assuming that aluminum prices had stayed at extremely depressed levels for the remainder of that period. The very reason BPA adopted the VI rate was its well-supported conclusion that the DSIs would not buy the same amount of power at the IP rate when aluminum prices were depressed. With the VI rate, the DSIs will buy more power, at prices above what BPA could otherwise sell the power for, and this extra revenue is the benefit of the VI rate to BPA and its other customers.

In March 1994, BPA calculated that, as of that time, the VI rate had improved BPA's overall revenues by \$52 million. The DSIs estimate that, over its life, the VI rate will add about \$50 million to BPA's revenues. Our estimate uses BPA's method of comparing its overall revenues with and without the Variable Rate, and it uses more current aluminum prices than were available to BPA in March. In retrospect, the VI rate has operated as planned to benefit all of BPA's customers. The DSIs benefited from more stable operations. Other customers benefited from higher revenues. In fact, at the top of the aluminum price cycle, the VI rate allowed BPA to cancel one of its scheduled rate increases.

Cost Shifting Under The Business Plan

Currently, costs and benefits of BPA's programs and products are not closely tracked by rates. BPA's historic practice of selling highly bundled power products has resulted in many customers paying for services they do not use while other customers pay less than the cost they impose on the system. This is the true cross-customer subsidy in BPA rates. As a result, BPA's prices are not competitive for some products while other products are over-utilized because they are underpriced.

The graph attached to my testimony illustrates this point. Natural flows and associated power generation capability of the Columbia River system are low in winter and very high in spring and early summer. Power needs of northwest utilities, in contrast, peak in winter and are low when water is abundant and power would naturally be produced. A very large part of BPA's costs were incurred to shift water and associated power from the time when it naturally occurs to when it is most needed.

While BPA's current rates do differentiate somewhat between seasons and time of use, the "one size fits all" approach in BPA's current marketing program means that particular customers may pay more or less than the costs their loads impose upon the system. Unbundling of products in the new Marketing and Business Plans allows BPA to correct this problem. It also helps make BPA's marketing complementary to rather than in conflict with its expanded fish and wildlife responsibilities.

BPA's current competitiveness problem in large part is caused by its current bundled rates. If a utility develops its own combustion turbine, for example, it can run its own resource at an extremely efficient 100% baseload operation to meet the cheapest to serve part of its load. This leaves BPA to provide the costly services above the line of the utility's own resources.

Under the new Business Plan, BPA provides "baseload" power "below the line" (through each customer's share of Tier 1 power) and each customer is responsible for meeting variations in its own loads (through either their own resources or by buying unbundled or "rebundled" BPA power and services). This insures "apples-to-apples" competition rather than leaving BPA with an inherent competitive disadvantage because it delivers an entire fruit basket with each apple it sells. Unbundling will shift costs towards those customers who place higher costs on BPA and away from customers that have been systematically overcharged for what they get from BPA. This movement to more cost-based rates and real competition is a positive and appropriate development. It is one of the reasons I think it is important for BPA to implement the Business Plan by October 1995.

Regional Preference

The Task Force report suggests that BPA might be less vulnerable in a competitive power market if the Regional Preference Act were amended to facilitate power sales to California. I disagree. The only possible reason to amend the Regional Preference Act would

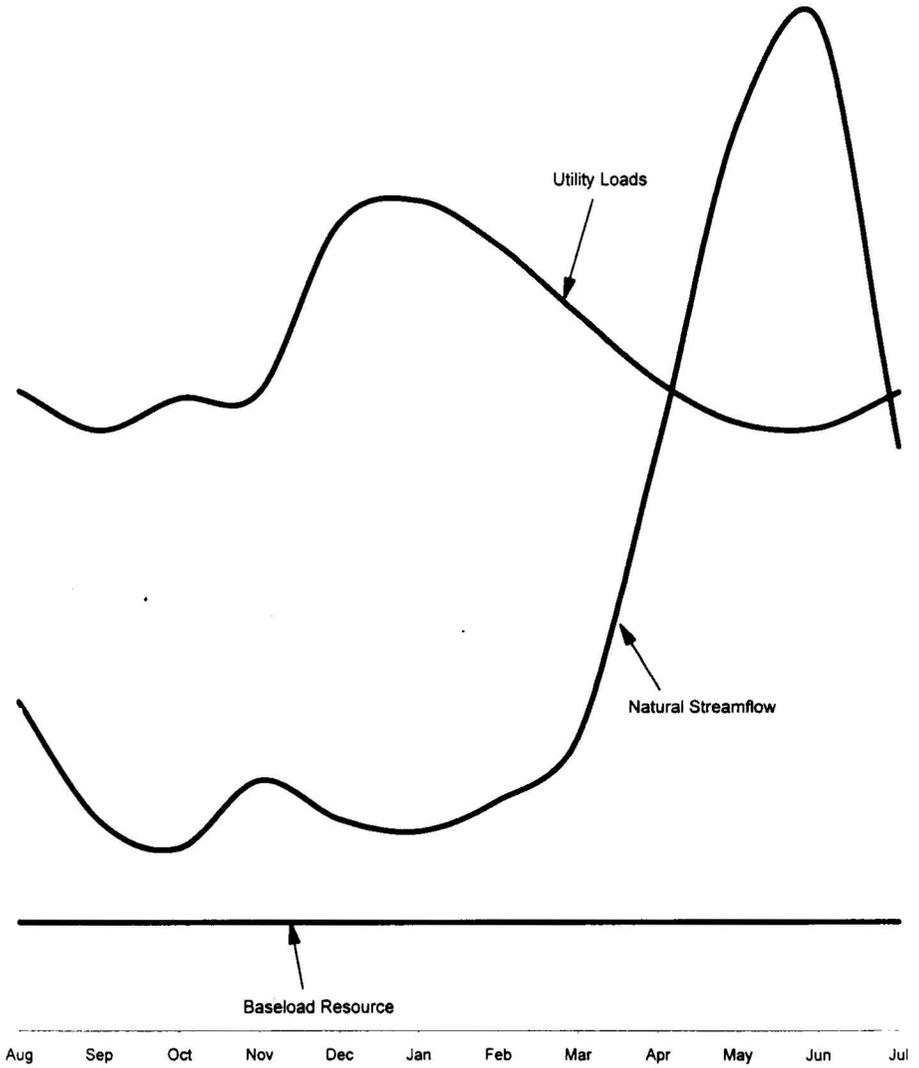
be if the hydro system were so badly mismanaged that BPA's rates forced the closure of much of the region's industry. Rather than planning for such failures, this Committee should encourage BPA's effort to change the way it does business to succeed in the competitive future. Moreover, the days when it was possible to sell bulk power to California at a profit appear to be gone; to the contrary, BPA's analysis shows that currently BPA can most economically meet its own resource needs through power imports.

Summary

BPA's Strategic Business Plan is a reasonable blueprint to address very real and very pressing problems. I hope you can join to support prompt adoption of the plan and implementation of its rates and contract elements by October 1995.

The assertions made by some parties that the DSIs pay subsidized rates are incorrect. Rates to the DSIs recover the cost of serving the DSIs. Rather than criticize BPA's contractual restriction rights and the Variable Rate, customers should applaud them as creative and successful responses to market conditions and urge BPA to use similar creativity in the future.

Hydro Resource Capability and Utility Loads



TESTIMONY OF KEN PETERSON, JR.
CHIEF EXECUTIVE OFFICER OF
COLUMBIA ALUMINUM CORPORATION
BEFORE THE HOUSE NATURAL RESOURCES COMMITTEE--
AUGUST 9, 1994

My name is Ken Peterson. I am the Chief Executive Officer of Columbia Aluminum Corporation. My company owns an aluminum smelter near Goldendale, Washington, which is a direct service customer of the Bonneville Power Administration (BPA). Columbia Aluminum Corporation is owned 30% by all of its employees through an Employee Stock Ownership Plan, and the remainder is owned mostly by myself as well as some other employees. In short, we are 100% employee-owned.

Like Mr. Wilcox, my co-owners and employees are deeply concerned about BPA remaining a competitive source of power into the future. We want this because we live and work in the great Pacific Northwest and we know that the aluminum industry is like the proverbial canary in a mine shaft. That is, our business is more sensitive than most to uncompetitive power rates. For example, we cannot switch to natural gas or fuel oil or coal as a substitute for electricity. We require electricity truly as a raw material, as many people learned in the BTU tax debate. Moreover, the cost of electricity can typically make up 30% of our total production costs. Therefore, problems will show up for our business as a kind of early warning system for more pervasive systemic problems. This helps to explain why my company is deeply concerned as we see BPA struggling to retain its relevance into the 21st century.

My objective today is to make two points:

Number 1. This Task Force's May 1994 report entitled "BPA at a Crossroads" erroneously states at page 9 that "the low price the DSIs pay for power [because of the variable rate] . . . impose an economic cost on the region by increasing the electricity rates paid by all other BPA customers."

Number 2. On the other hand, the Majority Staff Report's conclusion on page 12--"BPA should implement tiered wholesale power rates and offer certain unbundled services to better serve customer needs."--is exactly correct and should be affirmed at every opportunity.

Now let me address these points at more length.

1. The idea that the Variable Rate is some sort of regional subsidy to the aluminum industry is a myth. The Majority Staff has done a profound disservice to the region by repeating this falsehood. In fact, the direct opposite is true. That is, the Variable Rate is an outstanding example of a public policy which achieved its objectives pretty much exactly as planned. The Majority Staff's analysis of this issue was shallow and apparently substituted a simple, but wrong, answer for a more complex, but accurate, one. Let me explain.

Apparently the Majority Staff simply took the actual amount of direct service energy sold pursuant to the Variable Rate from the time of its implementation, multiplied this by the relevant plateau rate (the otherwise "normal" rate) in effect over time and compared this to the actual revenue produced under the variable rate to date. Using this simplistic approach it is mathematically true that more money would be generated if that amount of power had been sold under the standard Industrial Rate.

Unfortunately, this represents a completely static analysis of a policy whose purpose it was to change what behavior would otherwise be. It also completely disregards the present value of money which must be included in any comprehensive analysis.

I can personally testify, however, to the effective use of this policy in influencing behavior. In 1987, after the Variable Rate had been implemented, Commonwealth Aluminum, the prior owner of the Goldendale smelter, completely shutdown the smelter and went out of the smelting business in North America. During the preceding three months, and the succeeding six months, I along with many others worked very hard to buy this closed plant with the intention of restarting it. We negotiated an unprecedented labor contract with the United Steelworkers of America. We negotiated a multi-year sale of most of the output of the plant to a foreign company. We also worked with BPA on transferring the power contract. In spite of all these efforts I was unable to finance this multi-million dollar transaction with American bank capital. By mid-1987 aluminum prices were considerably stronger than at the end of 1986. Nonetheless, American banks refused to back the transaction because of a fear that prices would soften again.

The consortium of foreign banks that eventually supported us were intensely interested in the Variable Rate and I remember BPA sent an employee to thoroughly brief them on how it worked. I can say categorically and unequivocally that without the Variable Rate we would have been unable to buy the smelter and restart it in 1987. Perhaps someone else could have come along in 1988 or 1989, but

that would be sheer speculation. The fact is that insofar as my smelter's power usage is concerned there would have been zero used during at least 1987 and 1988 but for the Variable Rate.

I also want to emphasize that when the power contract was transferred to Columbia Aluminum Corporation in mid-1987 we were given the opportunity to choose either the Variable Rate of the standard Industrial Rate. We chose the Variable Rate even though we knew before one kilowatt-hour had been used that we would start off paying a higher rate than if we chose the standard rate. The downside potential was simply too great under the circumstances. I know that my experience was similar to others' and taken together the Variable Rate was a key element in returning or maintaining literally thousands of jobs in the Pacific Northwest. But it also provided BPA with millions of dollars of revenues at a critical time which it otherwise would not have had. In short, the entire region was a winner.

The simplistic analysis that assumes mistakenly that my smelter's power use in 1987 and 1988 (and maybe longer) would have been the same whether or not there was a Variable Rate conspicuously proclaims its complete lack of understanding of the Variable Rate and what was happening in the region in the mid-1980's. Compounding this mistake is the total failure to appreciate that a dollar paid in the present is more valuable than a dollar paid in the future. The Variable Rate resulted in huge "overpayments" in its early life and only later did the rate fall below the standard Industrial Rate level. The Majority Staff apparently ignored this.

2. A major reason for the drastic erosion of BPA's competitiveness lies in the debacle involving the Washington Public Power Supply System's construction of five nuclear power stations. Only one was completed. The other four were multi-billion dollar "dry holes." The completed one is a high cost source of power itself. While I was in law school in Oregon and then as I practiced law in Eastern Oregon I was a critic of WPPSS.

I mention this because as I see it the fundamental policy problem with these ill-fated nuclear plants was that there was then no tiered rates. If we would have had tiered rates I cannot imagine that the region would have spent the billions of dollars it did with nearly nothing to show for it. Tiered rates do not make much sense when the incremental cost of power is going down, as it was during much of BPA's earlier years. But it makes a great deal of sense when the incremental cost is rising. Not only does it place the cost of meeting demand growth on those who are growing, which is only

fair, but it also provides more appropriate economic signals concerning the cost of such additional power.

I believe strongly in the capitalist, free market economic system that has evolved in America. Its genius lies in the ability to transmit signals to consumers and producers so as to stimulate or suppress demand or supply at any particular time. Thus, when price signals from BPA said that power only had a 2 mill cost it was reasonable that demand projections would look rather rosy. Power at 25 mills, however, had a completely different demand curve, as should be expected. Not surprisingly people became more aware of uninsulated walls and ceilings and the disadvantages of baseboard electric heating.

Thus, I believe part of the reason for the WPPSS tragedy was the lack of tiered rates. Consequently, the idea that BPA is finally serious about them is good news, although it is 20 years too late for my tastes.

I also believe strongly that "unbundling" is the only reasonable and fair way to conduct business in these circumstances. There is no doubt that in the "one size fits all" world that has been BPA there are products and services that have been provided to all when only some find the particular feature of value. If I am right then this means that some customers have been paying more than they otherwise should because they have picked up part of the tab for those using the more expensive features. Conversely, this has given some customers the idea that certain features are "free", thereby encouraging excess use, since the true cost has been shifted to others.

I understand the concept of "unbundling" to mean matching the proper costs with the particular products and thereby sending the appropriate economic signals to customers. This is completely fair and equitable and, in the final analysis, is the only way I know of for BPA to honestly meet its statutory objective of providing the "lowest possible rates to consumers consistent with sound business principles."

Finally let me say a word about speed. There is no doubt that some of the things BPA has announced it wants to do represent significant changes in the way it has done business during the last 50 years. Change is always threatening. It is always upsetting. This is part of the human condition. But change is also fundamental to remaining alive and viable.

I know that the Task Force report raises the issue of whether BPA is pushing these changes too rapidly or not. I do not believe they are. Earlier I pointed out that certain changes made decades ago

could have saved tremendous grief for the region. If, as some have suggested, BPA waits any further to implement significant changes and only does so when it is literally forced to at the precipice of a utility death spiral it will be too late. I can tell you that in the dynamic and real world of competition it is almost never the superior strategy to be the last to respond to changing customer demands, which we loosely call the business environment. The cases of International Business Machines and Digital Equipment would seem to provide ample proof of this statement.

Because change is so hard to truly accomplish, and I suspect this is doubly hard in a government bureaucracy, it is imperative to begin when the signs are clear that trouble is brewing on the horizon. The signs are clear now, even if the exact magnitude and proportions are not known in exquisite detail yet. The changes BPA proposes should increase fairness and equity. There is no valid reason to put off for tomorrow what can be done today in this regard. This committee should be urging such changes and I add my voice to the support you have given to things such as tiered rates and unbundling. On the other hand, this Task Force's credibility is undermined by superficial and simplistic analysis which wrongly supports myths about our regional electric system. As President Clinton says, "We can do better than that."

Thank you for this opportunity to provide some input on this matter of urgent importance to our region.

Mr. DEFAZIO. We go now to Ms. C. Clark Leone.

STATEMENT OF C. CLARK LEONE

Ms. LEONE. I am manager of the Public Power Council, a service organization representing 114 of Bonneville's municipal, cooperative and PUD customers and the primary organization representing our members before Bonneville in rate cases, contract negotiations and other Bonneville policy matters.

While we don't agree with all the features in the business plan, we support Bonneville's general direction to increase its efficiency, improve customer service and retain its position as the supplier of choice in the Northwest. The issue of competitiveness has served as the backdrop for much of BPA's reinvention efforts. While I share the concern that BPA's rates could rapidly become uncompetitive, I think that a review of the rate level alone is too simplistic. Equally important is rate stability.

Many brokers, marketers and independent power producers are offering long-term contracts at fixed rates. In contrast, BPA faces a murky future of ESA compliance costs, vagaries of the weather, fluctuating surplus power prices, potential repayment, reform initiatives and nuclear decommissioning costs.

Predictions of BPA rates are more an issue now for mystics and seers than rate analysts and utility managers. I applaud the steps that Congress has taken to minimize some of these uncertainties, for example, legislation recently introduced by Senator Hatfield and you, Mr. Chairman, to refinance Bonneville's outstanding appropriated debt.

Second, the administration's agreement to credit Bonneville for the cost of recent emergency fish protection measures is also welcome, and we hope this is not an one-shot affair. It represents a sharing of extraordinary costs into the future.

And third, of course, the cost saving proposals contained in the majority staff report outline important steps to reduce revenue requirements and increase certainty. There are some folks that look at the scope of change proposed in the draft business plan and urge caution and slowdown.

I feel that the concerns prompting calls for delays can be allayed if BPA proceeds in a sensible and deliberate fashion. The first critical matter that PPC sees is the business arrangement, which is the contract renewal terms, and then rate case issues followed on by that.

I was just reviewing Mr. Robertson's chart, business plan before and after. I hope I am not to be disappointed in it. The agreement that PPC and BPA entered into is that intensive contract negotiations will begin now with a target finish date in mid-December. If and only if, core contract issues are resolved and set in concrete—not just negotiation and discussion, but set in concrete—then a rate case with the unbundled products, tiered rates, et cetera, will follow on in January. And then, of course, the target would be October 1, 1995 as the new date that rates would become effective.

My written testimony outlines PPC's responses to the specific questions raised in our letter of invitation. Let me just quickly summarize our key points.

Tiered rates are a useful tool to send a price signal on the cost of new resource acquisitions. We do not object to tiered rates provided that they comport with PPC's tiered rate principles. We believe, though, that the tiers should reflect specific resources and their costs, specifically the Federal-based system, including conservation resources achieved to date. The second tier should be new resources, including purchase power. We think the draft plan inappropriately spreads existing resources across both tiers.

Next, Bonneville must adhere to the cornerstone Federal policy of preference. PPC's concerned that the draft plan proposes treating new preference customers as second-class citizens in that they will have less call to Tier 1 rates than will existing customers.

Finally, we support the conservation reinvention efforts. We believe local utility controlled and directed conservation programs can achieve the conservation targets contained in the power plan of the Council at costs lower than those under the current system.

Before concocting a Rube Goldberg compliance mechanism, the parties—those parties who doubt us should give us a chance to prove them wrong. I believe this committee provides the ultimate accountability mechanism. Our members' failure to achieve commonly held conservation objectives will result in a mandatory imposition of highly restrictive conservation mandates.

We want conservation reinvention to work. I simply ask that we be allowed to succeed. Thank you.

Mr. DEFAZIO. Thank you.

[Prepared statement of Ms. Leone follows:]

**Testimony
of
C. Clark Leone
Manager
Public Power Council
before the
House Natural Resources Committee
Subcommittee on Oversight and Investigations
Bonneville Power Administration's Draft Business Plan**

August 9, 1994

**General Comments on Recommendations Contained in the
Majority Staff Report, "BPA at the Crossroads"**

The Majority Staff Report provides an important and up-to-date review of Bonneville Power Administration (BPA) and some of the options available to the agency in its attempts to lower its costs and remain competitive. As you know, BPA's public utility customers have suggested areas where they also believe savings can be realized. (For example, for the FY 1993-1994 rate period, customers identified approximately \$70 million dollars of expense and capital reductions that BPA could make in the conservation program that would have had relatively minimal effect on program success.) BPA appears to be seriously considering all suggestions as it goes about reinventing its entire operation from the bottom up.

The Majority Staff Report lists specific and detailed actions that the Administrator can take to bring costs down. The BPA Draft Strategic Business Plan (Draft Plan), on the other hand, deals with ways to provide guidance to employees, to improve its relationships with its customers, and to structure the agency's operations to keep its costs down over the long-term. The difference between the Majority Staff Report and the Draft Plan appears to be one of emphasis rather than of substance.

- (1) **Please discuss your view of BPA's competitive position at present and over the next ten years. What are the competitive threats? What are BPA's competitive advantages?**

BPA's competitive position is still good. The Federal Base System (FBS) remains valuable. Evidence of this value to BPA's preference customers is found in the extensive effort and commitment they are making to ensure that BPA's reinvention efforts are successful. We believe that BPA is moving in the direction of improving its long-term competitive position, although many significant issues remain.

The costs of new wholesale generation are coming close to BPA's wholesale rate and recent experience indicates that non-federal power is being offered contractually at specific or formula

prices at or near BPA's Priority Firm rate, which applies to purchases by preference customers in the Northwest. These kinds of contract offers tend to minimize, allocate and control the uncertainties faced by utilities in the wholesale electricity markets. BPA's continued competitiveness depends on its ability to control its costs. If unable to do so, BPA's prices will increase and its customers will protect their competitive position by exploring alternatives to BPA.

Some disagree with this view of BPA's competitive situation and argue that BPA is overreacting to a threat that is perceived, not real. Yet Snohomish County PUD in Washington state was recently offered approximately 8000 megawatts in response to its request for resources proposal. We understand that the offers are not all less expensive than BPA's price, but they are more predictable and stable because the offers generally contain firm prices for fixed amounts of power over definite time periods.

- (2) **How likely is it that BPA's rates will be uncompetitive when compared to alternate generation sources in the 2002-2003 rate period?**

The costs of new generation are dropping, retail wheeling services are being requested by industrial customers, and BPA's costs are rising. If BPA is able to reduce its costs, thereby keeping its prices to its preference customers down, the agency should be able to retain its competitive advantage. If not, it will be difficult for BPA to remain competitive in the near-term, making it difficult to be competitive in the long-term.

Price alone, though, is not the only challenge for BPA. Equally important is rate stability, for competitors are even now offering long-term contracts at fixed prices.

- (3) **BPA's Business Plan asserts that BPA will lose at least 1400 aMW of load if the actions proposed in the plan are not implemented, though the analysis contained in the Business Plan DEIS concludes that under the status quo only 599 aMW of firm load will be lost. How likely is it that the BPA Business Plan's "death spiral" scenario, in which BPA loses more than 7000 aMW out of its present load, will actually take place?**

PPC is working on gaining a better understanding of all the numbers in the Draft Plan and DEIS. Loss of BPA's entire load seems highly unlikely, but 1000-1400 aMW loss within the next five years is possible. We know that many of BPA's preference customers are planning to develop resources that will insulate them, at least partially, from uncertainties about BPA's future power supply and prices. We very much want BPA to succeed in its reinvention and to retain as much load as possible.

- (4) **The Task Force report discussed what it called the BPA "hassle factor." Has BPA moved to correct its deficiencies in the area of customer service and satisfaction?**

PPC believes that BPA is moving toward correcting deficiencies in the area of customer satisfaction. The Draft Plan identifies ". . . high and continually improving customer satisfaction" as its first Strategic Business Objective (SBO). This SBO contains four specific measurements that BPA plans to use to measure its success with its customers and to hold specific organizational components accountable. This SBO, when combined with the appointment of Account Executives charged with assisting specific customers, should help the customers feel confident that BPA is sincere in its desire to reduce the "hassle factor".

- (5) **Actions proposed in BPA's Business Plan, such as tiered rates, unbundled services and conservation reinvention, taken together are likely to shift costs between customer categories. For example, all customers now bear part of the costs of regional conservation investment, but many will see those costs decline under the actions proposed in the Business Plan. Others will likely see their overall costs increase. What cost shifts do you anticipate as a result of the proposed actions in the Business Plan DEIS?**

It is certain that the changes that BPA is undertaking will alter the current cost relationships among BPA's customers. We at PPC are very concerned that these issues are addressed fairly, prior to the implementation of tiered wholesale rates and unbundled products and services. We are concerned, for example, that the rate paid by the DSIs could differ significantly from that paid by the industrial consumers of the region's preference customers, a result we believe to be contrary to the intent of the Northwest Power Act. We are troubled that the application of tiered rates to the residential exchange program could result in inequities between the region's preference customers and the residential ratepayers of the IOUs. At this point, the complexities associated with tiered rates, unbundling, changes in subtransmission cost allocations, the low density discount, and other components of rate design leave all observers without a clear picture of the impacts on their individual utilities. Consequently, we are working to develop the necessary analytical tools to allow utility-specific analysis of the impacts of alternate approaches to tiered rates.

- (6) **The Business Plan DEIS estimates that, compared to the status quo, the market-driven alternative will yield about 40 aMW of utility-sponsored conservation as a result of a tiered rate's price signal, 22 aMW as a result of fuel switching, and 130 aMW as a result of independent utility programs. How likely is it that BPA's customers will acquire the cost effective conservation in their service areas in the absence of BPA programs and financing? Will the application of the Business Plan's conservation reinvention principles ensure that the region will acquire the conservation called for in the Power Planning Council's plan?**

PPC's members are committed to independent development of conservation resources. We believe that our members will, in the near-term, continue to operate most of the core conservation programs developed by BPA because they are technically sound and they provide benefits to consumers. We expect changes to occur in the nature, structure and amount of financial incentives offered by the sponsoring utility in conjunction with these types of programs. PPC expects to see payment and incentive structures that more closely mirror local conditions instead of the uniform regional approach of the current BPA programs.

BPA's conservation program is at a crossroads: We can continue the centrally designed programs of the last 14 years with all their attendant shortcomings (40% overheads, inflexibility, and cross-subsidies), or we can pursue a decentralized, locally-initiated and -controlled approach to conservation. Neither approach is without risks. The centrally-designed programs of the past have demonstrated that, if money is no object, we can deliver all the conservation that has been targeted. In a decentralized, locally-initiated approach to conservation, we will be challenged to deliver conservation more creatively and less expensively.

In any event, if we continue on the current course, BPA's available borrowing authority for directly-funded conservation programs will expire in three or four years. At that point, BPA will

have borrowed the remaining \$700 million for conservation, further exacerbating the upward pressure on its rates and worsening its competitive position. This situation could drive customers off the BPA system, thereby jeopardizing the agency's ability to repay its federal debt and fulfill its fish and wildlife responsibilities.

The Draft Plan proposes a reinvention of BPA's conservation program. In doing so it relies upon three key elements: "market transformation"; customer-initiated energy efficiency programs based upon integrated resource plans (IRPs); and demand-side products and services. PPC has been working with BPA, the Northwest Power Planning Council (Council), the Northwest Conservation Act Coalition and others to define these activities. We are approaching a consensus and expect to finalize regional IRP guidelines soon. PPC expects to recommend principles designed to gain regional consensus about approaches to "market transformation".

Despite PPC's optimism about the success of conservation reinvention in the region, we do have some concerns. As with any new system, the approach outlined in the Draft Plan may need fine-tuning. For example, we are troubled that the Draft Plan discussion about midcourse corrections may be read to permit a return to BPA centralized funding of all conservation. We do agree that if problems arise in the reinvented conservation world, some sort of corrective action may be needed. But centralized funding is not the answer.

The potential benefit of the reinvention lies in capturing the imagination and creativity of BPA's customers who are working on developing guidelines for IRPs with provisions for tracking and accountability. We believe that centralized programs should be limited to "market transformation" activities which are appropriately conducted at the regional level but that the creative efforts needed to make conservation reinvention work reside with the local utility boards and commissions. That creativity could be thwarted through intrusive directives and limitations on the self-governing authority of consumer-owned utilities.

We understand that there are those who doubt the conservation commitment of the region's public power systems. We intend to prove the doubters wrong.

(7) What steps should BPA be prepared to take if the Draft Plan's expected conservation achievements are not fulfilled?

BPA should be prepared to offer products and services designed to assist utilities to meet the targets, and Energy Service Charges (ESC) should be available to preference customers who wish to use this vehicle. Customer IRPs should help us to know whether utilities are on track to accomplish the conservation goals outlined in their IRPs. We do not believe that there should be any backsliding from the conservation reinvention goals. All signals to BPA and the customers should be to make reinvention work at the local level.

(8) Does BPA need new legislative authority or any changes in existing authorities to implement its conservation reinvention plans?

In order to implement the ESC, which is one of the cornerstones of BPA's conservation reinvention, we believe that Congress may need to take steps to authorize BPA to offer an ESC. PPC intends to initiate discussions with BPA to define ESC vehicles that may be tailored for easy utility use, and we expect to support any needed congressional action.

- (9) **What alternatives would you propose that would better achieve the region's conservation goals, while reducing the need for new BPA Treasury borrowing authority?**

The best approach to achieve the region's conservation goals, without new Treasury borrowing authority, is to place the responsibility for conservation resource development at the local utility level. This is appropriate because conservation involves working with end-use consumers and is thus an inherently retail activity.

- (10) **One key element in BPA's conservation reinvention is a requirement that its utility customers agree to a contractual requirement for integrated resource planning and efficiency action plans intended to acquire all cost effective conservation in each customer's service territory. Do you support such a requirement in principle? Do you believe it will have the effect of reaching the conservation goals set by the Northwest Power Planning Council?**

PPC supports the notion of contractually requiring integrated resource planning commitments. We have been working collaboratively to define guidelines that will assist customers in developing their IRPs. We believe that the Council's conservation goals will be met through the local utility IRP mechanism. The Council's goal, however, is regional and not utility-specific, while IRPs are very customer-specific and are intentionally designed to capture the details of local situations and opportunities. It will thus not be a simple matter to draw direct comparisons between local IRPs and a regional conservation plan.

- (11) **What are the implications of the Business Plan for the development of renewable energy resources?**

We are unsure about the implications of the Draft Plan for renewable resources, though in and of itself, it could have negligible effect. In the future, renewable resources will compete to serve markets transformed by competition, but affected as well by tax incentives, conditions of transmission access and new technologies. It is too early to tell how these will interact.

- (12) **What alternatives would you propose for treatment of the DSIs in a tiered wholesale electric power rate?**

Please refer to the answer to question 15.

- (13) **What other changes to BPA's tiered rate proposal would you suggest?**

PPC has adopted detailed positions with respect to tiered rates. Last winter, BPA's customers developed a set of principles for the implementation of tiered wholesale rates. Based on discussions with BPA, the customers modified the principles which were then incorporated into the agency's Draft Plan. The customers' goal is to assure a commercial foundation for a basic relationship with BPA that covers the purchase of power from the federal system. This commercial foundation is necessary for the customers to be able to make well-informed business decisions regarding the purchase of federal and non-federal power in the future.

The customers' approach to tiered rates is driven by the emerging characteristics of the changing wholesale market, which emphasize a contractual approach that balances the interests of

both buyer and seller in any long-term arrangement. Recent examples of the long-term approach include wholesale contracts with specific prices, as well as rates that are based on a specified pool of generating resources. These contracts support the significant financial investments necessary on both sides of any long-term arrangement, by minimizing, allocating and controlling the sources of uncertainty that face both buyers and sellers. The success of any long-term relationship between BPA and its wholesale customers in the Northwest depends on wholesale contractual arrangements that provide acceptable levels of certainty about rates and other terms and conditions of the sale.

We have been working with BPA on tiered rates, specifically on the details of implementation of the principles listed in the Draft Plan. Through this process, we have discovered that many of the principles are subject to various interpretations, and there remain significant differences of opinion between BPA and the customers on how tiered rates should be put into place.

For example, the customers had proposed, and thought that BPA had agreed, that Tier 1 be defined as a fixed set of resources, with the costs of those resources determining the Tier 1 rate. In our minds, a list of specific federal resources should be included in Tier 1, with short-term purchased power forming the basis of BPA's expected service to Tier 2 loads. On this issue, we even seem to have agreement from the environmental community. BPA, on the other hand, disagrees, apparently out of concern that the "cost basis" of Tier 2 would end up exceeding the market price, and thus will interfere with BPA's goal of using Tier 2 sales to build up financial reserves. We have offered several mechanisms to protect against risks in BPA's Tier 2 business line, and await BPA's response to our proposals.

In other areas, BPA's approach differs from that proposed by the preference customers. For example, PPC advocates that newly-formed preference utilities be offered the same rights to power from the federal system as are offered to preference customers at the time of the original determination of rights to purchase Tier 1 power, even though this would mean that all Tier 1 customers would give up some Tier 1 rights in this situation. BPA's approach would create in effect a "second class" of preference customers, those formed in the future, whose rights to the FBS would be more restricted than the rights of those preference utilities in existence today.

The bottom line here is a simple one: the preference customers are concerned that BPA's approach to tiered rates will not provide the basis for a long-term purchase relationship with BPA or protection of preference rights.

(14) Has BPA allowed enough time for public comment and participation in its tiered rate implementation schedule? Are you satisfied with the process to date?

Given the pace, complexity and number of changes called for in the Draft Plan, some have recently sought a slow-down of BPA's entire reinvention processes. At the same time, many preference customers are anxious to reach closure on issues that have been pending for months. A balance is therefore needed between timeliness and thoroughness. We believe we have reached such a delicate balance and now have an opportunity to meet the needs of the customers and of BPA.

Specifically, PPC and BPA have agreed to a sequencing of events for the next 14 months. The basic structure is this: Intensive contract negotiations will begin in early September with a target finish date in mid-December. A BPA general rate case is planned to commence after the first of the new year, with a target of October 1, 1995, as the date new rates become effective. Core

contract issues will be resolved and set in concrete by the December target date. If they are not, contingency arrangements will be necessary.

- (15) In the longer term, what relationship should BPA seek with its DSI customers? What changes would you suggest be made in new DSI power sales contracts?**

PPC advocates that no more than 75 percent of the DSIs' historical loads on BPA be used to determine their access to Tier 1 power, but BPA has concluded that several hundred average megawatts more should be used. We also believe that preference customers should have the option to recall service at Tier 1 to the DSIs in the event that further reductions in the capability of the FBS are required to assist migrating anadromous fish. In the new long-term business relationship with the DSIs, preference customers wish the variable industrial rate discontinued and a value of reserves payment based on competitive bidding. At the same time, we believe that the DSIs should have access to the transmission system on the same terms and conditions as other BPA customers.

- (16) What opportunities exist for BPA to expand its sales of power outside the region and the profits from those sales? Should Congress consider providing any new authorities that would allow BPA to maximize its returns on the sale of power surplus to regional needs?**

BPA already has significant, albeit statutorily limited, authorities to sell power outside of the region. PPC believes it premature to discuss amending these authorities until basic regional relationships are structured by means of new wholesale power sales contracts.

Thank you for the opportunity to testify before this Subcommittee.

Mr. DEFAZIO. Mr. Scott.

STATEMENT OF DANIEL C. SCOTT

Mr. SCOTT. I am Dan Scott. I am a commissioner from Mason County PUD No. 1 in Shelton, Washington.

I want to thank you for the opportunity to come back here and give my testimony about the BPA business plan and your committee's work on the subject. I would like to commend the committee for an excellent report. I think I am in whole-hearted agreement with it.

I represent both Mason PUDs and a group of utilities called the Aluminum Information Project. They include Mason 1; Mason PUD 3, also in Mason County, Washington; and five utilities from Oregon, which are the Canby Utility Board, Central Lincoln People's Utility District, Emerald People's Utility District, Salem Electric and the City of Cascade Locks.

The first thing I want to talk about a little bit is the business plan, and I want to emphasize that our utility is not unlike most utilities in the region. It seems to me that there are about 10,000 utilities that signed the agreements to build the WPPSS plant and that is kind of a good mark of what utilities are. Half a dozen of them fall into the Clark and Snohomish ilk, and probably 60 or 70 or even 80 are fairly closely paralleled to Mason 1.

We have 4,200 customers. We have absolutely no industrial load. We have a very small commercial load. We have a total of 17 employees; that includes meter readers to managers. So when they come out with a business plan that asks us to unbundle our services and possibly look elsewhere for our power, it makes me nervous because we simply don't have the ability to buy smart. We don't have the staff or the resources.

I think that Bonneville's business plan looks too heavily to the revenue enhancement side and not enough to the cost containment side. It is my experience from being in business that you can talk about revenue enhancement all you want, but you need to be competitive within. That is really what determines your competitiveness.

I'd like to talk about the DSIs and Bonneville's approach to serving them. We believe that they do get a subsidy. The 7C2 Delta indicates 300 and almost 60 million dollars per biennium. That is money that my ratepayers and all the ratepayers in the region pay to subsidize the DSIs. I think the DSIs provide an important service for Bonneville. They provide important jobs for the region, but those jobs are no more important than five jobs in a cabinet shop in Shelton or 50 jobs in a mill, in Omak, or jobs anywhere else in the region. I can't understand the idea of subsidizing them.

We should have an orderly approach to DSIs. We should offer them a contract that makes sense, both to them and to the region. And we should not eliminate preference in the process. Thank you very much.

Mr. DEFAZIO. Thank you.

[Prepared statement of Mr. Scott follows.]



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**HOUSE COMMITTEE ON NATURAL RESOURCES
Subcommittee on Oversight and Investigations
The Honorable Peter DeFazio
Washington, D.C.**

**TESTIMONY OF DANIEL C. SCOTT
Commissioner
Mason County Public Utility District No. 1
Shelton, Washington**

**ON BEHALF OF:
The Aluminum Information Project Utilities**

August 9, 1994

SUMMARY OF TESTIMONY

My name is Dan Scott. I am a commissioner of Mason County Public Utility District No. 1 in Shelton, Washington.

Thank you for inviting us to appear before you today.

In your invitation, you asked us whether the Bonneville Power Administration's draft Business Plan is consistent with this committee's BPA Task Force Report.

The short answer is no. The Task Force Report contains a series of forceful recommendations, including calls for Bonneville to reevaluate its long-standing relationship with the region's aluminum smelters. Unfortunately, Bonneville's draft Business Plan ignores those recommendations.

Furthermore, Bonneville's schedule for drafting new power sales agreements, unveiled only last week, is unrealistic. The schedule calls for drafting these contracts in only three months.

Bonneville says it does not need to prepare a separate environmental impact statement (EIS) on its contracts because the draft Business Plan covers the subject. But the Business Plan does not discuss contract options for the aluminum smelters at all, an issue which was addressed in prior federal court decisions holding that Bonneville must prepare an EIS for power sales agreements. (See pages 13-14 of this testimony for details.)

We fear that Bonneville's rushed effort will almost certainly fail or produce results that over time will harm the long-term interests of both Bonneville and the region's publicly-owned utilities.

The schedule also precludes this committee from conducting oversight hearings and continuing its valuable work. That ought to be as untenable to you as it is to us.

We see the need for change. We understand that the federal power system is facing significant problems, and we remain committed to working with Bonneville and other customers to address these challenges. But we need time to evaluate proposals and alternatives, and Bonneville's schedule does not allow us to do that.

The Aluminum Information Project

In the last year, Mason PUD No. 1 has been working with a group of other utilities on issues relating to the region's aluminum smelters and other Direct Service Industries (DSIs).

Our group is informally known as the Aluminum Information Project. In addition to Mason PUD No. 1, participants include Mason PUD No. 3 in Washington and five utilities in Oregon: the Canby Utility Board; Central Lincoln People's Utility District in Newport; Emerald People's Utility District in Eugene; Salem Electric and the City of Cascade Locks.

The purpose of our group is to analyze the existing Bonneville-DSI relationship and to press Bonneville to undertake the necessary analysis to ensure that future rates and contracts between the DSIs and Bonneville provide a net benefit to the region.

I am appearing today on behalf of the Aluminum Information Project utilities, and my comments reflect their concerns.

Why Mason County PUD cares about the DSIs

Mason PUD No. 1 serves approximately 4,200 customers, most of them residential. We have a very small commercial customer base and no industrial customers. Our utility was established in 1934 -- it was the first PUD in Washington State, and we recently celebrated our 60th anniversary.

Since 1959, Mason PUD No. 1 has been a full requirements Bonneville customer. We wish to remain so in the future.

Bonneville, however, appears to be "reinventing" itself in a way that is damaging to its long-term relationship with publicly-owned utilities. For example, Bonneville appears to have devoted more attention in recent months to ensuring the survival of the region's aluminum smelters than in ensuring that we survive.

Bonneville has concluded in the EIS for the draft Business Plan that:

In contrast to BPA's preference customers and IOU [investor-owned utility] customers, BPA has no statutory obligation to provide power to the DSIs beyond the term of their existing contracts [in 2001].
Page B-5.

But elsewhere in the EIS, Bonneville asserts that its new proposed pricing policies, compared with the status quo, will increase Bonneville's DSI firm load by 422 average megawatts (by making Bonneville power more attractive) and reduce the load of publicly-owned utilities by 140 average megawatts.¹

¹ See page 4-63 of the EIS. Public agency loads are reduced "primarily because of price-induced conservation and fuel-switching."

That seems backwards. If publicly-owned utilities are indeed Bonneville's preference customers, then its pricing changes and other policies ought to address our needs, as core customers.

Finally, the draft Business Plan raises so many questions about what Bonneville will actually charge for power that many utilities now question whether Bonneville can in fact remain a low-cost provider.

Although the Plan outlines a general approach to "tiered rates" and "unbundling," it contains few hard facts by which utility commissioners or general managers can evaluate Bonneville's proposals.

As a result, the Plan leaves the overall impression of being poorly thought out. If implemented, it may encourage publicly-owned utilities to leave the federal system.

Mason PUD No. 1 does not want to leave the federal system. Our load is only six average megawatts. We have 17 employees, and we have little ability and resources to "go it alone." Like many small and medium-sized utilities around the Pacific Northwest, we have no plans to build our own generating resources or buy power from independent producers.

The BPA Task Force Report

Mason PUD No. 1 and other Aluminum Information Project utilities endorse the House Committee on Natural Resources' BPA Task Force recommendations regarding the DSIs.²

We are pleased to see that the Task Force called on Bonneville to conduct a comprehensive analysis of the economic costs and benefits of continuing to serve the DSIs.³

Unfortunately, Bonneville has not responded to this recommendation nor has it agreed to undertake a request from the Aluminum Information Project to conduct a similar study of the DSIs.

² The DSIs consume approximately 3,200 average megawatts of electricity every year. Last year, the 10 smelters paid Bonneville about \$356 million for power. The smelters currently purchase electricity under a special variable industrial rate that fluctuates with the price of aluminum. The rate was implemented in 1986 and expires in 1996. Because the price of aluminum has been low in the last several years, Bonneville's revenue from the smelters is also down. The difference between Bonneville's projected cost of service and its revenue from the smelters is known as the "7(c)(2) delta." In fiscal year 1994, the projected delta is \$178 million. Most of those costs are shifted to publicly-owned utilities and to the residential and small farm customers of investor-owned utilities which buy power under the "priority firm" rate.

³ The Task Force report, "BPA at a Crossroads," page vi, concluded:

"BPA needs to conduct a comprehensive analysis of the economic costs and benefits to the Northwest of the region's aluminum industry, known as the direct service industries or DSIs. Based upon this analysis, a new rate structure should be designed for the DSIs that equitably balances the interests of the DSIs and all other regional ratepayers. Furthermore, Bonneville must prepare for the very real possibility that some of the individual DSIs may not survive the competitive challenges facing the industry in the near term."

In April 1994, we wrote Bonneville with suggestions for a study that would examine options for continued DSI service. We had meetings with Bonneville staff and followed up with letters to Administrator Randall Hardy, but no action was taken. That is where things stand today.

We are not suggesting that Bonneville decline to offer new agreements to the DSIs when the existing ones expire in 2001. We recognize that the DSIs provide certain benefits, such as reserves, to the federal system.

But we believe Bonneville has a legal responsibility to carefully examine future service to the DSIs.

Bonneville's reluctance to study the costs and benefits of continued DSI service is perplexing in light of the agency's purported new business approach.

Conclusion

The Aluminum Information Project utilities believe Bonneville is rushing to sign long-term power purchase contracts with the DSIs before first examining alternatives.

We fear that if Bonneville proceeds with its current approach, we will continue to subsidize the smelters and assume significant risks for continuing to serve them for years to come.

In the draft Business Plan, Bonneville assumes that any loss of DSI service is bad for the system (no matter when it occurs). It assumes that the DSIs should get a large assignment of cheap federal hydropower. And it assumes that DSI rates will remain lower than the rates of publicly-owned utilities.

We challenge those assumptions and request that Bonneville look at other options.

If Bonneville is to become more business like, then it ought to act more like a business. That means evaluating its relationship with the DSIs, placing more emphasis on cost containment and doing a better job of consulting with its customers.

To achieve those goals, we have two specific requests:

1. Congress needs to pressure Bonneville to examine its relationship with the DSIs as part of the overall Bonneville "reinvention." That means looking at new DSI contract options and alternatives, including more interruptibility, shorter-term agreements and other options identified in your Task Force report.

2. This committee should, as soon as possible, hold an oversight hearing in the region on the future of preference and Bonneville's continuing assault on the basic tenets of the Bonneville Project Act of 1937. The Act states that the Bonneville administrator shall "give preference and priority to public bodies and cooperatives" in disposing of power from federal dams.

We are alarmed at the present direction. A federal agency, bound in theory by statute, appears to have taken upon itself the reinvention of its priorities and duties. In so doing, it is whittling away its historical and legal responsibilities to core customers, the public bodies and cooperatives.

The bottom line, Mr. Chairman, is that the federal system was built for publicly-owned utilities and their customers. As preference customers, we deserve the best Bonneville has to offer, not the leftovers.

Thank you for asking us to testify.

SUPPLEMENTAL TESTIMONY

Part A contains a general discussion of Bonneville's draft Business Plan.

Part B contains answers to specific questions relating to the DSIs.

PART A: BONNEVILLE'S DRAFT BUSINESS PLAN

Bonneville released its draft Business Plan on June 29. Under the Plan, Bonneville proposes to adopt a "market approach" to selling power from the federal dams on the Columbia River system and other sources.

Those proposals are the most significant for the Pacific Northwest federal power system since Bonneville was first established 57 years ago.

The Business Plan, however, outlines only the general direction in which Bonneville wants to proceed. It contains little analysis of how these proposed changes will affect the power bills of utilities around the region.

1. Rate impacts for publicly-owned utilities

Bonneville insists it will examine rate impacts later -- during formal rate proceedings.

But how are utilities supposed to evaluate the Plan if they have no numbers and no basis by which to compare the alternatives?'

That's the chief problem with Bonneville's draft Business Plan. It proposes to launch major new changes but has not provided the information by which publicly-owned utilities can evaluate if they will be better or worse off under the new regime.⁵

At the heart of the Plan is this principle: Bonneville will treat all its customers alike by offering them equal access to a range of products and services.

Unfortunately, the thrust of the principle seriously weakens the rights of 121 publicly-owned utilities that rely on Bonneville for their supply of power. And it elevates the DSIs to a status traditionally accorded to publicly-owned utilities.

⁴ To understand how important these numbers are, imagine you rent a fully-furnished apartment for \$850 per month, including utilities. The landlord comes to you with an "offer" that will supposedly improve your situation. He proposes to rent the same apartment to you for \$500 per month but charge you separately for utilities, furniture, elevator, swimming pool and underground parking. But he won't tell you what these "unbundled" extras cost. How do you make your decision?

⁵ Larger publicly-owned utilities, investor-owned utilities and DSIs have the resources to move off the federal system. Typically, they do not need or want a "full meal" from Bonneville. Many small and medium-sized utilities, however, are interested in remaining full requirements customers of Bonneville.

At a time when the federal system is under a huge amount of stress and many publicly-owned utilities need more power, Bonneville proposes to continue selling large quantities of power to the DSIs -- even if it means encouraging utility customers to look elsewhere for their supply.

This problem is best illustrated by contrasting Bonneville's commitment in the Business Plan and related documents to maintain DSI load, no matter what.

Bonneville's preferred alternative -- its proposed action -- will use price signals to encourage some utility load growth to move off the federal system, and will similarly entice the DSIs to stay as Bonneville customers.⁶

If publicly-owned utilities are indeed Bonneville's preferred customers, then Bonneville must find ways of meeting their loads first, and if necessary, reducing DSI loads over time.

⁶ Total DSI firm load is projected to stay about the same, approximately 1,850 average megawatts, under either the status quo or market-based scenario. The issue is whether the DSIs buy Bonneville power or acquire their own resources.

2. DSI rates and contracts

Another problem is that the Plan and environmental impact statement (EIS) do not mention DSI rates. Why did Bonneville neglect to mention smelter rates?

Because Bonneville assumed that DSI rates would continue to be about 4 or 5 percent lower than preference rates in the future.⁷

But if Bonneville plans to develop new products and services, why would it not examine DSI revenues to assess whether the DSIs would, or should, pay more for Bonneville services?

The answer is that Bonneville apparently wants DSI rates to remain low because it wants to keep DSI loads on the system, no matter what.⁸

This discrepancy between the way Bonneville treats the publicly-owned utilities and the way it proposes to serve DSI load needs to be addressed.

⁷ This information was obtained from Bonneville staff but is not in the Plan itself.

⁸ The Draft Business Plan in Brief asserts: "Now more than ever there is considerable risk that some of the Northwest's aluminum plants may permanently close or operate intermittently....If our rates were to rise to around 35 mills, it is possible half of the aluminum smelters in the Northwest could go out of business. This would mean a huge loss of load to BPA -- around 1,450 average megawatts (aMW)." Page 5.

The Plan describes this as a "dire scenario" but does not analyze whether DSI load would gradually move off the federal system, thus alleviating any potential impact.

The Plan ought to look at other options for DSI service. Your Task Force Report identified some of those options, including greater interruptibility, seasonal power sales, shorter term contracts and other alternatives.

Bonneville has not examined those alternatives.

Despite those omissions, Bonneville says it intends to rely on the Business Plan and EIS to guide it in developing new power sales contracts with the DSIs and utility customers. It apparently believes that this EIS -- which contains no discussion of contract options -- is adequate to cover the contracts when they are drafted later this year.

Bonneville has lost two Ninth Circuit Court of Appeals decisions on the subject and ought to know better than to proceed with contracts before preparing an EIS that carefully examines contract alternatives.

In Port of Astoria, Oregon v. Hodel, 595 F.2d 467 (1979), the court ordered Bonneville to prepare an EIS for a new power sales contract with a proposed aluminum smelter in Warrenton, Oregon. Bonneville had argued that an EIS was unnecessary.

In Forelaws on Board v. Johnson, 743 F.2d 677 (1984), the issue was raised again. Bonneville claimed that Congress had intended to exempt it from the preparation of the EIS on new contracts when it passed the Northwest Power Act. The court ordered Bonneville to prepare an EIS on its power sales agreements. Bonneville took eight years to prepare the EIS, which was only released in January 1992.

The argument that Bonneville makes today is similar to the losing propositions in those cases. Here, unlike Port of Astoria or Forelaws, there is an existing EIS, done in preparation of Bonneville's draft Business Plan.

The problem is that the EIS contains no discussion of contract options, particularly for the DSIs. Topics, such as increased interruption of DSI service, which were covered in the 1992 EIS, have been ignored in the current impact statement.

Bonneville appears to have taken the position that the preparation of the EIS, never mind its contents, is sufficient. We question whether this is a sound interpretation of federal statute and court decisions, and we ask your assistance in making sure that Bonneville analyzes DSI contract options before it offers new long-term agreements to the aluminum smelters.

PART B: ANSWERS TO SPECIFIC QUESTIONS

Question 12: What alternatives would you propose for treatment of the DSIs in a tiered wholesale electric power rate?

Answer: Bonneville appears to be locked into a single approach to serving the DSIs in tiered rates: providing them with an assignment of 85 percent of historical loads in Tier 1, the cheap resource pool.

It is easy to understand why the DSIs want more Tier 1 power and less of the expensive Tier 2 power. The more cheap federal power they buy, the better off they are.

But if Bonneville removes the DSIs from paying for load growth and regional conservation, those costs are shifted to other customers.

Bonneville has not looked at alternative assignments, and has not evaluated whether a smaller assignment (e.g., 50 or 75 percent) would lower rates for publicly-owned utilities.

In sum, Bonneville needs to use the next three months (before the rate case) to consider alternatives to DSI service other than the 85 percent assignment.

It is difficult, if not impossible, to design tiered rates for the DSIs without first considering larger contract issues: What are Bonneville's legal obligation to the smelters? How are new preference customers treated under tiered rates?

Will new preference customers be allowed to obtain the same rights for Tier 1 power as existing preference customers? What happens to power that is assigned to a smelter which subsequently closes? Is it resold at market rates as part of the Tier 2 pool or returned to Tier 1 for use by existing and new preference customers?

Unless and until Bonneville confronts these issues, we believe it should not proceed with a tiered rate assignment for the DSIs.

Question 14: Has BPA allowed enough time for public comment and participation in its tiered rate implementation schedule? Are you satisfied with the process to date?

Answer: No. Although Bonneville's new schedule for tiered rates removes some of the frantic pressure on utilities and other interested parties, it still is inadequate.

Bonneville unveiled its draft tiered rate methodology only on July 14. Participants -- customers and other interested parties -- in its Tiered Rate Work Group offered comment on July 28.

Most of the publicly-owned utilities, including Mason PUD No. 1 and other Aluminum Instream Project Utilities, said they did not have sufficient information by which to evaluate Bonneville's draft methodology.

In part because of comments from numerous customers around the region, Bonneville announced last week that it would postpone the beginning of the new rate case by three months. Instead of beginning October 1, the rate case will now begin January 1.

Furthermore, Bonneville has abandoned its "bifurcated" approach, in which it intended to deal with methodology first and specific rates second. The revised Bonneville proposal calls for a "single track" approach.

Although we are pleased that Bonneville has postponed the rate case for three months, we fear that Bonneville will not reevaluate any of its assumptions in the intervening period.

The critical issue is not time, but Bonneville's commitment to consult the Work Group and ask it for a recommendation.

Our assessment is that Bonneville refuses to acknowledge its legal obligation to the Work Group, which was established as part of a settlement agreement in the 1993 rate case.

The hearing officer's (administrative law judge) order establishing the Work Group specifically said:

BPA shall commence a process to consider and possibly develop a tiered rate methodology, beginning in the Summer of 1993 and concluding prior to the start of BPA's next general rate case. The tiered rate process shall consist of two phases. The purpose of the process shall be to provide parties and interested persons an opportunity to engage in a cooperative effort to reach consensus on (a) a tiered rate methodology...and (b) whether or not tiered rates should be implemented.

See Administrator's Record of Decision, 1993 Final Rate Proposal, pages 136-137, and Appendix D for the complete order.

WP-93-A-02, page D-4.

The purpose of Phase 1 was to identify problems and concerns with tiered rates, establish potential tiered rate principles and develop tiered rate alternatives. Phase 2 was to evaluate various tiered rate options.

The order also said Phase 2 was to end no later than July 1, 1994, "with a BPA determination, based on recommendations from the work group (1) for a preferred methodology or methodologies, or (2) not to proceed with tiered rates."

The July deadline was not met in large part because Bonneville had not completed its work. It did not present its methodology to the Work Group until July 14, two weeks after the deadline.

Bonneville's postponement of the rate case until January 1 therefore gives the Work Group more time to review alternatives and fulfil its responsibilities.

But Bonneville has said it intends to proceed, no matter what the Work Group decides. In comments before the Public Power Council in Portland on Wednesday, August 3, Bonneville staff said the agency would proceed without a Work Group recommendation. The order does not require the Work Group to reach consensus, they said.

We concur that the Work Group is not required to reach consensus. But we disagree strenuously with Bonneville's statement that it is not required to ask the Work Group for a recommendation nor bound to accept its conclusions on whether to proceed with tiered rates.

Bonneville's interpretation renders the Work Group purely advisory. Under this approach, Bonneville could and would do whatever it wished. That is not what the order and the formal Administrator's Record of Decision state.

Question 15: In the longer term, what relationship should BPA seek with its DSI customers? What changes would you suggest be made in new DSI power sales contracts?

Answer: Bonneville needs to reevaluate and assess its entire relationship with the DSIs. Its draft Business Plan and accompanying documents have concluded that it has no statutory obligation to serve DSI load after 2001, when the existing contracts expire.

We therefore believe Bonneville has a "clean slate" by which it can draft new agreements. These agreements should recognize the vulnerability of some aluminum smelters, which are old and face competition from within the industry.

Specifically, we believe new DSI contracts should carefully examine the following general contract options:

1. Shorter-term contracts. Bonneville ought to offer a menu of possible contract options to the DSIs, including shorter agreements for companies that intend to close all or part of their operations in the next decade.

There is no reason that Bonneville should offer standard, 20-year agreements to all the smelters and commit itself to acquire power to meet the loads of companies with varying degrees of economic stability and efficiency.

2. Take or pay provisions. Bonneville ought to consider including some sort of provision that requires the DSIs to pay for the amount of power reserved for them during the contract term, whether used or not. If properly structured, these payments could discourage the DSIs from signing long-term agreements and then reducing or halting power purchases during the contract period. (At present, the DSI are required to give only one year's notice if they want to reduce operating demand.) Take or pay provisions would help make the DSIs more accountable.

3. Increased interruptibility. Make one or more quarters (quartiles) of DSI load interruptible. At present, only one quartile of DSI load is interruptible. The other three quarters -- approximately 2,400 average megawatts -- is considered firm.

What are the costs and benefits of alternatives, such as supplying the DSIs with one quartile of firm power and three quartiles of interruptible power?

4. Seasonal sales. Bonneville should consider selling firm power to the DSIs only during certain seasons. Instead of offering firm power year around, Bonneville could sell more firm power to the DSIs in spring and summer (when surplus) and less in winter (when needed by utilities).

DSI load is valuable to Bonneville in spring and summer. The reason is that Bonneville can sell firm power to the DSIs and receive revenue when the energy has little value to its utility customers. Furthermore, Bonneville also needs the water to run through the dams at this time for "fish flush" (migration of juvenile salmon downstream.)

Any one or combination of these alternatives could protect public preference and ensure that publicly-owned utilities do not subsidize the smelters or assume the risks of their continued operation in the Pacific Northwest.

Mr. DEFAZIO. Mr. David E. Piper.

STATEMENT OF DAVID E. PIPER

Mr. PIPER. Thank you, Mr. Chairman. Good morning, Mr. Smith. I appreciate being with you this morning.

I am Dave Piper, the General Manager of the Pacific Northwest Generating Cooperative. We are a cooperative generation transmission system; we have 29 rural electric distribution systems in Oregon, Washington and Idaho, and we serve as the power manager for those systems.

Our focus today is on competition, of course, and when we talk about competition, we worry about the retail level; we need to be competitive at the retail level, and from a rural cooperative perspective, our concern is not maybe the traditional one, because we have very few industries. We have primarily residential and agriculture communities.

We don't worry about alternative fuels because there really aren't alternative fuels in the rural area. What we worry about, from a competitive standpoint, is to be able to keep the rural economy viable, to keep rural jobs, to keep people from migrating to the cities.

This is important to us because cooperatives are traditionally lean. They do not have extensive staffs or resources. They have roughly 50 to 70 percent of their total costs represented by their power bills to BPA. So what Bonneville does will pretty much dictate what happens at the retail level.

We want Bonneville to be competitive and we want to be able to control our future in power supply. So with Bonneville in danger of being noncompetitive or uncompetitive at the wholesale level, absolutely. We believe in fact that Bonneville's predictions for the future on future rates are too low for their rates and they are too high as far as other resources are concerned. So basically, Bonneville is underestimating the problems that it has in the competitive sense for the future.

As an example, today, our organization is building a relatively small methane landfill project near Corvallis called Cofbin Buke, and that resource is projected to be competitive with today's Bonneville rate, not the tier 2, but today's PF over the long haul.

That is a resource that we are going ahead with, and we have given notice to Bonneville that that will be part of our take. We are also looking at purchase systems for other investor utilities in the region, and we are also participating in what is called the Northwest Resource Project. So resources are a fact of life. What we don't have is the certainty to be able to move ahead on some of them. I know that Bonneville is in competitive danger because in fact we intend to provide that at the wholesale level, provided it is cost-effective to do so.

Should the process at Bonneville be slowed down? I don't think so. Otherwise, we are looking as customers at a rate increase in October of 1995 that could be as high as 15 percent. The priority firm rate will provide a less competitive Bonneville if that occurs. Fifteen percent on top of what presently exists puts Bonneville into that uncompetitive fact situation very soon.

The real problem we have is how do we plan in this period of uncertainty, this state of flux that we are in right now. How do we decide what resources we need to purchase? We are doing an IRP right now; we are in the middle of it. When we get the results of that and as we go along, we need to know what resources to purchase; we need to know what conservation that we can effectively accomplish.

We need to develop the pools that will put all of this together economically. Until this rate case, until the contracts first get resolved and then the rate case, we don't know how we are going to do this. The competitive factors at the retail level aren't waiting for these resolutions, and we need to get ahead with this project.

I agree with the new direction that Bonneville is projecting here this morning with the schedule; I haven't seen it to know the details, but certainly the concepts are agreeable to me.

Our concerns with the business plan are outlined I think pretty well in the written testimony. I concur with Ms. Leone on the tiered rate comments. We in the rural areas are significantly exposed from a transmission perspective from what is called the fringe or the actual delivery to our member systems, and from transfer agreements. So we are concerned about transmission.

We need pooling; we need to be able to develop the economies of scale that are available to large systems, mitigate the risks that are available to it—that are facing us, and to be able to have the ability to buy and sell on a long-term basis.

Conservation is on the right track. It provides the right incentives. We are doing the IRPs; we are not going to do anything that isn't in the best interests of our member consumers. We have no purpose other than that. We are going to do cost-effective conservation.

We are worried about the present plan where the equity does not exist. Our members are PNGC, pay Bonneville \$150 million a year for conservation, get back about \$10 million of that in terms of benefits, as compared to Seattle City Light.

We are treading water right now until this is resolved, and our members are treading water. They are trying to stay competitive, the industry and the economics are changing rapidly and we need a resolution as fast as possible.

I appreciate your time.

Mr. DEFAZIO. Thank you.

[Prepared statement of Mr. Piper follows:]



Partners in Power Management

David E. Piper
 Testimony Before the
 Oversight and Investigations Subcommittee
 of the
 House Natural Resources Committee
 August 9, 1994

Mr. Chairman,

Good morning. My name is Dave Piper and I am the General Manager of the Pacific Northwest Generating Cooperative (PNGC), a generation and transmission company located in Portland, Oregon. PNGC is made up of twenty-nine rural electric cooperatives which serve over 500,000 customers in eight Western states. We continue to appreciate the Committee's help in exploring key changes affecting the energy future of the Northwest. I would also like to thank you and Congressman Smith for the opportunity to testify today.

The central question before the Committee today is a crucial one -- to what degree and how fast should change occur in the way Federal power is delivered in the Northwest. PNGC, as the power manager for its member systems, is vitally interested in the answer.

Competitiveness

We all have heard the word competitiveness a lot lately. While it has primarily been used in reference to The Bonneville Power Administration's (BPA) competitive position, we believe that the real focus should be on the competitiveness of Bonneville's customers. The farms, businesses and communities that depend on PNGC-member utility cooperatives do not operate in a vacuum. They increasingly operate in a global economy and have competitive problems of their own -- which we have a responsibility to help solve. Our goal is to position them well, not to serve some internal need to change the way Bonneville looks.

With that said, I do believe that BPA is heading in the right direction. If you look at the baggage that Bonneville is saddled with, you understand that they have no choice. Exponentially rising fish and wildlife costs, rock bottom world aluminum prices, continued drought, coupled with the emergence of low-cost generating alternatives such as gas combustion turbine projects presents the possibility that Bonneville customers will seek their power elsewhere.

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PNGC provides a good example of customer response to increasingly competitive energy markets. We have been very active in searching out alternative power suppliers and have a good understanding of what the market looks like. That search has been predicated on several factors. First, we believe that Bonneville's forecasts for future rate increases are too low and that the price of alternative resources will be even more competitive than now anticipated. In addition, uncertainty over future fish and wildlife and regionalized conservation costs make it easier to look at alternatives to Bonneville that do not have large unknowns attached to their cost structures.

Just last month, we broke ground on PNGC's Coffin Butte project. Located North of Corvallis, the project will run on methane gas recovered from a regional landfill, displacing several megawatts of Bonneville power. In addition to being a source of environmentally friendly renewable energy, we believe that Coffin Butte will operate at a levelized cost that is lower over the long-term than Bonneville's projected priority firm rate. There are other projects like it out there, and, coupled with low cost natural gas projects, we believe that Bonneville is in for some real competition.

Bonneville's reaction to this competitive pressure has been constructive. We applaud Randy Hardy for helping to build momentum to achieve structural change at Bonneville that will upgrade their customer service -- in terms of both rates and responsiveness. We do not want in any way to stall that momentum. Without it, we will not achieve the broadscale change necessary to keep Bonneville, and our customers, competitive.

Process for Change

The key question at this point is whether we have the information necessary to endorse the changes envisioned in Bonneville's Draft Business Plan. Unfortunately, the answer is that we do not have a good idea of what specific impacts they will have. The way to gain some certainty of what those impacts are, however, is not to stall the process, but to modify it.

PNGC strongly believes that Bonneville must make substantial progress in negotiating new customer contracts before proceeding with a new rate case. Again, we do not advocate a delay in the projected October, 1995 rate case completion date. We do believe, however, that in order to have that rate case make sense, it needs to be based on firm contractual commitments.

To that end, I have attached an outline produced by a review group of Bonneville customers for sequencing the business plan with the contract negotiation process. By timing the offering of new contracts with the issuance of a Record of Decision on the new rate case, we hope to be able to mesh the numbers with the proposed policy changes. In this way, we can make reasonable decisions based on real world considerations.

I am under no illusion that to get all of this work done by October, 1995 will be easy. That is the point. We need to keep the pressure on Bonneville to make meaningful changes and to lock those changes into contracts. If we can start contract negotiations now, it should be possible to have contract language to consider along with the rate case in January. We believe that linking up the contract negotiation and rate case processes will provide the customers timely information with which to view Bonneville's reinvention proposals while maintaining a meaningful deadline for moving forward.

In order to make good resource decisions for PNGC's future, we need to have some degree of certainty over Bonneville's future rate structure. Having the reinvention principles locked into customer contracts provides that certainty. Resource acquisition decisions at the utility level are long-term decisions -- taking into account a twenty or thirty year time frame. We need to have some assurance that, two years down the road, Bonneville will not use a new rate case to change its mind on the basic mechanics of its business plan. Without that certainty, PNGC and other utility players will be far less likely to commit to new resources -- whether they are conservation or generating resources.

Draft Business Plan

PNGC has reviewed the Draft Business Plan and has submitted comments to Bonneville (attached). In general, we are concerned that the plan is too preoccupied with finding new revenues rather than with controlling costs. In particular, it is vital that BPA institute an accounting system that can separate costs and revenues by its different business lines. We need to be assured that the services that BPA is offering its preference customers are cost-based. On the other major items, we have the following comments:

Tiered Rates -- The Draft Plan's implementation of tiered rates has substantial shortcomings. Consistent with the PPC tiered rate principles, which we endorse, the entire existing Federal Base System must be the only source of power and costs for Tier 1 service and rates. Individual customers will be less likely to invest in conservation programs to meet load growth if they are having to foot the bill for regionalized conservation measures funded out of tier 1. Subsidizing tier 2 power rates to keep them artificially low provides less incentive for Bonneville to acquire low-cost resources and provides less of a conservation incentive for utilities seeking to meet new loads.

In an increasingly competitive energy market, it is also important to remember that, by keeping the price of tier 1 low, a properly structured tiered rate system helps guarantee continued participation. This, in turn, guarantees ongoing debt repayment and fish and wildlife mitigation funding.

Transmission and Unbundling -- PNGC is vitally concerned that Bonneville will inhibit competition by retaining the ability to

manipulate non-power factors like access to transmission. For utility systems to truly have the ability to make independent resource decisions, Bonneville must provide access to transmission service that is cost-based. In addition, we believe that postage stamp rates based on the entire BPA transmission system, including so-called "fringe" and transfer agreements, should be included in "rolled in" average pricing for both existing and new resources.

It is increasingly important that we make sure we are comparing apples to apples as we discuss the impacts of unbundled services. BPA's stated goal of providing no increase in the tier 1 price over the current Priority Firm rate is misleading because tier 1 service will not include load shaping and other necessary products.

Pooling -- As part of the business plan implementation, BPA should enter into contracts directly with pooling organizations for tier 1 power, tier 2 power, and other products and services. Small utilities need to be able to take advantage of the economies of scale, risk mitigation, and efficiencies in resource operation available with pooling.

Conservation -- PNGC supports Bonneville's conservation program reinvention. We believe that the costs of the current conservation program are not borne equitably. Those utilities who get the benefit of conservation savings should bear their costs. A lack of commercial and industrial customers virtually guarantees that PNGC-member utilities will never get back what they put into the current program and will continue subsidizing larger urban systems. For instance, as the present system is configured, PNGC members annually contribute roughly \$150 million in revenues to Bonneville and get back roughly \$10 million in support of conservation programs. At the same time, Seattle City light pays Bonneville about \$40 million a year and gets that same \$40 million back.

A proper price signal, through implementation of a well structured tiered rate system, will provide ample incentive for us to acquire all cost-effective conservation and renewable resources. You must remember, cooperatives are locally controlled and operate without a profit motive. Our sole concern is providing the lowest-cost power to our members over the long-term. If that means acquiring additional conservation, then that is the path we will follow. The key is providing adequate planning information and the flexibility to permit an independent choice. PNGC is currently in the middle of preparing an Integrated Resource Plan. While we are required to do one as a condition of REA financing, we view it as an important tool in providing the lowest-cost resource acquisition possible.

We have been alarmed by calls for a strict "command and control" style approach to conservation acquisition complete with penalties and surcharges for not meeting preestablished conservation goals. We believe that these efforts would put BPA in a regulatory role that violates the principle of local control inherent to member-owned utility systems. It is a heavy-handed reaction that ignores the key point -- we want to acquire all cost-effective conservation

and are obtaining the information to determine what that is. We want Bonneville to help us to succeed in meeting the Regional Act's conservation goals rather than to engage in practices that interfere with our local decision-making prerogatives.

Conclusion

How far and how fast Bonneville should travel in the course of its reinvention is a complicated question. We believe the underlying competitive reasons for moving forward are sufficient to justify the effort to make Bonneville more cost conscious and more customer oriented. Implementation of a true tiered rate system remains the single most important component of a new competitive arena where customers have resource acquisition choices. While some may ultimately leave Bonneville, the competition alone will continue to drive the agency to become more efficient. A low-cost tier 1 will insure Federal debt repayment and fish and wildlife mitigation funding.

While much constructive work has gone into charting a new path for Bonneville, customers must know the long-term implications before choosing to support or oppose the new policies included in the Draft Business Plan. Key to that knowledge is making progress toward signing new long-term power supply contracts. By sequencing the next rate case with the offering of new contracts, Bonneville customers will have a much better basis on which to judge the application of the principles included in the Draft Business Plan.

PNGC has appreciated Bonneville's willingness to work together to define the road ahead and believes that delaying the process will hamper our ability to become more competitive -- as an industry and as a region. We do not support pushing back the rate case. Any such delay will also delay the day when we can adequately plan for our resource future. Without some sense of certainty, the industry will sit on its hands -- choosing to forestall decision making and delaying the ability to benefit from a more competitive energy market.

Again, thank you for the opportunity to testify today. We view this as a useful process and appreciate being included. I would be happy to answer any questions that you may have.

**Proposed Outline For Establishing
New Business Relationship**

A. Basic Sequence and Schedule.

1. August 1 - December 15, 1994 -- Negotiate complete contracts (to be offered after rate case).
2. October 10, 1994 -- BPA issues non-official "Preliminary Draft" rate design that looks as much like an Initial proposal as possible.
3. October 10 - December 23, 1994 -- Rate issue workshops.
4. January 9, 1995 -- BPA publishes single track rate case Initial Proposal, and a Federal Register Notice on the proposed new contracts.
5. January 9 - July 1, 1995 -- Formal rate case.
6. August 1, 1995 -- Rate ROD issued, BPA offers new contracts.
7. October 1, 1995 -- New rates and new contracts (for customers that accept them) become effective.

B. Negotiations and Rate Process.

1. Begin bilateral negotiations immediately between representatives of all customers and BPA segment managers in a customer driven process modeled after CRR Tiered Rates and Products and Pricing task force discussions. Target -- completed contracts by December 15, 1994.
2. Initially, the discussions should encompass all elements of the business relationship in order of importance without attempting to distinguish between contract and rate issues. Section C lists the key issues in the order to be resolved.
 - a. As negotiation progresses, rate issues will be identified (but will remain within the negotiation discussions until the Initial Proposal issues).
 - b. Issues common to all customers will be addressed and resolved first.
 - c. Separate discussions with customer classes and individual customers on unique issues may occur in parallel with main negotiations.
 - d. Non-customers are free to initiate their own informal discussions with BPA.

3. BPA's October 1994 "Preliminary Draft" proposal on Rate Design, Tiered Rates, Marginal Cost, Service Charges, Transmission and Cost of Service issues will kick off detailed informational workshops but will not be an initial proposal and will not require beginning of "ex-parte" rule.
4. The formal rate case (and "ex-parte" rule) starts on January 9, 1995. After customers and BPA have completed contract negotiations, any rate related contract issues requiring 7(i) approval become part of rate case.
5. Some changes to 7(i) process should be implemented for upcoming rate case and more fundamental changes must be developed for all future cases.
 - a. Allow for direct presentation to decisionmakers on more than one occasion.
 - b. Allow for contacts between parties and BPA staff (subject to notice, etc.) without the need for transcripts. Parties requesting opportunity for such contact will set the agenda and control input from other parties. Minutes of discussion to be kept and served on all parties.
 - c. Explore means to allow parties to respond to matters raised in staff briefings to decisionmakers (e.g., if different from staff testimony).
6. After Rate ROD issues, previously negotiated contracts are fine-tuned (e.g., if negotiated arrangement change due to 7(i) or to accommodate how BPA resolved purely rate issues) and offered to all customers.

C. Contract Issues.

No attempt will be made to segregate contract from rate issues initially; the parties to the contracts should be free to negotiate all elements of the business arrangement. After the fact, several issues may turn out to be susceptible only to a 7(i) process (e.g., actual numerical rate schedule changes); others may need 7(i) approval (e.g., cost allocation formulas the parties may agree to).

Negotiations should start with core issues important to all parties and proceed to non-core or customer unique issues.

1. Proposed Core Issues in very rough order of importance.
 - a. Define Tier 1 rights and obligations.
 - b. Define a couple of basic options for Tier 2 service.
 - c. Define flexibility rights.
 - d. Define key shaping services.

- e. Define basic transmission rights.
- f. Define purchase relationship (full, partial) and rules for switching.
- g. Define termination rights.
- h. Define billing determinants.
- i. Define basic pooling rights
- j. Create procedures for dispute resolutions and contract interpretation.
- k. Improve rate case procedures.

2. Non-Core

- a. Scheduling procedures.
- b. Billing procedures.
- c. Force majeure
- d. Share-the-shortage rights and obligations.....
- e. Planning insufficiency rights and obligations.
- f. Interruption rights.
- g. Standards for service.
- h. Exchange of planning and operation information.
- i. Exhibits and rules for revising.
- j. Relationship to other documents.

Note: Dispute Resolution, Contract Interpretation and Rate Case Procedures are listed at the end of the core issues. However, the development of a mutually satisfactory and fair method to resolve disputes and decide issues that must necessarily be left partially open, to adjust contracts for future events and assure timely performance is critical to a successful business arrangement. In addition, how parties decide to resolve failure disputes will have a significant effect on how much detail need be spelled out in the contracts at this time.



Partners in Power Management

BPA Public Involvement
P.O.Box 12999
Portland, OR 97212

August 3, 1994

Subject: BPA Draft Business Plan

Dear Sir or Madam,

INTRODUCTION

PNGC and its Member Rural Electric Cooperatives consider the BPA Business Plan and the fundamental changes that it envisions the most important policy development affecting BPA and its Customers in the last ten years. Allowing for changes in scale between BPA and Cooperatives, the many competitive challenges that BPA describes in the Business Plan are exceptionally real to your cooperative Customers. Therefore, we appreciate this opportunity to comment.

As stated above, we strongly agree with BPA in its description of the competitive challenges that we must confront over the next few years. Further, we believe that our businesses' continued success depends on BPA's success. We therefore support BPA's decision to vigorously pursue a restructuring of its business and the reinvention of its various business lines.

However, the Draft Business Plan narrative¹ has a fundamental shortcoming. It fails to adequately recognize the reverse of our competitiveness equation; that BPA's competitiveness is integrally dependent on its Customers' competitiveness. Throughout the document solutions to BPA's perceived problems are proposed and considered without adequate regard to the effects on, particularly, Cooperative Customers and our consumers. The discussion below on tiered rates is the most important example of this situation. If the implementation of the Business Plan is to be successful over the long term, BPA must more fully recognize this interrelationship and take a substantial portion of responsibility for its Cooperative Customers' competitiveness.

¹In the months leading up to publication of the Draft and in the weeks since, we have had many discussions with BPA staff that have assured us that BPA has not forgotten the interrelationship between BPA's and its Customers' competitiveness. However, the marked failure of the narrative to reflect these assurances and to describe a mutually satisfactory business relationship has been most disappointing.

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August 3, 1994

This shortcoming directly leads to the Draft's preoccupation with finding new revenues (from both existing and new customers) rather than with controlling costs. We recognize the cost control efforts in the Draft; but find them inadequate². These limited efforts seem more interested in apportioning pain rather than putting BPA and our industry on a sound and business-like path.

NEW RESOURCES & TIERED RATES

The primary source of increasing costs for our industry is the cost of new resources, both generation and conservation. BPA's Business Plan must provide a competitive environment to control these costs and must help remove both economic and political impediments for customer acquisition of resources. The Draft Plan's implementation of tiered rates and the reinvention of conservation have substantial shortcomings with respect to these goals.

1. The entire existing FBS³ must be the only source of power and costs for Tier 1 service and rates. All new resources including short term power purchases, other generation and all new conservation must be the only source of power and costs for Tier 2 service and rates. If the final Business Plan fails to make this clear separation between Tier 1 and Tier 2 then the competitive market and Customer acquisition of both generation and conservation resources will be short circuited.

Consider the negative effect on a Customer's conservation program from BPA's failure to keep all new conservation costs out of Tier 1 rates. A given customer could be paying for all of its

²PNGC and its Members recognize the many political pressures to continue excessive spending in a number of areas. We are committed to helping BPA with our Members of Congress to impress upon them the importance of making sound business decisions for BPA rather than continuing what is often perceived as "federal largesse".

³Here, the term FBS is used broadly. It may include some existing resources such as Idaho Falls, short term power purchases for the purpose of maintaining FBS capability in below critical water years, and possibly Tenaska.

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own new conservation costs with its own money; that is a "Customer-Tier 2" cost in their rates. At the same time BPA will be funding at the same Customer's Tier 1 expense another Customer's new conservation. The obvious unfairness of this situation could inhibit the (first) Customer from investing in its own conservation⁴.

A similar situation arises for generation. Consider the first Customer above investing in new generation at its own cost; that is as a Tier 2 cost. If BPA subsidizes a new BPA resource by placing some of its costs in Tier 1, this customer will end up paying some of another customer's Tier 2 cost. Again, independent resource acquisitions will be inhibited. There is another potential way for this inhibition to occur. The customer who wants to acquire its own generation could be concerned that BPA will subsidize its Tier 2 power sufficiently to keep the BPA Tier 2 rates below the customer's costs. Just the possibility of this occurring could prevent Customers from their own independent resource acquisitions.

Ultimately, BPA can not give itself the flexibility to include uncompetitive, or simply higher, tier 2 resource costs (conservation or generation) in Tier 1 power costs or our mutual goals for a competitive market and Customer acquisition of new resources won't work.

As to BPA's concern that at least ten percent of FY 1996 loads should be subject to the second tier, we note that according to BPA data on the December through March loads and resources of the federal system, at least fifteen percent of loads would be in Tier 2 under our approach during these winter months (based on the monthly average megawatts of power purchases). Since this is the load period that will strongly determine our new resource requirements, certainly BPA's concern is satisfied.

2. We see the issues of BPA's resource integration services, including transmission services, in the framework of providing a competitive environment for resource acquisitions. BPA should price these services at the same price for BPA resources as for Customer owned resources. BPA should not use these services to make its Tier 2 resources look more competitive than they are.

⁴Specifically, items 1a and 3b in the Conservation Reinvention Principles need work. First, market transformation funds must be limited; certainly, no more than \$10 million per year. And two, there can be no "forgiveness" of energy service charges. All new resource costs are Tier 2 costs; they must not be put in Tier 1 at any time.

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Specifically with respect to transmission, we believe that postage stamp rates based on the entire BPA regional transmission system, including so-called "fringe" and transfer agreements, should be included in "rolled-in" average pricing for both existing and new resources.

The ability to deliver federal and non-federal power at the same rate to an existing BPA power requirements customer's system is essential to the development of a competitive power market. If BPA can reach a utility for delivery of federal power, it should retain the responsibility to put in the arrangements necessary to reach such a system for wheeling purposes. Without this leveling of the playing field, the competitive power market will remain economically out of reach for all of BPA's requirements customers who are currently served via transfer arrangements. Because of the highly integrated nature of the transmission system, and the multiple uses and benefits of new and existing transmission facilities, identifying separate lines and facilities as the basis for transmission rates is difficult and contentious. BPA should offer transmission rates to both federal and non-federal users based on rolled-in, embedded costs. As facilities which were previously classified as "fringe facilities" come into wheeling use, the cost of these should be included in the "network segment" revenue requirement; preference customers should then be granted points of delivery at their systems (the same points where Federal power is delivered) under IR or other network transmission contracts.

The "single utility" principle should continue to guide BPA's transmission planning so as to avoid redundant investment. Costs associated with transferring power over third party systems may arise because the best plan of service requires use of facilities other than BPA's. These should be treated the same as BPA's transmission system costs and included, as appropriate, in either the BPA's wheeling or federal power revenue requirement. If new costs to transfer across non-federal systems are incurred as a result of a preference customer requesting wheeling service, these new costs should be treated in the same manner as if BPA had made an investment in new transmission plant to meet such request.

3. The ability to pool all loads and resources within a pooling organization is critical if small utilities are to be competitive with BPA and other organizations in resource acquisitions. BPA should enter into contracts directly with the pooling organization (including wholesale power utilities - e.g. G&Ts) for Tier 1 power, BPA Tier 2 power (if purchased by the pooling organization) and all integration services.

Small utilities need to be able to take advantage of economies of scale and efficiencies in resource operations and acquisitions the same as large systems. In order to do this, co-ops must

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be able to do real-time scheduling and marketing of power to minimize costs and take advantage of load diversity. Advantages to BPA include administrative benefits of working with fewer organizations and the very important competitive yardstick that pooling organizations will provide for BPA's own new resource activities.

Without pooling, take-or-pay obligations for power would be unfair to small utilities. Some small utility loads are much more volatile than for the generally more diverse loads of large utilities. One large industrial load can go away overnight for a small utility. Some small utilities have large proportions of their loads in one rate class that have homogeneous reactions to economics or weather. The small utility will find it virtually impossible to effectively mitigate the financial risk of take-or-pay provisions in the manner of large utilities or pools.

BPA insists on being able to operate its system on an integrated basis, but is dragging its feet on letting small systems pool together to operate their combined system on an integrated basis. PNGC's proposed tiered rate implementation does not preclude BPA from operating as it wants. We only require a reasonable accounting of costs.

4. In order to acquire resources, Cooperatives will need to do Integrated Resource Plans (IRPs). It is important to us that BPA should not include any provisions in our power sales contracts that would constrain us from meeting our social goals with respect to generation or conservation. The authorities of BPA and the Council should not be expanded beyond what was required by the Act. Local control remains important for Cooperatives and an effective way for us to stay competitive at the retail level. Additionally, it is important that BPA not interfere in the IRP requirements from the Rural Electric Administration (REA).

CONTROLLING COSTS

Controlling costs must become a way of life for the restructured BPA; it must become part of the corporate culture. This must be accomplished if BPA and its Customers are to be competitive. Market forces and non-market measures must be brought to bear.

1. We suggest, as others have, that BPA should institute an accounting system that can separate costs and revenues by its different business lines. Your Customers must be satisfied that they are not paying for other entities' services. The various business lines (transmission, Tier 1 power, Tier 2 power --including purchases, specific resources and load growth services--, resource integration services and conservation --DSM--) must sink or swim on their own. If one is found to be uncompetitive, costs will be cut, or the business line will close up shop.

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2. Another suggestion for controlling costs is to develop measures of effectiveness where market forces do not exist. Specifically in the Fish & Wildlife arena, BPA must prove to itself as well as to its Customers and the public at large, that its expenditures are cost effective. We believe that some measures for fish have actually been counter-productive; for example the recent additional spill program. We believe that other programs have not been cost effective when compared to alternative measures; for example flows versus transportation. As your customer survey revealed, BPA has been slow to take this type of Customer advice. We recommend that your final Business Plan remedy this situation.

REALLOCATION OF COSTS

The draft Business Plan is notable for what it includes as well as what is left out. If the aim of this process is to put both Bonneville and its customers on a more competitive footing, the agency should not overlook major opportunities to mitigate increased rate pressure.

Section 4 (h) (10) (C) of the Northwest Power Act directs BPA to treat expenditures in excess of the power share of a hydroelectric project's cost "as payments for other project costs for which BPA is responsible under the law." This provision provides clear direction to the Administrator to allocate a share of the fish and wildlife expenses of multipurpose facilities to project purposes other than power production. Those expenses are to be borne by the taxpayers rather than the ratepayers and should offset a portion of BPA's annual Treasury payment.

Section 4 (h) (10) (C) is applicable to past, present and future expenditures and adds up to a significant dollar amount. Since passage of the Northwest Power Act, Bonneville has reportedly spent \$270-\$325 million on fish and wildlife mitigation that is attributable to non-power project purposes. In addition, it continues to add to that total by at least \$50 million a year.

As part of Bonneville's reinvention or by separate action, PNGC urges the Administrator to exercise his responsibility under Section 4 (h) (10) (C). While BPA has ignored this requirement in the past, exponentially rising fish and wildlife costs pose a significant threat to the future of competitiveness of the agency and its customers.

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OTHER ISSUES

A variety of other issues concern us in our desire to see that we and BPA are competitive.

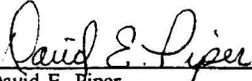
1. Exchanging IOUs could receive a windfall from the implementation of Tiered Rates. We believe that reform of the Residential Exchange is mandatory to prevent this.
2. The Low Density Discount, mandated by the Regional Power Act, is also an essential element of our competitiveness. Any changes contemplated in the LDD should not hurt our competitiveness, should take into account the purposes of the Act and should be done in consultation with your Cooperative Customers.
3. The DSIs may also receive a windfall from the implementation of tiered rates; that is they may escape sharing in some of the costs of load growth. We believe that BPA should neither discriminate in favor, nor against, the DSIs relative to Public Utility industrial consumers. BPA should institute whatever reforms are necessary to put the DSIs on a par with other industrial consumers in consultation with your other Customers.
4. Finally, it is our strongly held opinion that the complexity and risks of the BPA restructuring and the implementation of tiered rates requires that we negotiate new power sales contracts before the next rate case. We simply must have contractual guarantees as to our business relationship and pricing methodologies. A genuine partnership between BPA and its Customers can permit nothing less.

CONCLUSION

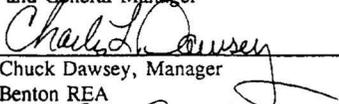
The Business Plan, the restructuring of BPA and the challenging new environment in which we find ourselves are all terribly complex. It is not possible in one letter to fully communicate our concerns or our ideas. Particularly in the area of tiered rates implementation, we have additional thoughts that may be helpful. We look forward to the additional opportunities to exchange information to which the BPA staff have committed. The PNGC staff and the undersigned are eager to answer your questions or continue discussions at your convenience. Again, thank you for this opportunity to comment on the Draft Business Plan.

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August 3, 1994

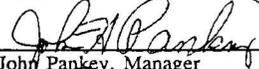
Sincerely,



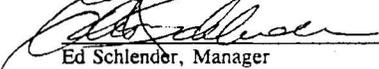
David E. Piper
Executive Vice President
and General Manager



Chuck Dawsey, Manager
Benton REA



John Pankey, Manager
Clearwater Power Company



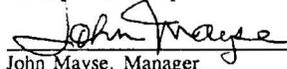
Ed Schlender, Manager
Coos-Curry Electric Co-op



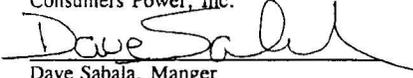
Lane Powell, President
Manager, Central Electric Co-op



Jim Ramseyer, Manager
Blachly Lane Co-op



John Mayse, Manager
Consumers Power, Inc.

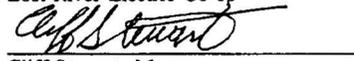


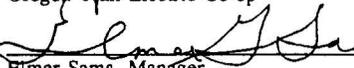
Dave Sabala, Manger
Douglas Electric Co-op

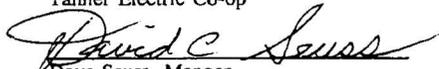
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Burton Phillips, Director
Fall River Rural Electric

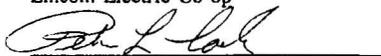

Lew Greene, Manager
Lost River Electric Co-op


Cliff Stewart, Manger
Oregon Trail Electric Co-op

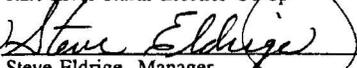

Elmer Sams, Manager
Tanner Electric Co-op


Dave Seuss, Manger
West Oregon Electric Co-op


Bill Graedel, Director
Lincoln Electric Co-op


Peter Cook, Director
Lower Valley Power & Light


Bud Tracy, Manager
Raft River Rural Electric Co-op


Steve Eldridge, Manager
Umatilla Electric Co-op

STATEMENT OF JUDY LAMSON

Mr. DEFAZIO. And finally, Ms. Lamson.

Mr. LAMSON. Good morning, Mr. Chairman and Mr. Smith. My name is Judy Lamson, and I am a policy specialist with the Washington Utilities and Transportation Commission.

We very much appreciate the opportunity to present the Commission's views this morning. In the Commission's role as regulators of IOUs, we are very concerned with BPA's treatment of the residential and small farm customers of these IOUs. Both the business plan and the proposed tier-rate methodology would impose an arbitrary limit on the rights of these customers to the Federal-based system.

Let's look at the history of the Power Act, its original intent and the facts as they are today. Prior to the passage of the act, regional interests were competing for access to BPA's limited, low-cost energy resources.

Because at that time BPA was not authorized to acquire new resources, BPA was forced to notify its customers that it had insufficient power to meet their needs. BPA initiated a process to allocate that limited Federal power to cover a fraction of each customer's load.

At the same time, customers of IOUs were using indirect methods to gain the same access to the low-cost Federal resources as their neighbors served by public utilities. I think many of you in the room today are familiar with the State of Oregon's creation of the Domestic and Rural Power Authority and the City of Portland's litigation in this area.

The act was designed to resolve these problems, to provide equal access to the Federal base system and to allow BPA to acquire new resources. The act specifically gave residential customers of all regional utilities, both public and IOUs, direct access to low-cost Federal power through a priority firm rate.

Unlike the other public utilities, the IOUs are required to offer something in return for this access: An adequate power supply at the reasonable cost. The IOUs must offer to sell BPA an equivalent amount of power at their average system cost, well below what it would have cost BPA to acquire new resources.

The Direct Service Industries, or DSIs recognized at that time that their contracts to the existing Federal system were about to expire and traded planning certainty in the long run for quote, "dramatically higher rates and substantially lower power quality," close quote. That was a statement made by a DSI witness testifying on the Power Act before the Subcommittee on Energy and Power back in 1979.

Using the projections prepared by BPA in 1979, attached to the Senate committee report on the Power Act from that same year, the Commission has estimated the rate distortion that has transpired since the passage of the Power Act. The results are startling. The IOU customers are receiving less than one-third the benefits intended to be achieved by the act.

In 1986, BPA offered the aluminum smelters a special variable rate which is currently 21 mills per kilowatt. BPA argues that without that special rate, it might have lost up to 1000 megawatts of industrial load. Meanwhile, one of our IOUs, Puget Sound Power

and Light Company, is purchasing 500 megawatts of power from new resources at twice the price of the current variable rate, about 42 mills per kilowatt hour.

We recognize that maintaining the viability of the DSIs is an important public policy issue. We are urging, however, that as we consider the future of BPA, we look at the entire economic picture, and balance the interests of all of the stakeholders in the region.

Let's look at what might have transpired if BPA had not chosen to offer a variable rate to the DSIs and see how much money BPA could have saved. If BPA had offered 500 megawatts of power to Puget at the current nonvariable industrial rate of 27 mills per kilowatt hour, instead of selling it to the DSIs at the variable rate of 21 mills per kilowatt hour, BPA would have received an additional \$28 million per year in revenue. Without the variable rate, BPA would be serving the remaining aluminum load and others at the regular industrial rate, receiving an additional \$114 million per year in revenue. That is not all.

Puget would be buying that BPA power for about 15 mills per kilowatt hour less than Puget is now paying other suppliers, and Puget would be saving about \$72 million per year. This would lower Puget's average system cost to an approximately \$35 million reduction in BPA's annual purchased power expense through the residential exchange. In total, BPA could have saved about \$178 million in 1994.

In summary, I would like to make the following points: first, we expect BPA to recognize the IOU residential and small farm customers of IOUs have the same rights to the Federal base system as do the customers of public utilities. BPA's sale of power to IOUs is at cost-based rates. It is not a subsidy.

Second, we expect BPA to recognize the exchange power purchase for what it is, a lowest cost, highest quality of any major resource acquisition BPA has made since passage of the act.

Third, we expect BPA to cease treating the difference between its power sales revenue and its purchased power expense related to the exchange as a net cost subject to management control in the same manner as overhead.

Fourth, if BPA proposes to provide the DSIs with low-cost power, they should be prepared to consider low-service quality, such as through more interruptible power or other options to ensure that all customer classes cover their cost of service. This matching of service quality with costs to serve should be done before the new contracts are executed.

We appreciate the efforts of this oversight committee and Congressman DeFazio's task force in ensuring the continued accountability of the Bonneville Power Administration, and we thank you again for the opportunity to present our views.

Mr. DEFAZIO. Thank you.

[Prepared statement of Judy Lamson follows:]

TESTIMONY OF
JUDY LAMSON, POLICY SPECIALIST
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION
before the
U.S. HOUSE OF REPRESENTATIVES
COMMITTEE ON NATURAL RESOURCES
SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS
"BPA at a Crossroads"
August 9, 1994

Thank you for the opportunity to present the views of the Washington Utilities Transportation Commission at such a timely hearing on issues that are of critical importance to the citizens of the Northwest.

The Washington Utilities and Transportation Commission, or WUTC, regulates the investor-owned utilities in Washington. These utilities serve about 55% of the population of the state, or about 2 1/2 million people. The remaining population is served by municipal utilities, public utility districts, electric cooperatives, and mutual power companies. In our role as regulators of investor-owned utilities, or IOUs, we are very concerned with BPA's treatment of the residential and small farm customers of these "IOUs."

Under the Pacific Northwest Electric Power Planning and Conservation Act (the Power Act), these customers are provided equal access to the benefits of the federal hydropower system through an "exchange" program. This exchange will be the focus of our testimony. We will leave detailed comments on BPA's conservation programs and fish and wildlife obligations to others. The WUTC and other state agencies are continuing to review BPA's business plan and will have additional comments in the future which we will share with the Committee.

We are becoming increasingly concerned that the Bonneville Power Administration has lost sight of the charges that Congress imparted it in 1980 under the Power Act. The Power Act's primary purposes are to encourage conservation and renewable resources, to protect anadromous fisheries, to provide for an adequate regional power supply, to ensure public participation in energy decisionmaking, and to provide equal access to the benefits of

the federal hydropower system to ALL citizens of the region for their domestic and small farm needs.

BPA's draft business plan contains many desirable elements, such as efficiency improvements, a streamlined bureaucratic process, unbundling and repricing of certain products and services, and offering of additional and more specialized products and services. While proposing to implement these improvements, however, BPA has lost sight of the origins of the residential exchange program, how it benefits BPA, and what the alternatives to this program were at the time the exchange program was created by Congress.

I would like to focus at this point on the history of the Power Act, its original intent, and the facts as they are today.

THE REGIONAL ENERGY PICTURE PRIOR TO THE ACT

Prior to the passage of the Act, the regional interests were competing for the right to BPA's limited low-cost energy resources. At that time, Bonneville was not authorized to acquire new resources to meet increasing demands. Bonneville would have been forced to allocate each utility's share of federal power to a fraction of its load. In fact, BPA initiated such an allocation process in 1979 to do just that. The public utilities and the Direct Services Industries (DSIs) opposed such an allocation and supported Bonneville's efforts to obtain authority from Congress to acquire additional resources, thus avoiding allocation.

Without the Act, BPA may well have been obligated to serve the residential customers of the IOUs through indirect methods. The state of Oregon had created a new public utility, the Domestic and Rural Power Authority, to purchase power from BPA to serve residential customers in Oregon. The city of Portland had filed suit seeking the right to acquire low-cost resources from BPA for its residents and municipal facilities. In both of those cases, BPA would have been required to serve additional customers at the same rate it served the public utilities, but without the benefits of the lower-priced exchange power. Furthermore, either of these would have meant less cheap power for the public utilities.

At the same time, BPA had notified its customers that it had insufficient resources to meet their requirements, and BPA's contracts with the direct service industries were about to expire. The DSIs were concerned enough that BPA would not have enough power to serve them that they had contracted to buy a portion of the output of the now-terminated WPPSS nuclear plants 4 and 5.

THE POWER ACT WAS PASSED - SOLVING THE PROBLEMS

The Act was designed to resolve these problems. It gave the residential customers of ALL regional utilities access to low-cost federal power. The Act allowed BPA to purchase additional resources needed to serve load growth, and it created the residential exchange program to provide BPA with a large and assured low-cost resource. The DSIs gave up their

contractual rights, which were about to expire, to the existing federal system, in exchange for new, long-term contracts at higher rates. The DSIs specifically recognized that planning certainty in the long-run was worth "dramatically higher rates and substantially lower power quality." That was a statement made by a DSI witness testifying on the Power Act before the Subcommittee on Energy and Power in 1979. BPA appears to be forgetting these very important facts.

The legislative history of the Act is replete with members' statements on how the resource allocation and rate construct of the Act were designed to assure residential customers lower cost power and to provide the industrial customers with higher cost power. Senators Hatfield, Packwood, Jackson, and McClure, and Representatives Ullman, Duncan, Moorhead, Kazen, and Dingell all spoke specifically about how the Act was to result in lower rates for residential customers, including those of the IOUs, and higher rates for industrial customers. Attachment 1 includes excerpts of these comments.

The residential exchange program was a part of the process to assure BPA an adequate power supply and to avoid allocating limited resources. The investor-owned utilities did not seek the exchange -- they would have preferred to be customers of BPA just like the public utilities, simply purchasing power for the IOU residential and small farm loads. That would have allowed the IOUs to avoid high-cost new resources planned at that time, such as Colstrip 3 and 4, Valmy, Boardman, Skagit, Pebble Springs, Creston, and so forth, all of which were expected to cost much more than the "average system cost" rate at which the exchange program requires the IOUs to sell power to BPA.

Under the Act, the "priority firm" rate class was established, consisting of the "general requirements" of the public utilities and federal agencies, plus the residential and small farm loads of the IOUs. This class of customers is entitled to be served with BPA's lowest-cost power resources. First, this customer class is entitled to 100 percent of the "federal base system" resources, BPA's cheapest. When the first source is exhausted, this customer class then receives service from the power BPA buys under the residential exchange agreements. Only if these sources are insufficient will the public utilities and residential customers be served with new, higher-cost resources.

Under the residential exchange program, BPA sells power to the investor-owned utilities in an amount sufficient to serve the IOU residential loads at the Priority Firm rate, the same rate schedule available to public utilities under section 7(b) of the Power Act. Unlike the public utilities, however, the investor-owned utilities must offer something in return: they must offer to sell BPA an equivalent amount of power at their average system cost. (Section 5(c)(1) of the Power Act.) BPA has the option -- but not the obligation -- to purchase this energy. (Section 5(c)(5) of the Power Act.)

RESOURCE ALLOCATIONS UNDER THE ACT

BPA currently meets its priority firm load with about 8000 megawatts of power from the federal base system, plus about 2000 megawatts from exchange purchases. Without the power which BPA purchases under the exchange agreements, BPA would have faced a massive power deficit beginning in 1981 and probably would have been forced to complete high-cost resources, such as WPPSS nuclear plants 1 and 3. The result would have been much higher rates for the public utilities, the DSIs, and all other BPA customers. The exchange is saving BPA customers hundreds of millions of dollars per year compared with the higher-cost resources BPA would otherwise have acquired.

Under the Act, BPA's non-priority customers, including DSIs, are served with resources not assigned to the priority-firm pool. These resources include the exchange, surplus, and new resources. Currently, the DSIs receive one fourth of their power on an interruptible basis from surplus hydro when available. The remaining three-quarters is served 86% with BPA purchases from the residential exchange, and 14% with new resources BPA has acquired from various sources. The cost of providing these resources, plus transmission and conservation costs allocated to the DSIs, adds up to about \$700 million per year. (BPA 1993 Wholesale Power Rate Development Study, Table 14.) However, the DSIs pay only about \$500 million per year to BPA for this power. This is largely due to the fact that the variable rate which the DSIs pay is tied to the world aluminum market price, which has remained depressed. Thus, the cost to provide DSI service is forecast to cost nearly \$200 million more than the DSIs will pay for power.

EXPECTATIONS UNDER THE ACT -- AND REALITY

We've reviewed the projections prepared by BPA and attached to the Senate Committee Report on the Power Act (Report No. 96-272, July 30, 1979, Appendix B), and we've made some simple calculations based on those projections. The General Accounting Office report "Impacts and Implications of the Northwest Power Bill" (1979) includes a graphic depiction of the expected rates for each class of Bonneville customers. A copy of that graph is included in Attachment 2.

When Congress passed the Power Act, residential customers of private, or investor-owned, utilities were expected to receive some \$650 million per year in benefits from the exchange program as of 1994. Instead, the current benefits are less than \$200 million per year. Even adjusted for the lower-than-forecast loads, the exchange benefit would have been \$450 million for 1994.

In BPA's 1979 forecast, the cost of power purchases projected from the residential exchange for 1994 were expected to average about 34 mills/kwh, and the priority firm rate was expected to average about 22 mills/kwh, so that residential customers were expected to receive an approximate 12 mill/kwh benefit under the exchange. Instead, BPA is paying only on the order of 32 mills for the exchange power, and today's priority firm rate is about

28 mills, so that the residential customers receive only a 4 mill/kwh benefit under the exchange.

On the other hand, for 1994, it was expected that the DSIs would pay 10 mills/kwh more than the expected priority firm rate paid by public utilities and residential customers, or \$400 million per year more than the priority firm rate. Adjusted for the lower loads which actually materialized, the DSIs would have paid \$240 million over and above the priority firm rate. Instead, the DSIs today are paying much less than the priority firm rate -- by more than \$100 million. Today's priority firm rate of 28 mills/kwh is 7 mills more than the DSI rate of 21 mills/kwh.

Today, the residential ratepayers are paying a lot more than was intended when the Power Act was passed, and the DSIs are paying a lot less than intended. The residential customers are receiving **less than one-third** of the financial benefits intended by Congress. The DSIs are the only customer group paying less than intended. BPA's proposal to limit the exchange included in its Business Plan, would only exacerbate this distortion.

WHY ARE THINGS SO DISTORTED?

The origin of the current rate distortion is in a 1984 amendment to the Average System Cost methodology approved by BPA without engaging in the consultative process with the state Commissions or the Northwest Power Planning Council as directed by Congress in section 5(c)(7) of the Power Act. In that decision, BPA removed the equity return and federal income tax from the price it pays to the IOUs for power. In effect, BPA now requires the IOUs to offer BPA power below the IOUs' cost as a precondition to purchase power from BPA at BPA's cost to serve the IOUs' residential customers. If anything, the residential exchange is a subsidy of Bonneville by the residential customers of the IOUs, who must pay not only the full cost of BPA power in rates, but also the equity return and federal income taxes associated with the IOUs' power resources.

Not only is BPA buying power from the IOUs below cost, but BPA is receiving far less from the DSIs than projected, largely due to the Variable Industrial rate paid by the DSIs, as discussed above.

BPA COULD ENHANCE REVENUES WITH SALES TO INVESTOR OWNED UTILITIES

In 1986, BPA offered the aluminum smelters a special "variable" rate, tied to the world price of aluminum. BPA has argued that, without the special rate, it might have lost up to 1000 mw of industrial load. Currently, the DSIs are paying about 21 mills/kwh for power under this rate. Meanwhile, Puget Sound Power & Light Company is purchasing over 500 megawatts of power from new resources at prices of around 42 mills/kwh. We recognize that maintaining the viability of the DSIs is an important public policy issue. We are urging, however, that as we consider the future of BPA rates, we look at the entire

economic picture and protect the interests of exchange customers. Let's look at what might have transpired if BPA had not chosen to offer a variable rate to the DSIs.

If, instead of offering the DSIs a variable rate, BPA had offered power to Puget and others at the regular, non-variable DSI rate, and Puget and other utilities had purchased that power instead of purchasing contracts for gas-fired power, both Puget and BPA would be better off.

BPA would now be selling Puget about 500 megawatts of power at the current non-variable Industrial Power (IP) rate of 27 mills/kwh, instead of the Variable Industrial (VI) rate of 21 mills/kwh, and would therefore be receiving an additional \$28 million year in revenue. But that's not all. Since BPA would not have offered the variable rate, BPA also would be serving the remaining aluminum load and selling power to others at the regular Industrial Power rate, rather than the Variable Industrial rate. BPA would be receiving an additional \$114 million per year in revenue from those sales. That's still not all.

Puget would be buying that BPA power for about 15 mills/kwh less than Puget is now paying other suppliers, and Puget would be saving about \$72 million per year. Since about half of Puget's load is residential, Puget sells about half of its power to BPA, so the \$72 million reduction in Puget's power cost would result in a \$35 million reduction in BPA's purchased power expense through the residential exchange.

Altogether BPA would have been much better off had it sold power to Puget at the regular industrial power rate rather than selling to the DSIs at the lower variable rate. BPA would be receiving \$28 million in extra revenue from power sales to Puget, \$114 million in extra revenue from higher-priced sales to aluminum smelters and \$35 million in savings in purchased power costs through the exchange. Altogether, offering power to Puget at the regular DSI rate instead of offering the variable rate to the DSIs could have saved BPA about \$178 million for 1994.

WHERE DO WE GO FROM HERE?

In view of this serious shortfall in benefits to the residential customers of the region compared with what Congress expected and intended, one would hope that BPA's new "reinvention" activities would include restoring the residential exchange to expected levels in a manner mutually beneficial to both BPA and the IOUs. One would expect BPA to be looking for ways to bring its cost of service into balance with the rates it charges all customers. In fact, we are finding exactly the contrary. BPA's Business Plan and its preliminary tiered rates methodology appear directed at exactly the opposite result.

First, the draft Business Plan carries an explicit goal of holding down the residential exchange benefits to \$200 million per year, less than a third of what BPA forecast at the time Congress was considering the Power Act. There is absolutely no logic or methodology to the proposed target, and it bears no relationship to any change in either BPA power supply

costs or exchange utility power supply cost. BPA's own recent forecast of exchange benefits over the next seven years is in the \$285 - \$350 million per year range, and we expect those benefits to be received. A copy of that forecast is included in Attachment 3.

Second, BPA's July 1994 Preliminary Draft Tiered Rates Methodology proposal utterly fails to recognize the residential customers as a legitimate component of BPA's obligation to provide service from the existing federal system. This is in direct conflict with sections 5(b)(1) and 7(b) of the Act. BPA's Tiered Rates proposal would allocate the "existing system" among the public utilities and the DSIs. The exchange customers would only be given access to power at undefined tier one rates, with no specific link to the federal base resources. **The residential customers of the IOUs are entitled under the Power Act to the same service from the federal system as the public utilities. The DSIs do not share this entitlement. This must be acknowledged by BPA.**

CONCLUSION

We recognize that many of the historical circumstances under which the Act was drafted have changed, and we certainly do not expect BPA to follow blindly along a previously selected route which has evolved in other ways in the past decade and a half. We do, however, expect BPA to adhere to the primary directives and intent of the Act. We welcome any assistance the Subcommittee can provide in this regard.

First, with respect to the residential exchange sales, we expect BPA to recognize the IOU residential customers as a legitimate load which BPA is obligated to serve. Residential and small farm customers of IOUs are entitled to pay the same rates and are entitled to the same service and recognition that other Priority Firm customers receive. BPA's sale of power to IOUs is at cost-based rates. It is not a "subsidy."

Second, with respect to the power BPA purchases from the investor-owned utilities under the exchange, we expect BPA to recognize this power purchase for what it is: the lowest cost, most reliable, best shaped power -- both seasonally and by time of day -- of any major resource acquisition BPA has made since passage of the Act. This IOU power costs BPA less than half of the cost of power from WPPSS 2 and significantly less than the power from the proposed Tenaska project. Furthermore, IOU power comes complete with capacity reserves and other valuable attributes. It is a purchased power opportunity at a price favorable to BPA. Moreover, if at some point BPA can find a cheaper source of power, section 5(c)(5) of the Power Act provides for that flexibility.

Third, we insist that BPA recognize its residential exchange sales to the IOUs as a legitimate component of BPA's priority firm obligation, to be treated exactly the same as the general requirements of public bodies and cooperatives for tiered rates allocation and other purposes.

Fourth, with respect to the level of exchange benefits, we expect BPA to cease treating the difference between its power sales revenue and its purchased power expense as a "net cost" subject to management control in the same manner as copy paper, overhead, or aluminum wire. It makes more sense for BPA to measure its savings from having the low-cost exchange power available to it, rather than having to contract with new resource developers for power from new power plants, which would be considerably more expensive than the average system cost rate.

Fifth, with respect to the difference between the cost of service to the DSIs and the revenue they provide, we believe that if BPA proposes to provide the DSIs with below-cost power, they should be prepared to consider lower service quality, such as through more interruptible power quality or other options, to ensure that all customer classes cover their costs of service. This matching of service quality with costs to serve should be done before new contracts are executed. We have experienced a reluctance on BPA's part in the past to perform necessary quantitative analyses of rate options, such as in the tiered rates discussions. We hope this is not repeated in other contexts, such as the negotiation of new contracts.

Sixth, BPA should fully meet its conservation obligations under the Act. We have required the utilities we regulate to include conservation as a resource in their integrated resource plans and to include conservation in their competitive bidding resource acquisition programs. We have also allowed them to recover conservation costs in rates. If BPA does not do the same, it becomes more difficult for the regulated utilities to compete with the other utilities in the region.

Finally, BPA's proposed change of "corporate" direction to become "market driven" and "customer focused" must not be given priority over and above BPA's statutory obligations. These include using the federal Columbia River Power System to give priority to conservation and renewable resources, to provide equal access to that system for residential customers of IOUs, to protect, mitigate, and enhance anadromous fisheries, and to ensure that its processes are public and that the agency is responsive to the needs of the entire region. BPA is first and foremost a federal agency with broad responsibilities under the law; it is not a commodity marketeer and should not behave like one.

We urge the Committee to take steps to ensure that BPA adheres to its directives under law. These steps can and should include the following:

- Do not accept any proposed legislation making BPA a federal corporation unless and until BPA can demonstrate that it is moving fundamentally in the right direction;
- Do not accept any proposed legislation making BPA a federal corporation unless BPA is subject to adequate regional accountability. This can be accomplished through regulation or by appointing a Board of Directors (possibly the Northwest Power Planning Council) to oversee Bonneville;

○ Ensure through your oversight capabilities that BPA recognize that the residential and small farm customers of investor-owned utilities have the same rights to the federal base system as do the customers of public utilities.

We appreciate the efforts of this Oversight Subcommittee and Congressman DeFazio's Task Force in ensuring the continued accountability of the Bonneville Power Administration, and we look forward to working with you and others as we enter into a new era in the electricity industry.

Thank you.

CONGRESSIONAL RECORD CITATIONS REGARDING EQUAL ACCESS TO THE FBS FOR IOU DOMESTIC AND RURAL CONSUMERS

Jackson, S 14691, 11/19/80

The rate provisions of the bill make it possible to immediately extend the economic benefits of low-cost Federal power to consumers served by investor-owned utilities; this is accomplished by raising rates to the aluminum companies. At the same time, preference customers rates are limited by a "rate ceiling" to no greater than what they would have been without the bill. Preference customers and residential users of electric power are always entitled to the lowest available BPA rate while commercial and industrial consumers generally pay higher rates reflecting new resource costs.

Hatfield, S 14695, 11/19/80

For many years the people of Oregon have been discriminated against in the rate structure because of our system of distribution. This bill sets a uniform rate structure for BPA power sold to any utility for its rural and residential customers. This bill will mean, in effect, a saving of \$1 billion in the next 10 years for the ratepayers of Oregon, with the revenue slack being made up by the direct-service industrial customers who will get renewed long-term contracts in return for the higher rates that they will pay.

McClure, S 11596, 8/3/79

This exchange power will also be sold at the Administrator's lowest rate...

Packwood, S 11601, 8/3/79

Residents served by private electric utility companies will again have access to much cheaper hydroelectric power generated at Federal installations.

Ullman, H 9843 (9/29/80)

And, importantly, S. 885 would provide much-needed rate relief for the residential and small farm customers of private utilities. These ratepayers, now disproportionately burdened by the enormous costs incurred in adding new generating capability over the past decade, would be able to share equally with public utility customers in the benefits of the Northwest's low-cost Federal power system.

Dingell, H 9848, 9/29/80

The rate provisions of this bill are fair and equitable. They protect the rights of preference customers to lower cost Federal-based resources. They provide that the Administrator's direct service industrial customers will pay substantially higher rates. These rates permit the residential customers of investor-owned utilities to share in the economic benefits of the Federal-based resource system.

Moorhead, H 9849, 9/29/80

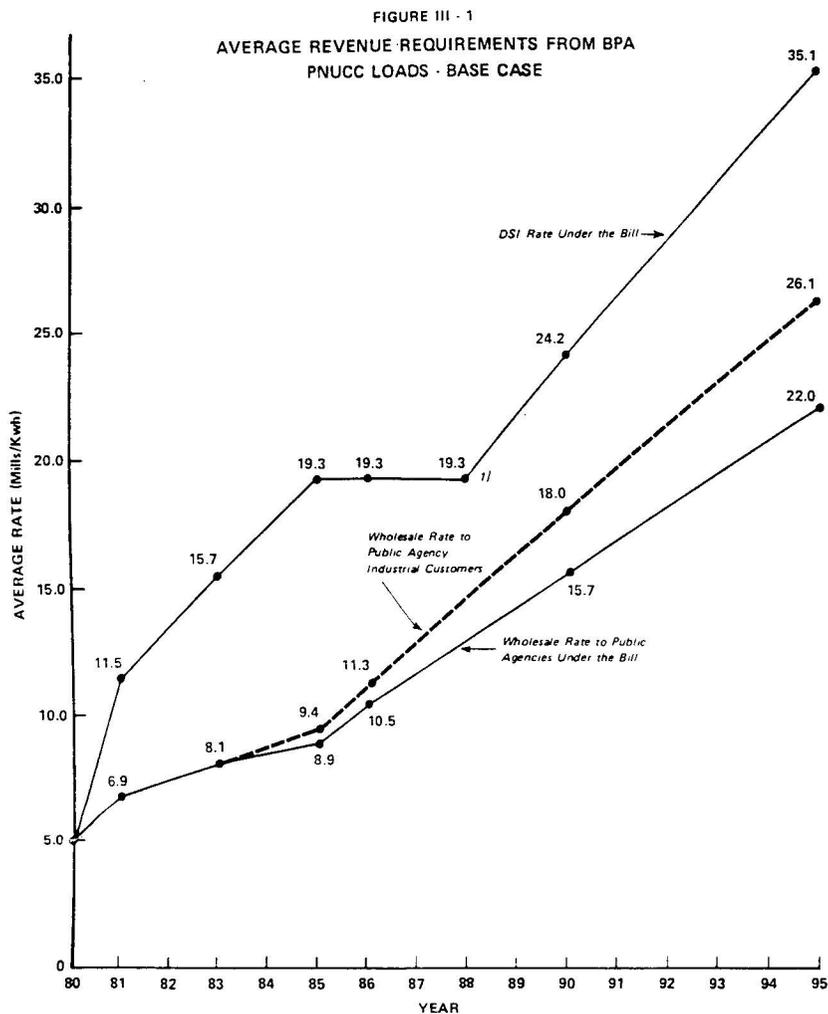
Because the residential rates of public agencies are 50 percent of those of the private utilities in Oregon, there is a movement toward creating a new public agency for the State of Oregon. While this may bring some temporary relief to the residential consumers of Oregon's private utilities, it would create such a huge strain on Bonneville's resources that the entire region's power supply would be thrown out of balance and into court.

Duncan, H 9863, 9/29/80

The bill corrects the rate disparities between public and private utilities.

Kazen, H 10674, 11/17/80

S. 885 will ... provide low-cost power to residential and small farm customers of the region's investor-owned utilities.



1) After 1984-85, the rate will be set at a level no less than that set for the year 1984-85 and that is equitable in relation to the retail rates charged by the public body and cooperative customers to their individual customers.

Source: Bonneville Power Administration

DRAFT

RESIDENTIAL EXCHANGE
COST STABILIZATION STRATEGIES

One goal of BPA's Business Plan is to limit the net cost of the Residential Exchange Program. Because of the interaction between the Residential Exchange and the PF Rate, Business Plan success in holding BPA's costs and rates down results in increased exchange net costs. Original estimates of the gaps between Residential Exchange costs and the Marketing Plan, were as follows:

	FY 1996	FY 1997	FY 1998	FY 1999	FY 2000	FY 2001
Marketing Plan Target	\$220.1	\$282.9	\$314.5	\$344.3	\$346.4	\$346.9
Exch. Program Est.	\$152.0	\$214.4	\$167.8	\$186.4	\$159.1	\$170.0
GAP	\$68.1	\$68.5	\$146.7	\$157.9	\$187.3	\$176.9

Current estimates of the gaps, using latest Business Plan assessment rate estimates and revised ASC estimates, show smaller gaps than originally estimated. The gaps between projected Residential Exchange costs and the Business Plan goal of \$200 million, are as follows:

	FY 1996	FY 1997	FY 1998	FY 1999	FY 2000	FY 2001
Exch. Program Est.	\$180.8	\$240.8	\$256.6	\$283.5	\$261.6	\$285.1
\$200 Million Target	\$200.0	\$200.0	\$200.0	\$200.0	\$200.0	\$200.0
GAP	(\$19.2)	\$40.8	\$56.6	\$83.5	\$61.6	\$85.1

Mr. DEFAZIO. I want to thank all of the witnesses for providing thoughtful testimony within the prescribed time and will now go to a series of questions. Again, we will do it in the same manner as last time, 10-minute blocks for myself and for Congressman Smith.

I will pretty much sort of go across the panel, and then I will have some questions that others may want to respond to.

With Mr. Golden, I guess I would like you to expand a little bit. You have heard the earlier testimony on the rate increase that might follow with the conservation reinvention. You heard some of the other concerns I expressed about what some utilities might do when confronted with that rate increase as opposed to the options that are out there to basically acquire additional power.

Do you think that is a realistic fear, and would you like to talk about that, that cost increase analysis BPA provided to some people? I don't know if you have seen it; I haven't seen it, but I guess perhaps the council saw a draft of it.

Mr. GOLDEN. I have seen some charts that I think contain some of the analyses that you are describing. I do think that it is not at all surprising that the proposed conservation retention would entail retail rate increases. The point of the conservation reinvention.

Mr. DEFAZIO. What about the testimony we heard on this side by Mr. Piper that his customers are paying \$150 million for conservation on an annual basis and not getting anything back? Would this address those inequities that he has professed?

Mr. GOLDEN. I would like to address that by challenging whether there are inequities. Conservation is not a revenue distribution mechanism, it is a resource acquisition. If you want a lot of hydro-power, you build a dam at Grand Coulee. If you want a lot of saved energy, you have to go where the buildings are. Relative to other energy resource acquisitions, conservation expenditures are spread relatively evenly throughout the region, but you wouldn't expect them to be spread perfectly evenly unless the resources were distributed.

Mr. DEFAZIO. How are they spread evenly, on a per capita basis? I mean is conservation, are conservation benefits unavailable to smaller utilities? I mean they can't participate in the program, only the bigs can participate?

Mr. GOLDEN. No. And that distinguishes them sharply from generating resources. I did not hear Mr. Piper or PNGC making any objection to the fact that Bonneville develops generating resources, and therefore, all the benefits of Tenasca are going to Tacoma. Of course that is not an issue. Tenasca is a resource, the benefits go to the region. The region bought it because presumably they thought it was the best resource deal available.

The same is true of conservation. It is different from generating resources in the sense that at least some of it is available to all service territories. With a generating resource, it all goes to one place. And the notion that it should somehow be distributed evenly at all or on a per capita basis simply is a failure to recognize that it is a resource and if you want the resource, you have to go to where it is.

Mr. DEFAZIO. So this goes to the earlier point that Mr. Duncan made about the 58 megawatts at 23 mills, and there was nothing

cheaper available, and it was a whole region cost and the whole region benefited; is that the point you are making?

Mr. GOLDEN. Right. Indeed there are beneficiaries in the buildings where the efficiency measures were installed, and that is a good thing. That is one of the reasons that we prefer energy efficiency. But that is not why Bonneville did it. They did it because it needed energy resources and that was the best deal.

Mr. DEFAZIO. The council made some recommendations on ways to reinvent or modify conservation to deal with the massive overheads and some of the other problems, but without going quite as far as has been proposed in the business plan.

Have you reviewed those? Do you support any of those as options for a way to reduce some of the costs and burdens to the region and the inefficiencies of the system decentralizing it, getting away from the Soviet-type bureaucracy we have at BPA?

Mr. GOLDEN. I do think that Bonneville has experimented successfully in the last couple of years with decentralizing program implementation and we support that very strongly.

Would I make a sharp distinction between providing maximum local flexibility for program design, program implementation, and running the programs in the way that best fits the needs and goals of the local communities, and what Bonneville has at least initially proposed to do, which is shifting the lion's share of the responsibility for collecting revenues to pay for the programs to the local level.

Mr. DEFAZIO. What if there were some more burden placed upon local utilities? I mean right now it is mostly BPA-funded. What if there was a cost-sharing?

Mr. GOLDEN. Right. There is some cost-sharing.

Mr. DEFAZIO. But what if it were enhanced? The Federal Government used to give 85 percent for sewers. Now we are down to 50, and we don't give it to very many people. I mean something along those lines.

Mr. GOLDEN. The proposal that we provided you in your written testimony suggestion that the cost-sharing formula should be more closely aligned with the differing growth patterns of different utilities and the different proportion of their load that they do put on Bonneville, and that that could make the system more equitable, that will still not result in every utility getting back exactly the number of dollars that they put into conservation from Bonneville in the form of conservation programs, because Bonneville couldn't acquire the resource that way.

Mr. DEFAZIO. Okay. Mr. Canon, you raised a number of points. I thought that there were a couple of key points where you said you need information, you need time to evaluate that information, and time to respond. And I got sort of the drift of your remarks that perhaps you felt that thus far, you know, we hadn't had that, or under the previous time line.

Do you think the new time line will meet those concerns?

Mr. CANON. I think it is going to be tight, but I think it is doable if all of the parties to this process act responsibly, and that, as I mentioned before, means that we as parties and the other folks sitting up here who are customers have to raise as many issues, and there are many issues.

I think there are many issues that we don't even know yet as we get into the new answers of tiered rates. We have to raise those issues, ask Bonneville what is your thinking on this, and then Bonneville needs to be able to get back to us and say, well, this is the evaluation that we have done, or this is our thinking, so we can go through this process. It is going to be a challenge on the time. And I wouldn't want to dissuade you from that, but I think that it is important to have a schedule and it is important to try and stay on that schedule.

Mr. DEFAZIO. One of the concerns I have expressed personally and I know customer groups and others have had this same concern is the lack of that kind of analysis, and I share your opinion there.

But one analysis I have seen was created under contract for your group by Mr. Wolverton, and my understanding is that his analysis—I have read it, I can't say I fully understand it; but he says that—predicts there could be a \$200 million to \$300 million cost-shift, and I think it was on an annual basis, not biannual, from the DSIs to growing public utilities. I mean do you stand behind that analysis?

I mean if the growth—I mean the growth is occurring in these public utilities. He said by definition growing public utilities. My concern is what were the implications for growth if we are seeing a large cost shift from a constant consumer of electricity to areas that are undergoing growth in the region?

Mr. CANON. Let me summarize our concern on this issue. Linc's paper was done at a single point in time; we didn't know what Bonneville's tiered-rate proposal was looking like at that point in time.

Our concern is that essentially the Regional Act was a regional deal. Everyone had to give up something to get something, hopefully. One of the obligations that the DSIs took on is the fact that they weren't going to be able to grow, but because they wanted long-term contracts, they would still continue to participate in regional load-growth cost through essentially the rate directives.

Things have changed in this region, but the Regional Act still hasn't changed. And we want to ensure that not only the DSIs, but others who have essentially been party to the Regional Act fulfill those commitments until and unless the Regional Act is changed.

We are concerned that depending on the way that the tiered rate is structured, the DSIs, because they are limited in growth, perhaps would not be exposed and fulfill their commitment to participate in regional load growth. The numbers may change over time, depending on how the tiered rate is structured.

But the philosophy is that the DSIs are paid for 20 to 30 percent of regional load growth up to this point in time, and they may very appropriately feel like that is unfair. I would if I were a DSI. But that is the deal that was struck in the Regional Act, and that is what we are going to be vigilant on.

Mr. DEFAZIO. Are the customers you represent growing?

Mr. CANON. I am trying to think of any that are. The customers that I represent are not that different from the aluminum smelters, the chemical companies.

Mr. DEFAZIO. How many people are employed in the industries you represent?

Mr. CANON. Probably a couple hundred thousand.

Mr. DEFAZIO. Is that direct employment?

Mr. CANON. Direct employment. You have Boeing as a member.

Mr. DEFAZIO. You have a couple hundred thousand, and the DSIs have got 40,000 direct and indirect, so what is your direct and indirect? What do you think? I mean they are using a multiplier of 3.5 or 4, so you want to use the same ones?

Mr. CANON. Sure.

Mr. DEFAZIO. So you represent 800,000 to 1 million customers. Now, what rates are your people receiving? Are they getting a preferred rate?

Mr. CANON. They range in rates probably from Tacoma right now, which is 26 mills up to Seattle, which is 32, 33 mills. Most of them are in the 30-mill range, and of course we don't have a variable rate.

I think I want to be very clear that on many issues the DSIs and my members obviously are like kind. We are both industries. And we essentially do the paper as a shot across the bow, you know, establishing kind of the precept upon which we are going to operate. You know, I literally have lost a member because a facility closed down. The Atochem facility in Tacoma.

Mr. DEFAZIO. And what did they produce?

Mr. CANON. Chloroalkalide, and others, Bolton Paper Industries have taken significant downtime. Obviously one in your district, International Paper, has had a number of week-long and month-long type of shutdowns.

Mr. DEFAZIO. Having to do mostly with the prices they can obtain for their product, given the increase in inputs and their fixed costs of operating.

Mr. CANON. Right.

Mr. DEFAZIO. They could benefit with a variable rate; it would attract pulp, right?

Mr. CANON. Oh, they would love that.

Mr. DEFAZIO. My time is up. Here is what I am going to do: I am going to run over, since we are in the first part of the vote and vote, and leave Bob for his 10 minutes, and I should get back just about the time he has to leave to vote.

Do you think that will work out okay?

Mr. SMITH. Sure. You want me to miss the vote, don't you?

Mr. DEFAZIO. So I will be back as quickly as I can. Bob will question for a while. There may be a brief hiatus, but don't go anywhere.

Mr. SMITH. This is the new Chinese drill. It is called the Turtle Visit; we must go over and register our presence, very important.

First of all, Mr. Golden, I would like to ask you if you support a special rate for irrigation.

Mr. GOLDEN. We testified in the 1993 rate case that the irrigation rate as it is presently structured should be eliminated.

Mr. SMITH. I assumed that you might have; I didn't know that you testified to that extent.

So while you are suggesting that Mr. Piper's concern that he spends \$150 million, his group, and receives \$10 million back is even, you want to take away his irrigation rate as well. Do you think that is even?

Mr. GOLDEN. I think that all customers should pay the cost of serving their loads. I think that is one of the principal threats of Bonneville's competitiveness, is that many customers, the revenue that it collects from some customers is significantly less than the costs that it incurs to serve their loads.

Now, is providing some sort of preferred rate to irrigated agriculture a desirable social agenda? It may well be.

Mr. SMITH. But you are opposed to it.

Mr. GOLDEN. But I don't think that Bonneville should pursue that agenda through its rate structure.

Mr. SMITH. Do you believe Bonneville should have, as well as a competitive private agenda, a social agenda?

Mr. GOLDEN. I think Bonneville inescapably does, yes, and it should.

Mr. SMITH. And it should. Would that include making sure that agriculture as we know it would continue to exist with reasonable rates?

Mr. GOLDEN. Yes, and I think reasonable rates are rates that recover the cost of serving those loads.

Mr. SMITH. Mr. Piper—

Mr. GOLDEN. Incidentally, I would say that we have talked to some of the irrigation utilities about how they might continue to gain preferential access to some Federal power by making efficiency investments and other investments that help solve some of Bonneville's other problems, such as providing for fish.

Mr. SMITH. You contend that irrigation and DSIs are subsidized?

Mr. GOLDEN. To the extent that Bonneville fails to collect revenue sufficient to cover the cost of serving them, yes.

Mr. SMITH. So they are receiving power by your determination, energy, below their cost of providing it.

Mr. GOLDEN. Correct.

Mr. SMITH. Mr. Piper, do you agree with that contention?

Mr. PIPER. In terms of a subsidy?

Mr. SMITH. Yeah.

Mr. PIPER. It depends on how you define costs, obviously. And you can come up with various definitions. I think I would have to agree that there is a difference in the rate paid by irrigation companies—

Mr. SMITH. Understood.

Mr. PIPER [continuing]. From everybody else. But it gets back to the same issue that I was talking about earlier, and that is like the DSIs in jobs, rural economies and jobs are extremely important, and to the extent irrigators don't have cost-effective rates because their commodity prices aren't going to change, the market dictates that, just the way aluminum does. They can't stay in business, the retail business can't stay in operation, people leave, and so forth.

Mr. SMITH. How many irrigators—how many farmers does your organizations serve, any idea?

Mr. PIPER. I don't. We could sure try to make an estimate of that, though, and get it into the record.

Mr. SMITH. I think if we are going to analyze cost benefit issues, we need to know those kinds of things, because when the business plan finally takes form, I have a suspicion that there ought to be a balance in BPA's determination as to not only being competitive,

but also, as everybody has testified, part of their program as a social program which they have got to balance.

Mr. Wilcox, I want to ask you about the subsidy question. You have heard the contention that DSIs are subsidized and in fact irrigation at special rates are subsidized, meaning that BPA is selling energy to you below its cost. Do you believe that?

Mr. WILCOX. No, I don't.

Mr. SMITH. Well then tell me why you don't believe that.

Mr. WILCOX. I think the principal argument that people are making about the DSIs being subsidized has to do with the variable rate. In the task force report, it said that NCAC estimated that at current low aluminum prices, that that would result in up to a \$300 million a year subsidy, and I think that is where the source of that number is, the NCAC estimate and report.

Mr. SMITH. So if I had sold it for 26 mills rather than 21, I would have received \$176 million more money. That is where you think the subsidy comes in?

Mr. WILCOX. Well, but that wasn't—what happened in the variable rate is, when it was adopted in 1986, Bonneville had a 1,500 megawatt surplus of power. Bonneville and all its utility customers said, hey, we can't sell this. This is going to be water over the dam.

And so they adopted a rate structure that was designed to sell power to the aluminum industry that was then facing very low prices, and shut down plants for more than they could have gotten it sold in the open market to California.

And so they adopted a rate structure that varied up and down with the price of aluminum, but was very intentionally designed that it would recover far more revenues by doing that than letting the water spill and dump rates to California. And it has served that purpose dramatically.

It is, by Bonneville's estimates, it is ahead, and even the NCAC—what the NCAC analysis does is I think is faulty in two respects. They said, assuming aluminum prices stay at low levels, and they haven't, aluminum prices are up and the DSIs, I am very hopeful, will be at the base rate for the rest of the variable rate. So that assumption hasn't proved out factually.

But the second thing which is more fundamental is that their analysis is based upon the assumption that the amount of power you purchased is the same with or without the variable rate, and that is obviously not correct. If you just say you are purchasing the same 3,000 megawatts with one rate as you do with another rate, they just add up the difference and come to that number.

But the whole point of the variable rate was to ensure that you purchased more power and Bonneville got more total revenues. And by everybody's estimate that does that analysis, Bonneville is way ahead. Nobody complained about DSIs' subsidies when the variable rate peaked in 1990, and they collected \$280 million more than we would have paid under the standard rate.

Mr. SMITH. Well, I—with respect to that point, I am reading now from the staff report here that makes that same allegation, that if world aluminum prices do not increase significantly, the DSI rate could cost regional ratepayers more than \$300 million by 1996. You testified that in fact, the DSIs have had a surplus of some \$52 million; is that right?

Mr. WILCOX. That is correct. That is our estimate through the entire 10-year period of the rate.

Mr. SMITH. I might note, however, that BPA doesn't agree with that. There is a footnote here that says Bonneville Power Administration says this contention is wrong; they don't agree with it.

Mr. WILCOX. Bonneville—

Mr. SMITH. I am not sure where this came from, you know. It is in this report. Nobody agrees with it. I can't figure out who wrote it. Mr. Golden, you testified—I know you testified that it is going to cost \$300 million. Is this your—

Mr. GOLDEN. I don't have the analysis in front of me. As Brett said, we testified that if aluminum prices were to remain low; we didn't assume that they would, we said if we do, so that is explicit in the analysis.

Mr. SMITH. So this is a wish list. They might lose \$300 million; you don't know.

Mr. GOLDEN. I would certainly never wish that upon the DSI. What it says is that—

Mr. SMITH. Well, I think it might promote your argument.

Mr. GOLDEN. No. It is not what we wish, it is not what we predict. It simply says, if and when prices stay low, this will be the effect on other consumers.

Mr. SMITH. The question of, as I understood you, you said that you shouldn't sell energy to anybody below cost. And I am sure I should ask this question of somebody at BPA, but in your opinion, Mr. Piper, are they selling energy below cost, be it a variable rate or be it an irrigation rate, but below their cost? Again, I ask you that again. I asked you that one time.

Mr. PIPER. On average, Bonneville recovers sufficient revenues to equal all the cost.

Mr. SMITH. That is what Randy Hardy said here in fact. He said the variable rate we think has—we have broken even is, in fact, what he said. So what is this idea that they are selling, Mr. Golden, again, where is this idea they are selling energy at a variable rate below their cost to either irrigators or to DSIs?

Mr. GOLDEN. Quite apart from the variable rate, the idea comes from Bonneville's wholesale power rate development study which the infamous 7C2 Delta, which is sort of a nicer way of saying subsidies, but it comes to the same, which Bonneville calculates at \$350 million for the two-year rate period.

Mr. SMITH. Anybody wish to comment on that point?

Mr. WILCOX. I can comment on it. It is just not true. I haven't seen the document that they are referring to. If I have the document, I could respond in detail.

Mr. SMITH. All right.

Mr. WILCOX. I could tell you exactly, and it might—since Congressman DeFazio has similar questions, probably go through it when he gets here, but the DSI rate is by statute, Section 7(c)(2) of the Regional Act is required to meet Bonneville's applicable wholesale rates to its public utility customers, plus the typical margin that they charge their own industrial customers, minus adjustments for the character of the DSI service, and the value reserves.

And so the base power cost is the exact same PF rate that public utilities customers have to pay, and in the new business plan, it

will be exactly the same tier 1, tier 2 PF rate. So the base rate is the same.

Bonneville takes that base rate and adds the typical margin, which they computed to be 3 mills, and then they subtract the credit they get for value reserves and the character of the service, and that subtraction is 2.5 mills. So bottom line, the DSI rate is half a mill higher than the rate that is charged to public utilities. Now, I don't see how anybody can call that a subsidy.

Mr. SMITH. Okay. I want to get back into this, but excuse me, I have to go run and vote.

[Vote recess].

Mr. DEFAZIO. We will come back into session here. I would like to move these things along as quickly as we can so we don't hold people all day. I understand there was a discussion of the 7C2 Delta going on when I left, and I would like to continue that discussion because I didn't have an opportunity to benefit from it.

I understand the question was raised as to what document we were referring to. We got our numbers from the 1993 final rate proposal, Wholesale Power Rate Development Study, it's got some numbers from it, published July 1993 by the Bonneville Power Administration.

In there on page 98 they compute the 7C2 Delta, as they call it, and what they do there is they compute the total cost of service by their numbers to provide power to the DSIs, and then they compute the total revenues, and then in this case they subtract the total revenues from the cost of service, since it is less, and come up with a delta, which I guess means deficit, of \$337.999 million on a biannual basis. So hopefully that answers the questions.

Now, it may be that without the benefit of Mr. Robertson's testimony that other persons are unfamiliar enough with this process to comment on it, but that is the existing system, let alone the questions raised by Mr. Wolverton in the proposed changes and other questions raised by other people on the panel regarding—including the DSIs as the same as preference customers in tier 1, when in fact the preference customers would not just get a tier 1 power rate, obviously they have to purchase unbundled services, so the preference power rate would be lower for the DSIs than it would be for publicly-mandated, legally-mandated preference customers because they have to buy the service plus whereas obviously the industry doesn't need any of those services. So I assume that is the discussion. Now, I would invite any of the panelists to respond to that. That is a question—yes.

Mr. LAMSON. I would just like to concur with that reference to the 1993 BPA study, and also state that the rate equivalent for the DSI should be the retail industrial rates of the public utilities and not the wholesalers, more or less the equivalent of the retail rates.

Mr. DEFAZIO. And I think you gave me number—or well, no, I got the numbers from Mr. Canon or his customers. He said 26 mills to 32 mills. I think that was retail. What numbers do you have for industrial customers?

Mr. LAMSON. I don't have any precise numbers today.

Mr. DEFAZIO. Do you think his numbers are ballpark?

Mr. LAMSON. They are ballpark, sure.

Mr. DEFAZIO. All right. Mr. Wilcox?

Mr. WILCOX. Since you invited a response, if you look at Section 7(c) of the Regional Act which establishes the DSI rate, the first Section 7(c)(1)(b) sets out a general principle that says, after 1985, DSI rates are supposed to be set at a level that is equitable in relationship to the retail rates that preference utilities charge their industrial customers.

And then you go down to 7C2, which says that for purposes of interpreting Section 7(c)(1)(b), that is determined by taking the applicable wholesale rate that Bonneville charges preference utilities, adding to that applicable wholesale rate the typical margin that those utilities charge their industrial customers, and subtracting from that the value reserves and differences for the character of the DSI load.

And, you know, this is a—this rate has been involved in very extensive public processes, many rate cases over—since 1985, intense scrutiny by the public utilities and constituent interest groups, and basically what Bonneville has determined in these rate cases that were reviewed by FERC is that doing a detailed survey of all the preference agency and large and industrial customers, the typical margin above their wholesale power costs was 3 mills.

And then they did the value reserve study, which is an issue you have raised, and have determined that some of the value reserves was 2.5 mills, so they deducted that, which left the DSI rate at .5 mill above the—a net of half a mill above the rates charged the public utilities. And so that—

Mr. DEFAZIO. That doesn't pertain today, though. And what are you paying today?

Mr. WILCOX. It does and it doesn't. It does—

Mr. DEFAZIO. You are paying 21 mills and they are paying 27, so you are paying more than they are.

Mr. WILCOX. No.

Mr. DEFAZIO. Explain this to me.

Mr. WILCOX. Let me finish. That rate determines what Bonneville calls the plateau of the variable rate, which is the normal charge that is expected to be covered under the normal aluminum prices, and I think that extends from 64 cents a pound and above is the plateau, and then that rate goes down at low aluminum prices to a floor rate of 22 mills.

Mr. DEFAZIO. Okay. So today you are not paying half a mill more than a preference customer; today you are paying quite a bit less.

Mr. WILCOX. No, but at current aluminum prices, we—

Mr. DEFAZIO. Right. But my understanding is that next month because of the low aluminum prices that you will go above that 65 cents and you will go to 23 mills, which still is not what preference customers are paying for power.

I mean I guess the problem I have is in characterizing—see, I said I like people to be advocates, but I also want to say things pretty straight here. I don't know how one can say when one pays less than somebody else that they are paying more. They aren't.

I mean you can say well, there are these other things that are figured in. But the point is, cash out-of-pocket, you are paying 6 mills less per kilowatt hour, and after the adjustment, you will pay 4 mills less per kilowatt hour.

So we ought to at least temper the statements with saying, after we take into effect the other benefits to the system, we are paying, you know, we are paying only this much less than a preferred customer.

And then the question becomes, in the new structure, should you pay again less than preference customers, because they are going to have to buy unbundled services.

So first of all, we have the old value of reserves argument, which I think we have resolved, because we agree, let everybody bid on it. So we can put that aside. The value of reserves as we knew it is history; whether it was a good idea or bad idea, it is history. Now, everybody seems amenable to that. That is something we can agree on. But then the question becomes, you know, how should your basic rate be set in the future?

Yes, Mr. Peterson.

Mr. PETERSON. Mr. Chairman, if I might interject here, what is easy to fall into is to take a look at one minute and say, and project that on to a longer term time frame, and what I heard both you and Mr. Duncan say earlier is that what we want to do is take a long-term view of things, that is, we want to be a long-term competitor in that context.

Now, I would like to ask you to take that same look at the variable rate. The variable rate was never contemplated that at any one particular moment in time, that if we compare that against something else, that it will be exactly equal.

The variable rate was consciously put into place so that over its term, and that was contemplated to be 10 years, and in fact that is what it will be, over its term, the receipts from that rate will be what it would otherwise have been if there was only the plateau or the regular rate.

So when we say here is how we set the regular rate, Brett is saying the regular rate is set at such and such, and it is not below the preference rate. Now, when you say, well now, look at this moment in time, where is the variable rate?

Well, for several years, the variable rate was many mills above the plateau rate, and the fallacy that the NCAC analysis gets into is at bottom, I think, a matter of what I will call a static analysis. That is, it says, well, this particular customer group bought, you know, 50 billion kilowatt hours over this period of time with this rate, and if they would have paid a different rate, they would have generated different revenues. The problem is that the variable rate was intended and in fact—

Mr. DEFAZIO. Sure. I understand that.

Mr. PETERSON [continuing]. My company would not even have been in existence.

Mr. DEFAZIO. I understand that, and I have never in the past, you know, been one who said there should not be a variable rate. The problem is, the problem is, the only dynamic analysis that has been done, which is paid for by ratepayers, is proprietary information, so there is this great dynamic analysis out there that tells us of all of the benefits the variable rate provides and how in fact we are not even really reaching the break even point this year or didn't reach it last year, it is off in the future somewhere, which has some assumptions of whether or not you would have gone out

of business or someone else would have or something else, but none of the public policymakers or other customers can see it.

You know, I have a problem in dealing with a for-profit industry where they just say, we have a great analysis that shows that all of your ratepayers have benefited from us being here, but we can't show it to you. I mean I just got to tell you—

Mr. PETERSON. I don't know what you are talking about. I am not aware of a secret study that I would have anything to do with.

Mr. DEFAZIO. Well, BPA can tell you about it and they will. It was a proprietary analysis that was done under contract involving the aluminum industry which is what they used to come up with the so-called cost benefit and show at what point we cross what line.

It is just hard, you know, to hear that kind of testimony. But I think the point—if you would just give me a moment, the point I am getting at here is in the testimony is—again, I want people to be advocates.

But I mean the point is, Mr. Wilcox has said, DSIs should be treated no differently than other customers. Well, that is a point I am raising. But you do want to be treated differently because my pulp and paper plants can't get a variable rate. Boeing can't get a variable rate. The market is down for airplanes. We have heard from Mr. Canon, his industries employ 1 million people direct and indirect, you employ 40,000 direct and indirect, you don't want to be treated any differently, but, you do, and you are.

Mr. PETERSON. No.

Mr. DEFAZIO. These are some of the points. And then beyond that, I mean we still haven't got exactly to the bottom of the 7C2 Delta. In 1979, they had a forecast. They said, residential exchanging will be 34 mills per kilowatt hour, priority firm will be 22. Therefore, there would be a 12-mill benefit to residential customers, instead of course exchange is 32, preferred is 28.

They also forecasted for 1994 that the DSIs would pay 10 mills per kilowatt hour more than the priority firm rate paid by public utilities and residential customers. Now, we are off a little bit here. You are paying, instead of paying 38, which would be 10 mills more, or even 32, which was their old forecast plus 10, you are paying 21 and you are going to 23, and you want a future arrangement that locks something equivalent to that into place.

You know, my question would be, why don't we continue the variable rate with some adjustments, like taking out the value of reserves and putting it up for bid as opposed to putting you in the same status as the priority customers mandated by United States law, preference customers. I don't see anywhere in the law where the aluminum industry is entitled to a share of the Federal base system. It is just not in the law.

Mr. PETERSON. Well, it is in the law at the present time, and I think there is some discussion about it that you have brought up and the Majority report has brought up is the concept of regional preference. And I happen to be an electricity user in the region, so in that regard—

Mr. DEFAZIO. So we are going to run BPA like a business, but we might require that business to sell power at a loss in the region than it could sell elsewhere. I mean the problem is, some people

want BPA to be Adam Smith on some issues, but not theirs, and other people want BPA to be Adam Smith on their issues, but not others.

I am just trying to reach some consistency here. I am not against your industry. I think it has been vital and dynamic for the Northwest. I want to get a fair deal for everybody. But the question is, is BPA's proposed rate structure a fair deal or not. BPA can't even answer the question since the administrator told me to throw out the only analysis that has been done. Despite that, we have people sitting here saying we should go ahead with it.

How can you say that when we don't even know what it means? What does it mean to Boeing, what does it mean to IP at Gardiner? What does it mean to you? Those are all questions we should balance.

I am not here to attack you and say, gee, we should get rid of the aluminum companies and stick it to them. What I am saying is let's talk about a fair analysis and try to bring everybody in the Northwest along. That is all I am talking about.

Mr. PETERSON. That is all that I am talking about.

Mr. DEFAZIO. Okay. Well then, we have agreement, and my time has expired, and I will yield 10 minutes to the gentleman.

Mr. SMITH. Thank you. We spent the 10 minutes before you arrived trying to get at this question of cost, really. And basically Mr. Golden's contention is that you ought not to subsidize either irrigators or DSIs, and we are hung up on the question of what is the cost.

Mr. Wilcox has testified that they are paying cost plus half a mill, would you say?

Mr. WILCOX. Yes, sir.

Mr. SMITH. Cost plus half a mill. And you know, there is one benefit I see obviously, that is 460 jobs in The Dalles in Oregon. It is a hell of a benefit especially if you are living in The Dalles.

And my suspicion that if those 460 jobs were in Eugene, it might be a different tilt on this whole discussion. I would suppose that that would be the case. However, we are back to the question of fairness.

And again, Mr. Golden, I am having trouble determining what you believe the costs are. You have heard Mr. Wilcox testify that he is paying one-half mill over Bonneville cost. Do you agree with that?

Mr. GOLDEN. I believe he testified he is paying one-half mill over what the public customers who have full legal entitlement to the Federal base system are paying. I don't think he made any assertion between the relationship of that and cost.

Mr. SMITH. Let me ask Mr. Wilcox again.

Mr. WILCOX. When you were out voting, there was a further clarification of what I said. What I said was the DSI rate, the net average rate under Section 7(c) is half a mill higher than the PF wholesale rates.

Now, obviously, that average rate is adjusted in the variable rate, so Congressman DeFazio is absolutely correct, that at low aluminum prices, we are paying less than the average rate. But at average aluminum prices over the 10-year period, we are paying basically the average rate plus the half a mill.

Mr. SMITH. And over the 10-year period of time, Randy Hardy testified that that was a wash.

Mr. WILCOX. Correct.

Mr. SMITH. OK. So if you—in other words, you can't take it at a one-year window; I have to take it over the period, because the variable rate moves with the costs of aluminum?

Mr. WILCOX. That is correct. One thing that I would hopefully like to put the variable rate subsidy issue behind us in the same way that Congressman DeFazio put the value reserves argument behind us.

You have a 10-year variable rate that expires in 1996. Ken and I are not here saying in the new arrangement, renew it or don't renew it. The variable rate was adopted 10 years ago because the region felt it was a win/win situation for everybody; it was a way to keep the aluminum industry operating at the time that we were spilling energy or selling at dump rates to California.

And if we don't have a win/win situation in 1996, there should not be a continuation of the variable rate. If I can't convince you that it is the right public policy issue, there will not be a variable rate. And so we are not here saying continue this subsidy or not subsidy regardless of what you call it indefinitely, we are just saying it was a thing that made sense over its life; it is about to expire and it is a public policy issue on the table, whether it is appropriate to continue it or not.

Mr. SMITH. But it broke even?

Mr. WILCOX. Correct.

Mr. SMITH. Mr. Piper, you know, I have been in agriculture all of my life and I understand the difficulty in trying to work through farm programs and make it work. And given the fact that over the years, there is a return on investment of less than 2 percent in agriculture, generally speaking, tell me how sensitive you believe your irrigators are to any kind of rate increases?

Mr. PIPER. Mr. Smith, I can't tell you in specific terms; I just don't know the answer. But in general terms, they have no ability to control the market.

Mr. SMITH. In other words, they can't pass on any increased costs?

Mr. PIPER. They cannot pass it on.

Mr. SMITH. So they are doubly sensitive, at least if you were in some other business, you might have a shot at passing along costs, although unless Mr. Wilcox fixes a price on aluminum, I don't see what chance he has either. But they are sensitive—

Mr. PIPER. Very much so.

Mr. SMITH [continuing]. To any increases. And that was one of the—and I assume that was one of the reasons that BPA took a real close look at the question of a special rate for agriculture, recognizing that indeed, that is a social issue, isn't it?

It would be anti-social if you raised the rate to the point that you lose a third of agriculture in Oregon, or the Pacific Northwest, wouldn't it? It would be anti-social for sure.

Mr. PIPER. No question that it is a social issue.

Mr. SMITH. Yes. It is a social issue. But at the same token, I think it is a social issue that we maintain 470 jobs in The Dalles as well. That is all I have.

Thank you very much, Mr. Chairman.

Mr. DEFazio. I thank the gentleman. We will move on from this, and I will state for my purposes, you know, given the mishmash and the murky presentation by Bonneville so far, particularly having heard that I can throw out the only economic analysis provided me by BPA, I would prefer to have a bifurcated structure with a discernible, variable rate out there so that we can better understand what they are proposing today.

But we will see what they come up with as we go through this extended process, with modifications of bidding out the value reserve and other things. So you know, I would like to say that this is about jobs in the Dalles; it is also about jobs in Gardiner at the pulp and paper mill there, where one of their greatest costs is electricity and they would like to see a floating rate too, or Halsey Paper Mill or Greenbrier Rail Car Manufacturing in Portland or Boeing in Seattle.

All of these industries are subject to the same competitive international pressures as others, and what I want to see is a Northwest that grows vibrantly with jobs available both in rural areas and in urban areas, so we can accommodate that growth.

So that is what I think this hearing is all about, to come up with that fair and equitable treatment and the Northwest Power Act was pretty well structured among some extraordinarily divisive and competing interests to do that. My question is whether or not we are administratively unbalancing that bargain in a way that doesn't make sense for the 1990s and 2000 and after.

Miss Leone, one thing you brought up, which I think is really important here, and we haven't gotten to it, is this rate stability argument. We had some brief discussion earlier. I have a question for you and other people may respond.

You know, there is all this thing about Independent Power Producers and all the tremendous competition they are going to provide. But my question is, if I have a high value on stability or long-term, what backs up some individual IPP that doesn't own or operate on anything other than one plant which has a gas contract with someone, somewhere and has told me, don't worry, I am going to give you this great gas deal for 20 years? What if once they have the return on their equity, they just say, sorry, we just went bankrupt, we are out of business.

I mean I can see a scenario here where some people sign on to what look like sweet deals, and something unexpected happens in the gas market. The Wall Street Journal has just opined we will see a dramatic increase in gas prices because of changes in Canada. The Economist has about a 10-page article this month on the dramatic increase coming in energy costs worldwide. You know, what backs up these IPPs?

I mean if we are looking for stability, do you think people are going to find it there?

Ms. LEONE. Well, I think you are exactly right. This is a risk that customers are going to have to look at when they deal with these IPPs. What are their track—not just IPPs, marketers and others—what are their track records? What kind of guarantees can they get from them?

I suppose, perhaps, even with Bonneville's unbundling, you might be able to fix some short-term outage-type things, but, you know, I don't know if they will have a product that will go for 20 years. If you are in eastern Idaho, you might want to look to Utah Power for the same kind of short-term fix or at least reserve power. This is what makes the choice of freedom difficult.

If utilities are going to look to other suppliers for what we are starting to call Tier 2 price, Bonneville is tried and true to date in its product. Are the other choices going to be as operationally reliable? I don't know. Some seem to have been. Others could well be fly-by-nights.

Mr. DEFAZIO. On Tier 2 Power, I am curious, BPA, in the to-be discarded DEIS analysis, said the Tier 2 power will cost 38 mills. I guess I am wondering, if there is all this power out there at less than the 38 mill rate, who is going to buy power from BPA? I assume it is Mr. Scott and other small utilities, as he said, who don't even have the staff to go out and parse through the market.

It is like I don't go through my mail every month and figure out whether I am going to go to a new long distance provider because I could figure out half the offerings and what it means to me. I just throw it out.

You represent some of those people, the PPC?

Mr. DUNCAN. One hundred fourteen of them.

Mr. DEFAZIO. Do you think they are going to get stuck buying the Tier 2? Who is buying this stuff? Obviously we are planning on selling this stuff. Somebody is going to make a bunch of money from selling it. Who is going to buy it?

Ms. LEONE. If purchase power is included in Tier 2, that is what its cost is going to be and that is what it is going to be sold at from Bonneville. To take your analysis one step further, PPC may be reinventing itself to see what it can do to help customers like Mr. Scott.

Mr. DEFAZIO. I see. That is an interesting idea.

Do you have any estimate, since they can't tell me, how much additional cost the shaping and the other services might add on top of the Tier 1 cost? I mean, have you done any analysis, independent analysis of that, or do you think that is just basically imponderable because it is all up to BPA and how they price those products?

They obviously have some market in mind or competition in mind in pricing those products. I am wondering if anybody has done an analysis.

Mr. DUNCAN. We have not. In fact, I went to great pains to tell the Seattle Post Intelligencer the Link Wolverton study wasn't done by or for the PPC.

Mr. DEFAZIO. No. We know who to blame for that.

Ms. LEONE. We have not. And we are hoping, certainly within the next six months, to get exactly that done through working with BPA.

I would like to emphasize again that these contract discussions, as they are termed, are actually resolutions of core contract issues.

Now, at the same time, I think earlier today, someone mentioned that the TRIM, the Tiered Rates Impact Model, was nearing completion. My understanding is it will be out within the next couple of weeks and up and running and available. And we are hoping

that all kinds of answers to questions we have about the business plan numbers and lack thereof will be available within the next couple months so that we can make decisions.

Mr. DEFAZIO. Okay. On page 3 of your testimony, you raise the point that, again, when I refer rather facetiously but I think realistically to the Soviet style of bureaucracy at BPA, you talk about the central implant programs the last 14 years with the attendant shortcoming: 40 percent overhead.

Is that 40 percent out of BPA or is that 40 percent including the local overhead and the BPA overhead? I haven't seen that number before.

Mr. DUNCAN. I believe that is BPA, but I will check and get back to you.

Mr. DEFAZIO. We can ask BPA about that. That is a pretty extraordinary overhead.

Did you have a chance to look at those proposals made by, again, by earlier testimony by Mr. Duncan on possible changes to the conservation program, additional cost sharing, doing away with the central control of the actual measures and those sorts of things, having it results oriented? Did you have a chance to look at some of those as an alternative?

Ms. LEONE. I skimmed them briefly this morning while he was testifying. And my view is this. Both he and Mr. Golden and others were involved in preparing and drafting up conservation reinvention principles, I believe. Now seemingly other alternatives are being proposed. I wish that we could head off in some direction. Right now, the Northwest, my members are prepared to go decentralized and pull the cart all by themselves. If we are now supposed to do something else, we need to know yesterday. We expect to come up with some IRP guidelines by, I think, the 23rd of August.

Now, if this isn't—if we are spinning our wheels, we need to know.

Mr. DEFAZIO. It seems to me you represent, again, a lot of the smaller utilities, such as Mr. Scott represents. And this was a concern that came up when we were doing the IRP's with WAPA—and that a lot of small utilities have very little capability. They don't have a lot of staff sitting around. They can't afford expensive consultants to sort of start up their own programs.

Now, I guess what I am thinking is—I mean, looking at Mr. Duncan's conservation proposals again, if BPA were helping local utilities with start-up costs or they were doing some continued cost sharing but at a lower level, I mean, something, you know, rather than just a cutoff and a total send it out to the local utilities.

I mean, we could certainly lower the cost, do away with the BPA bureaucracy. You know, it would be more like what we do with grants from the Federal Government where you set guidelines. The people have to show their results. But you don't—it is not regulated day to day the way it is now. I mean, you wouldn't have BPA in there looking at what the weather-stripping people were putting on the doors and stuff like they do now. So—

Ms. LEONE. Right. I think Bonneville's proposed energy service charge takes a big step in that direction.

Mr. DEFAZIO. The DSM stuff, you are thinking of?

Ms. LEONE. Right.

Mr. DEFAZIO. Okay. My time has again expired. I will defer to Bob again.

Mr. SMITH. You are welcome to it.

Mr. DEFAZIO. Great. Because I want to go through some other questions. I thank the gentleman. At any point you want to jump back in.

Mr. Scott, I hesitate to bring up the DSI's versus preference again. I think we pretty much covered that ground. You may have been involved when I was out of the room and you weren't involved in a later exchange. You certainly made it a major focus.

Is there anything you think we missed? Unless you think there is something we missed, I would as soon leave it lie.

Mr. SCOTT. I guess the only thing that I might add is it disturbs me that Bonneville's business plan anticipates adding or at least not losing about, I believe it is, 420 megawatts of DSI load due to what they call price signals, and losing it again.

Due again to what they call price signals, about 130, 120 megawatts of preference load. There again, I don't quite understand why they intend to send those price signals, because it seems to me that preference should have more meaning than that.

Mr. DEFAZIO. Well, perhaps when Mr. Robertson comes up, he can discuss those assumptions. I don't know if they based it on Clark and Snohomish, they are looking at alternatives no matter what the price, or what they base that on. If he takes note of that, we can get a response out of them.

Mr. SCOTT. They say that is due to price signals.

Mr. DEFAZIO. Right. I would be interested in how—and do they have—that is the point you raised. Shouldn't they have some additional concern about trying to keep all the preference customers somehow in the net, if possible. Certainly.

Mr. SMITH. Mr. Scott, would you also criticize Bonneville for spending \$1 billion on salmon mitigation? One billion, not a million.

Mr. SCOTT. That is a whole other issue to get into. I have some real reservations about the salmon recovery program. I do not want to be a commissioner when the last salmon goes through the turbines or through the river.

Mr. SMITH. They already have.

Mr. SCOTT. You might be right. However, I think that the region needs to get together and that there are several causes for the salmon problem that we have, hydroelectric power being only one of them, and that we need to address all of the causes.

Mr. SMITH. No. I was just trying to make a point to you while you are criticizing them, if they had had a billion in the bank and hadn't had to spend it for salmon, which obviously didn't make any difference that anybody can measure, then there wouldn't be this agony about rates so much.

Mr. SCOTT. A billion dollars would be fine if it was working. Like a friend of mine said, if we are going to fail, let's fail cheap.

Mr. SMITH. Well, that is not cheap. If they had it back, we probably wouldn't be meeting here today. So when you criticize them, let's criticize—I've heard no one criticize them for spending a billion dollars for fish, not even the wildest environmentalist. They

think it is great. But it produced zero and with no opportunity in the future.

I yield back.

Mr. DEFAZIO. Thank you, gentleman. I will reclaim my time.

You know, I would like you to give us some perspective on unbundled services. You alluded to it. I think it is an important point for a large number of Ms. Leone's members and I think Mr. Piper's members, but maybe not necessarily the preponderance in terms of contributions to the organizations because the bigger ones contribute more.

Can you expand a little bit on what you see the challenges to be with the Tier 2 rate and the unbundled services for small utilities like yours?

Mr. Scott, that is for you. I am just trying to get it in a perspective.

Mr. SCOTT. Well, we don't know yet what they are going to offer in terms of unbundled services exactly. They haven't told us what they are going to be or what the prices are going to be, so it is really hard to analyze. And there again, when the time does come, we are probably going to have to hire some consultant or join some sort of group to help us do that, which is kind of disappointing to us because that in itself gives us some upward rate pressure.

Every time you join another organization or hire a consultant, it costs money. And that, of course, gives rate pressure. I would, I guess, prefer to be able to do what we have done in the past, and that is just buy what Bonneville has called vanilla power. We like vanilla power. It works well for us. We are not unlike our consumers when we look to the switch. When we flip the switch, we need the light bulb to come on. We don't have the flexibility like, say, a Clark or a Snohomish might have or some of those other utilities of shaping our load differently other than some DSM activities that we might undertake. Even that is not really going to contribute much. Nobody has come along and offered any interest in our six-megawatt load. Louie Dreyfuss hasn't called us or any of the others.

Mr. DEFAZIO. They haven't.

Mr. SCOTT. We don't expect to hear from them.

Mr. DEFAZIO. We know you are on the list.

Mr. SCOTT. They certainly aren't going to offer us a full meal deal at 27 mills for 20 years, or leveled.

Mr. DEFAZIO. Okay. Unfortunately, there is going to be some change, things will never be as they were.

I also want to make the point that there are varying needs among the customers, and you are expressing the needs for the preponderance of the customers but not perhaps the preponderance of the load on the system. So I think it is a really valid point that we need to remain sensitive to.

Mr. Piper, there is a point that I will be asking BPA about but you raised it, which puzzles me, which is about this rate increase in October of next year if we go with an interim rate case of 10 to 15 percent. Now, I have seen the numbers. Let's just do it this way. That rate increase of 10 to 15 percent assumes a certain level of revenues.

Now, the question which I have asked BPA is, you are going to need 15 percent more revenues next October, either through an interim rate increase or through unbundled services and tiered rates.

Who is going to pay? Are you confident that your customers or your members are not the ones who are going to pay? Do you know where the disparate rate impacts are going to fall? Do you know who is going to pay the additional bill?

BPA is seeking more revenue. That is from the customers. Some are going to be buying unbundled services, some are going to be buying Tier 2. Some are going to be doing this and that. The money is still coming out of the purse of ratepayers in the region.

There is one part I should add, and it is a proviso. They obviously, as Mr. Robertson said earlier, they did assume in their market-driven alternative things that they admit they could do, even if they didn't unbundle services and go to tiered rates. They assume \$100 million in annual administrative savings. They assumed worst-case scenarios and all that. They prejudiced it as much as they can.

So actually 10 to 15 percent is probably not accurate. Maybe we are looking at 5 to 10, after you assume all the common things you could capture in terms of administrative savings, reduction in staff and other efficiencies.

Still, who is going to pay for that? Somebody is paying for it in the region. I mean, do you know who that is? And are they your members, or whose members are they at the table? Who at this table is going to be ponying up the extra money?

That is my question. And BPA can't answer that. I am hoping maybe you can because you were strongly advocating we move ahead right now. So I assume you have done an analysis and you understand where that is going to go, because there can't be any other reason for saying we should go ahead now.

Mr. PIPER. No. I can't tell you that. I haven't done an analysis because there is nothing at this point to analyze. That is our whole point for proceeding as fast as we can, to get these things defined. If Bonneville comes back with an unworkable program, we will go elsewhere for power. There is not a difference anymore. We can buy reserves. We can buy maintenance downtime. We can buy storage and shaping. IOUs have already been around talking to us.

Mr. DEFAZIO. I guess I am really puzzled at her testimony, then, Ms. Lamson, that we have got a large utility in Washington that will be thrilled to buy power well above the preferred rate. So you are saying—

Mr. PIPER. That is today's PF rate.

Mr. DEFAZIO. That is pretty high above it. It is above the worst case projections I have seen for 2010 for BPA.

Mr. PIPER. All I am saying, the practical economic realities are such that if Bonneville raises costs to a level that is unacceptable to us, we have alternatives.

Mr. DEFAZIO. That is the key, the raising of the costs. You are assuming that if they adopt an interim rate, they can't have any cost savings. They assumed, which is now fallacious and they admit they did that, because when they interpreted the word "status quo," they didn't change anything. So part of it is the cost could still come down.

But the question is, after the costs come down, approximately the same amount absent the small amounts that go to conservation, where does the additional revenue come from? You are telling me you don't know and no one else knows.

Mr. PIPER. I don't know where it is going to come from, because as you point out, this question of the unbundled services and under what class of customers they fall is critical.

Transmission is a beautiful example of it. We are very concerned about that. As I stated earlier, yes, we are concerned. Yes, we care. That is why we want it defined, because we can't make any decisions on our own. Until those things are defined and until that happens, we have no choices.

Mr. DEFAZIO. Okay. So then it isn't quite the go-fast. In an earlier phone conversation with Mr. Wilcox, he told me BPA was going to use transmission to keep people from going to IPPs by pricing the unbundled products that people would have to get to follow an IPP load in such a way that they can keep competition at bay.

Now you seem to be assuming that if those prices are bundled in a way that is not acceptable to your customers, that you are going to be able to go out and buy IPP power at some extraordinarily low rate, despite what you might have to pay for wheeling, shaping, following, whatever else you have to buy.

Mr. PIPER. There are competitive factors at work that will allow us to do that, not necessarily all products, and services transmission is one of them. Transmission access rates are protected by the 1992 Energy Policy Act.

Mr. DEFAZIO. We are not sure what the 1992 Energy Policy Act means particularly in our region and even in California. It means there are changes coming, but we don't know exactly what they mean.

Mr. PIPER. They need to be tested, I agree with that.

Mr. DEFAZIO. Ms. Lamson, coming from the regulator's seat, I am curious why your major utilities haven't accessed this plethora of power at this rate and why they are paying the outrageous 45 mills, when I am told there are bundles of it out there at much less than that. You regulators are really asleep up there.

Ms. LAMSON. I am afraid I can't talk too much about that because there is a prudence review right now on that issue. The staff of the Washington Transportation Commission, the advocacy staff has challenged the prices of those contracts. And we just completed the hearings so that that decision is pending.

Mr. DEFAZIO. Okay.

Mr. SMITH. Mr. Chairman.

Mr. DEFAZIO. Yes, certainly.

Mr. SMITH. Mr. Wilcox, I saw you shaking your head. Are you brokering transmission around the country?

Mr. WILCOX. No. I was trying to figure out what Peter—I am sorry, Congressman.

Mr. DEFAZIO. He was referring to an earlier conversation.

Mr. WILCOX. It wasn't anything I testified to today.

Mr. DEFAZIO. It was a phone conversation, if the gentleman would yield back. BPA is telling me they have to do these things because they are worried about lack of control of transmission. This

was intended because they want to unbundle projects. Then they can charge for the other services which they can't charge for now.

You get the incremental cost of the wheeling. They could be putting prices on it which would require an even lower rate for the IPPs to be competitive or would raise the total cost of the package.

Mr. WILCOX. What I was trying to get back in that conversation was in the point of the testimony I gave today. Really, right now, Bonneville, in their one-size-fits-all rate making, is trying to compete in a market that isn't a level playing field. An IPP is selling vanilla power at as high a plant factor as they can, and that is what the IPP market is, and the Bonneville market is the same vanilla power plus load phone services, plus load shaping services, plus reserve service, plus, plus, plus. And part of the competitiveness project is to change these things so that Bonneville no longer is competing with its hands tied, that there is an apples-to-apples comparison that they are selling—vanilla power is being compared to vanilla power.

And if you buy from Bonneville or buy from IPP and need these other services, you are paying for those separately, and I think that is an appropriate thing to do.

In my opinion—and this is personal rather than kind of a DSI position—I think a big part of what is rightly or wrongly going on in the competitiveness project is because Bonneville's historic rate-making practices have given you built-in incentives to build your own resources. And what they are trying to do is take away those incentives that currently exist so that they can compete in the new generation business.

Mr. DEFAZIO. Okay. Just to sort of explore for anybody who wants to respond a little bit more about the transmission issue, because I think it is key, both to BPA's hysteria and—excuse me, their sense of urgency and to some of the arguments about the economics of the alternate power that is available.

And back to the 1992 act, which Randy says doesn't help him, but I always remind him that I voted against it. I was one of two Members of the conference committee that voted against it, one of 47 Members of the House that voted against it. It was ill-defined legislation.

Mr. SMITH. I was not here.

Mr. DEFAZIO. Congress didn't understand it. It wasn't this committee. It was the Energy and Commerce Committee which dealt with that section of the bill. Unfortunately, we didn't have jurisdiction. It would have been better.

Mr. SMITH. Transmission.

Mr. DEFAZIO. But only of BPA. On BPA, we did get a little bit of special language with the help of Al Swift and this committee.

And the question is, BPA has an undefined degree of discretion in managing its transmission system, for example, BPA says that the transmission costs would have to be just and reasonable, but that that doesn't apply to terms and conditions.

Now, that would be a question applicable to anybody at the table who thinks they have more of a handle on exactly what that means. I will hear more from BPA on that, I am sure. But maybe it is a little esoteric.

This does go to some of these issues about who is going to be competitive or not competitive in terms of coming into the region and transmitting power, under what conditions they can do it. Because BPA has not totally lost control. We have not suddenly created a common carrier, anybody can plug in any time they want. That is not the way BPA seems to have interpreted it.

Mr. PIPER. Mr. Chairman, if I can respond, I don't think we are concerned about access to the Bonneville system for non-Bonneville power so much as we are concerned about the pricing of it.

Having said that, I also will say when it comes to non-BPA Tier 2 power, we are very concerned in the rural areas about the transmit agreements over which that power would flow. The agreement with Idaho Pacific, Puget Sound Power and Light, those agreements exist because Bonneville found it appropriately cheaper to wheel over those lines than to build new facilities. So there aren't facilities connecting the Bonneville network to a number of the cooperative rural areas. Transfer agreements are a major concern that we have.

Mr. DEFAZIO. When are those agreements up?

Mr. PIPER. They vary in time. I think a number of them were negotiated about three years ago and I would guess they are 20-year contracts. We could get a schedule for you if you would be interested.

Mr. DEFAZIO. I think that is a very real concern. BPA is talking about a number of other things that go to your customers, low-density discount and that. I want to see that we are not sticking it to the rural areas here. I would be interested in the schedule of those things. BPA might be able to provide it, or you can, those agreements.

Anyone else want to comment on the new world of transmission? Okay. My eyes glaze over on some of these things, too. And unfortunately, Ms. Lamson was constrained from answering. I did have a question about the price. But as you said, there is a review going on so you can't.

Ms. LAMSON. I could add one point. That is, I believe it was Puget Power who said at that meeting that Mr. Duncan mentioned, Boy, give us a call, we will buy it. And I have heard some other comments from several other people in the region.

Mr. DEFAZIO. And that is at today's or even the projected, I would assume, hearing what I have been hearing, is a voided cost. Even the worst-case scenario for preferred firm rate under the DIS, which is, unfortunately, going to be thrown away and is not an accurate analysis, but when they were talking about 3—

Ms. LAMSON. I believe that is the rate they were talking about, yes.

Mr. DEFAZIO. Okay. I am being reminded I have neglected some important point. Okay, a couple of people have alluded to this. We have a new process in place, but in particular, Ms. Leone referred to this and I think there were some others.

You said we needed to have resolved the major issues or all the major issues in the contracts by the time we go into the rates or something else would need to be done. Are you saying that if we can't get that done—and I think it is a very ambitious schedule. But maybe perhaps it can be done, given the new BPA and their

new willingness to negotiate things more quickly. I would expect it took them three years to negotiate the contract for the three megawatt plant. Now they are going to renegotiate every contract with everybody in three months. This will be a reflection of the new BPA.

What do you have in mind if we can't get that done, I mean, just a worst case?

Ms. LEONE. Well, we are thinking about what contingency arrangements might be done. And this is not planning for failure, but we also don't want to fail to plan.

One thing that was mentioned at the executive committee meeting last week—executive committee of the Public Power Council, Sue Hickey, when we were talking about the sequencing of events, contracts first, in response to a question, I think from the Mason Canby group, What happens if we don't reach agreement, we don't resolve these core questions, core issues.

She said, Well, you guys would not want this, but it may be that we will have a rate case under the current methodologies that seeks 15, 10 percent, whatever rate increase that would be in place until we can get the contract issues resolved. And so I am guessing that that is one alternative.

PPC is not adamantly opposed to that. We haven't—as I say, we haven't come to any position on contingency arrangements yet, but apparently that is one that Bonneville is considering and it is one that we are open to.

Mr. DEFAZIO. And I guess, perhaps, if we reflect on my earlier dialogue with Mr. Piper, I mean, if you move some of the assumptions which are common to all the alternatives into the status quo alternative, I don't think we need to look at the 10 to 15 percent because some of the assumptions they made there are contingent upon whether or not they can reduce staff, which they are trying to do in any case, and they might need the corporate status to do better and so on and so forth.

So I guess, though Mr. Piper would say that that would be from your earlier testimony, that you would be adamantly opposed to that disaster, wouldn't it be better to go ahead with contracts, with issues hanging out there, to go ahead with the rate case on the tiered rates on the first of the year?

I think that is what I caught in your earlier testimony because that would be such disaster to the system. Is that correct?

Ms. LEONE. I think it would be a disaster not to have core contract issues resolved.

Mr. DEFAZIO. Right.

Ms. LEONE. And go into a brand new, brave new world rate case.

Mr. DEFAZIO. Okay.

Ms. LEONE. I think Bonneville, if it needs more revenues, will, of course, have to prove whatever it says it needs. But it would be under the old methodologies. That, I believe, is Bonneville's proposal.

Mr. DEFAZIO. Of course, we can all pray for snow, too.

Ms. LEONE. Right.

Mr. DEFAZIO. A lot of snow in the right places. Okay. I don't think that I have any more questions for this panel. Let's see if Bob does. No.

Is there anybody there who just didn't get to say something that you wanted to say that you came all the way to Washington for? Okay.

Ms. LEONE. I really want to say that that 40 percent apparently comes from the function-by-function review, the conservation overhead. I believe that is a Bonneville number.

Mr. DEFAZIO. It is a BPA, not a total adding in. If you added in the administrative costs of the local utilities, we are looking at less than 50 cents on the dollar getting applied to conservation.

Ms. LEONE. Right, through the overhead.

Mr. PIPER. Mr. Chairman, if I could make one statement.

Mr. DEFAZIO. Sure.

Mr. PIPER. It is not the reason I came to Washington.

Mr. DEFAZIO. You can't talk about health care.

Mr. PIPER. The weather is nice. One earlier statement by Mr. Golden I want to refute, that is, we care more about generating resources than we do about conservation. That is absolutely, unequivocally untrue. Two-tiered rates, we are totally blind as to what type of resources we want to see developed. It is strictly a financial issue. Our members' concern is the only thing we care about.

Mr. DEFAZIO. Okay. Okay, thank you. We will move on to the next panel, which is very small in number.

Okay. The next panel consists of one person, Mr. William G. Council, who is the Managing Director of the Washington Public Power Supply System.

Mr. Council, same rules pertain. We have your testimony. It has been read and we will give you five minutes to summarize the pertinent points. Go right ahead.

**STATEMENT OF WILLIAM G. COUNCIL, MANAGING DIRECTOR,
WASHINGTON PUBLIC POWER SUPPLY SYSTEM**

Mr. COUNCIL. Mr. Chairman, I am Bill Council, Managing Director of the Washington Public Power Supply System. In that capacity, I am responsible for the management of all supply system activities.

You have asked that my remarks address specifically the appropriateness of the recommendations in BPA's draft strategic business plan that pertain to the supply system. Those recommendations center around improving the performance of the planned two nuclear power plants focusing on three specific initiatives: completion of the plant, megawatt improvement program, cost control over the growth and cost of work performed at Plant 2 and identification of opportunities to further improve the plant heat rate in measure of fuel use efficiency.

The supply system agrees that these initiatives are important to the future success of the supply system and BPA and believes that they are achievable. In fact, the supply system has already demonstrated success on these fronts. The reactor power upgrade program should be completed during the next refueling outage.

This will increase the output capacity rating of Plant 2, allowing it to generate about 5 percent more electricity for BPA at low capital cost. And I might point out that calculating it this morning, it is a little under 17 mills power.

The supply system continues to concentrate on optimizing work schedules during refueling outages, minimizing the number of unscheduled outages and minimizing better budget in planning and control. As a result of these efforts, Plant 2 performance is on track to meet fiscal year 2000 generation two targets.

With respect to the third initiative, heat rate improvement, last year Plant 2 was the most efficient boiling water reactor in the United States.

Mr. Chairman, let me say a bit more about the recent accomplishments of the supply system and point out how the system's performance has benefitted BPA and the rate payers of the Pacific Northwest. I should say first that on-line performance and safe operations at Plant 2 are the top priorities at the supply system.

Plant 2 recorded its best generation rates ever during this past fiscal year, greatly exceeding all projected estimates and providing BPA with 7.4 more million megawatts of electricity to sell, which was 10 percent more than BPA expected to receive from the supply system. This extra power allowed BPA to avoid 20 million in power purchase costs from other sources.

In addition, during the last fiscal year, Plant 2 achieved a capacity factor 76.6 percent, its best ever. The goal for this year is 78 percent, ahead of the performance target established in BPA's draft strategic plan. During this same period, Plant 2 remained on-line for the entire winter, BPA's peak load period.

In fact, the plant was on line continuously 257 days, its longest run to date by 54 days. With ongoing drought conditions and a region that is heavily dependent on hydro power, this additional power was timely and appreciated.

Mr. Chairman, the supply system has achieved these performance levels while holding the line on costs and even trimming costs where possible without impacting safe operations. The cost of power for Plant 2 the past few years has been very close to the industry average and our preliminary calculations so that this will again be true in fiscal year 1994. As the majority task force report recognizes, I intend to maintain Plant 2 expenditures at the industry average or below.

As the task force report also notes, the supplies system programs includes optimization of staffing levels. Currently, the Plant 2 staffing level is approximately 1300, about 150 of whom are security personnel. This total, which is derived in accordance with industry standards at that facility, state valid plant-to-plant comparison is not out of line with the industry. These numbers may be trimmed further as appropriate to maximize efficiency and to allow the dedication of resources to areas that most directly improve safety and performance.

Overall for the last two years, supply system budgets have remained level and have been scrutinized and approved by the supply executive board and BPA. The supply system has also reaped considerable financial savings for the region as ratepayers, through a joint bond refunding program with BPA, through a series of 13 bond refunding sales that began in 1989, the supply system has reduced its debt service requirement by a cumulative total of more than \$1.62 billion. These savings are passed directly to BPA and ultimately are reflected in lower rates.

Also, I think you are well aware that on May 13th of this year, the supply system board voted to terminate units 1 and 3, keeping with the BPA recommendation.

In summary, Mr. Chairman, the supply system is committed to performance improvement, as evidenced by our actions during the past two years. Plant 2 performance has improved and costs have stabilized. Optimization of capital expenditures and staffing are critical elements of our success and operations and cost control.

Thank you, Mr. Chairman. I will be pleased to answer any additional questions you may have.

[Prepared statement of Mr. Council follows:]

Statement of

William G. Council

Managing Director,
Washington Public Power Supply System

before the

Committee on Natural Resources,
Subcommittee on Oversight and Investigations

United States House of Representatives

Washington, D.C.
August 9, 1994

Mr. Chairman, members of the Subcommittee. I am William G. Council, Managing Director of the Washington Public Power Supply System. For those who may not be familiar with the Supply System, we are a municipal corporation and joint operating agency of the State of Washington that is empowered to finance, acquire, construct and operate facilities for the generation and transmission of electric power in the Pacific Northwest. All electricity produced by Supply System projects is delivered to electrical distribution facilities owned and operated by the Bonneville Power Administration (BPA), which in turn distributes the electricity to utility systems throughout the region.

In my capacity as Managing Director, I am responsible for the management of all Supply System activities, including the operation of the Plant 2 nuclear power plant and the Packwood Lake Hydroelectric Project. I am also responsible for overseeing the disposition of the Supply System's two recently terminated nuclear power plants, WNP-1 and WNP-3.

Mr. Chairman, at your request, I am appearing today to provide the views of the Supply System regarding its impact on, and role in improving, the operations and finances of BPA. In particular, I wish to discuss some of the Supply System's recent accomplishments and to explain why I believe that the Supply System's achievements and goals will continue to support BPA in its

performance improvement efforts. I am pleased to be here, and I hope that my comments will be helpful.

Supply System Support For BPA Business Plan

Mr. Chairman, you have asked that my remarks address specifically the appropriateness of the recommendations in BPA's Draft Strategic Business Plan that pertain to the Supply System. Those recommendations center around improving the performance of the Plant 2 nuclear power plant, related specifically to plant capacity factor, power production levels, and cost of power.

In particular, the Plan calls for implementation of the following three initiatives in support of the general performance improvement objective: First, completion of the Plant Megawatt Improvement Program, which includes the Reactor Power Uprate Program to increase the output capacity rating of Plant 2 to approximately 1160 megawatts (electric), which will allow Plant 2 to generate about five percent more electricity for BPA; second, tighter control over the growth and cost of work performed at Plant 2, including optimizing work schedules during refueling outages, minimizing the number of unscheduled plant

outages, and implementing better budget planning and control; and third, identification of opportunities to further improve the plant heat rate.

The Supply System agrees that these initiatives are important to the future success of the Supply System and BPA and believes that they are achievable. In fact, the Supply System has already demonstrated success on these fronts. The Megawatt Improvement Program should be completed on schedule (by the end of the 1996 Spring outage), and Plant 2 performance is on track to meet FY 2000 generation targets. With respect to heat rate -- a measure of fuel use efficiency -- last year Plant 2 was the most efficient boiling water reactor in the United States. In spite of its number one ranking, the Supply System continues to strive for further increases in heat rate efficiency.

Mr. Chairman, let me say a bit more about the recent accomplishments of the Supply System and point out how the Supply System's performance has benefitted BPA and the ratepayers of the Pacific Northwest.

Supply System Accomplishments

The Supply System has recorded numerous business and operational successes and improvement trends over the past few years, all of which benefit

BPA directly. Three areas in which the Supply System has made significant progress are nuclear plant performance improvements, operating cost reductions, and debt service reductions. These successes demonstrate that the Supply System shares BPA's commitment to stronger, more efficient operations and will continue to support BPA's performance improvement objectives in the years ahead. Let me briefly expand upon each of these three areas of success.

Performance and Reliability

On-line performance and safe operations at Plant 2 are the top priorities at the Supply System. The Supply System has made great strides in the past few years toward excellence in performance among the nation's nuclear power plant operators. Success in this area benefits BPA directly in the form of reliable, abundant power supplies and, ultimately, lower costs. I will give you a few examples of performance improvements.

Plant 2 recorded its best generation rates ever during this past fiscal year, greatly exceeding all projected estimates and providing BPA with 7.4 million megawatt-hours of electricity to sell -- which was 765,000 megawatt-hours, or ten percent, more than BPA expected to receive from the Supply System. This extra power -- the equivalent of about an extra month of full power operation -- allowed

BPA to avoid approximately \$20 million in power purchase costs from other sources.

During the last fiscal year, Plant 2 achieved a capacity factor of 76.6%, its best ever. The goal for this year is 78%, ahead of the performance target established in BPA's Draft Strategic Business Plan. During the same period, Plant 2 remained on-line for the entire winter, BPA's peak load period. In fact, the plant was on-line continuously for 257 days -- from August 12, 1993, through April 26, 1994 -- its longest run to date by 54 days. With ongoing drought conditions in a region that is heavily dependent on hydro power, this additional power was timely and appreciated.

Cost Control

Mr. Chairman, the Supply System has achieved these performance levels while at the same time holding the line on costs and even trimming costs where possible without impacting safe operations.

Plant 2 costs for the last several years have been very close to the average for nuclear plants of its type operating in the U.S. As the Task Force Report recognizes, I intend to maintain Plant 2 capital expenditures at the industry average or below.

As the Task Force Report also notes, the Supply System's program includes optimization of staffing levels. Currently, the Plant 2 staffing level is approximately 1300, about 150 of whom are security personnel. This total, which is derived in accordance with industry standards that facilitate valid plant-to-plant comparison, is not out of line with the industry. These numbers may be trimmed further, as appropriate, to maximize efficiency and to allow the dedication of resources to areas that most directly improve safety and performance.

During two of the past three years the cost of power, as measured by the industry, for Plant 2 has been close to the industry average, as indicated in the table below:

<u>Cost of Power</u>		
	<u>Mills/Kilowatt-Hour</u>	
<u>Fiscal Year</u>	<u>Plant 2</u>	<u>Industry Average</u>
1991	21.65	21.52
1992	30.76	21.61
1993	22.61	21.52

For FY 94, just ended, our preliminary calculation of the cost of power for Plant 2 is 21.5 mills per kilowatt-hour.

Overall, for the last two years, Supply System budgets have remained level and have been scrutinized and approved by both the Supply System Executive Board and BPA.

Mr. Chairman, the Supply System is also cognizant of the sensitivity of BPA's financial situation to such factors as weather and market conditions. To provide needed flexibility in BPA's budget, the Supply System has on several occasions agreed to postpone to a later rate period certain capital expenditures that were not safety significant. Supply System expenditures are guided by the fundamental objective of sustaining safe, reliable, and cost-efficient operations at Plant 2 and throughout the system.

Mr. Chairman, controlling Supply System costs remains a top priority for Supply System management. We have initiated a three-year "Get Well Program" to improve Plant 2 operating performance. We have made good progress so far, without increasing budgets as have other nuclear plants. In the first year of the program, we focused on plant reliability and providing BPA with needed power. The result was an impressive 20 percent increase in Plant 2's capacity factor for the year. While continuing to look for improvements in Plant 2 performance, we are now concentrating on improving organization and process efficiencies, which should lead to lower operating costs and reduced capital expenditures. Our improvements to date have already been recognized by our regulator, the Nuclear Regulatory Commission, and we intend to continue them until we become one of the nation's top performing plants. These

performance improvements benefit BPA directly in the form of a more abundant, more reliable, lower-cost supply of electricity.

At the same time, I wish to emphasize that while low cost power production is a Supply System goal, broader commitments to reliability and safety dictate that less is not always better. Safety considerations and regulatory constraints will in part dictate appropriate standards in areas such as staffing, operating and maintenance budgets, and capital expenditures. Supply System management will continue to aim for maximum efficiency in these areas, without compromising in the least its commitment to safe and reliable operations.

Debt Service Reductions

The Supply System has also reaped considerable financial savings for the region's ratepayers through a joint bond refunding program with BPA. Through a series of 13 bond refunding sales that began in 1989, the Supply System has reduced its gross debt service requirement by a cumulative total of more than \$1.62 billion. Since inception of the refunding program, the Supply System's overall weighted average true interest cost has been reduced from 10.46 percent to 5.86 percent. These savings are passed directly to BPA and ultimately are reflected in lower rates paid by electric customers in the region. Each year those

savings translate into more money that is available for other critical activities in the region, such as the pursuit of conservation and salmon recovery efforts.

Termination of WNP-1 and WNP-3 Projects

Mr. Chairman, the Supply System has demonstrated support for the policies and objectives of BPA. On May 13, 1994, the Supply System Board voted, consistent with BPA's recommendation, to terminate the WNP-1 and WNP-3 nuclear projects in their current conception. The decision will lead to the termination of certain contract provisions between the Supply System and BPA for the WNP-1 and WNP-3 projects and could save BPA millions of dollars in project preservation costs beginning as early as 1995.

At the same time, the Supply System continues to explore possibilities for future use of these valuable assets which would benefit BPA. As noted in the Majority's Task Force report, one such option would be dedication of one of the plants, WNP-1, for use in reducing U.S. stockpiles of surplus weapons-grade plutonium. This is by no means a far-fetched proposal but rather a concept which employs existing technology and processes, which the National Academy of Sciences itself has recommended as one of the most desirable means of plutonium

disposition, and which continues to receive much attention within the U.S. Department of Energy and other bodies tasked with identifying the best options for disposing of surplus U.S. nuclear weapons materials.

The Supply System has explored the reactor-use concept prudently, without overcommitment of resources, and plans to continue to seek to preserve the option, as appropriate, as long as U.S. scientific and policy debate endorse it as a desired means of disposing of these materials.

Conclusions

Mr. Chairman, the Supply System is committed to performance improvement. Our actions during the past two years are evidence of that. A near-complete change-out of senior management with highly-qualified individuals has brought new approaches and experience from top-performing nuclear plants around the country. The safe, reliable and cost-effective operation of Plant 2 remains our top priority. Excellence in this area alone will do much to support the performance objectives of BPA. At the same time, efforts such as our bond refinancings and WNP project terminations have further boosted the operations and financial position of BPA. Going forward, we are working to diversify our

generation resources -- vigorously pursuing, for example, opportunities to construct and operate natural gas-fired combustion turbines in the Pacific Northwest.

These initiatives are consistent with, and are addressing, the findings and recommendations in the Task Force Report. Plant 2 performance has improved and costs have stabilized. Optimization of capital expenditures and staffing are critical elements of our success in operations and cost control.

I am convinced that through continued dedication to performance improvement and cost control, the Supply System will continue to contribute to the mission of BPA.

Thank you, Mr. Chairman. I will be pleased to answer any questions the Subcommittee may have.

Mr. DEFAZIO. Thank you, Mr. Council.

We have some analysis provided both by the Bonneville Power Administration and from Mark Holt of the Congressional Research Service surveying literature and studies that are out there. Just want to go through some questions regarding that, particularly having to do with staffing levels.

You said that there are approximately 1,300 employees, 150 of those being security. That is actually a little higher than the number I had, but that is fine. We will work with that number.

The INPO study, which is the Institute of Nuclear Power Operations, basically shows on-site nonsecurity staffing at a plant the size of WPPSS II of 783. And that has excluded security personnel again, nonsecurity staffing. Don't you feel that you are quite a bit above that level? You are basically at 150.

Mr. COUNCIL. Our staffing right now, Mr. Chairman, is higher than I would like to see our staffing. However, our costs are in line with the average in the industry. Since our costs are made up of approximately 80 percent staffing, I believe overall, you know, that we are on line.

We have a great deal of work that has to be done in the next two years. So consequently, I have elected not to reduce staff during that two-year period but to accomplish the work that perhaps should have been accomplished before the plant started up.

Mr. DEFAZIO. Well, if I were to apply a similar analogy, I would say BPA's costs, wholesale power costs, are better than in line. They are lower than most costs around the country. So, therefore, they shouldn't be concerned about the 4,000 some odd staff they have. But, in fact, they are concerned about having such a large staff. And they are going to take some extraordinary measures to reduce it.

I mean, I am glad you have admitted that you would like to see it lower, because I was going to go through a series of questions with analysis from the energy utility cost group, T.D. Martin and Associates. I mean, every one of these studies would find that WPPSS is considerably above.

I guess I will take a little different tact, since you basically admitted at the outset that you are higher than you would like to be, and just go to this cost issue. I mean, as you have heard from all the previous testimony, we are expecting a brave new world out there in terms of power generation.

You are a significant cost factor. When you add in the amortization for the debt for all the other WPPSS disasters, you are the most significant cost factor the bundle administrator has to suffer under. But with one operating nuclear power plant, you are still, if we exclude all of the water under the bridge there, you are still a significant cost factor.

I guess I am concerned that you are saying, Well, the staffing is higher but your costs are in line. Well, it would be nice if your costs were way below anyone, your costs were lower. What is your plan to reduce staffing to come in line with other comparable plants in the industry?

Mr. COUNCIL. We are in line with other comparable plants.

Mr. DEFAZIO. No, no. You admitted you weren't. We have the INPO study 783, okay? We have got the EUCG study, which would

be, you know, about 300 lower. We have got the TDM Associates study, which would put you down, again, as being about 500 over the average. So, I mean, you are not in line.

What is your plan to get more efficient and to remove some of these inefficiencies from the operation of that plant and reduce the most significant cost factor you have, which is payroll?

Mr. COUNCIL. Until I finish the Get Well Program for WMPT, I am not going to reduce staff.

Mr. DEFAZIO. The Get Well Program involves you being overstaffed.

Mr. COUNCIL. No, it does not involve being overstaffed.

Mr. DEFAZIO. You said you are in line with everybody—excuse me.

Mr. COUNCIL. It involves finishing the work I have to do.

Mr. DEFAZIO. Mr. Council, please. Let me frame the question better. The three studies I have show that you range from 300 to 500 more for comparable plants. You told me you are equivalent to comparable plants.

Please address those three studies, why you are wrong, why you are not 300 to 500 over comparable plants around the country, and then we will get to the second part of the question.

Mr. COUNCIL. The INPO study for our plant is 1031 people. You said 768 was the average.

Mr. DEFAZIO. Seven hundred eighty-three.

Mr. COUNCIL. Seven hundred eighty-three. So we are approximately 250 above that number, of which 150 is security. We included security in our study.

Mr. DEFAZIO. No, you told me you had 1,300 when you include security.

Mr. COUNCIL. I also said that that was our study.

Mr. DEFAZIO. No, no, wait a minute. Let's—how many people do you have? You are saying their study says 1150 and you told me you have 1300. Do you have 1300 employees?

Mr. COUNCIL. I have 1300 by my count at WMPT.

Mr. DEFAZIO. And 150 are security.

Mr. COUNCIL. Yes.

Mr. DEFAZIO. So you have 1150 people who aren't security at Plant 2, and the industry average, according to INPO, is 783. If I subtract 783 from 1150, I get approximately, it looks to me, like 17—that is 67, plus—477.

Mr. COUNCIL. The same INPO study lists us at 1031 people.

Mr. DEFAZIO. I don't care what they list you at. I am talking about the average. You say you are comparable to other plants. They say the average is 783. You have 477 more people.

Mr. COUNCIL. I am using the same numbers, same cost basis, so forth as INPO. If I use their numbers, which they have provided back to us, it is 1031. I told you, I have really 1300. I have 250 additional personnel working on additional regulatory required programs for the next two years.

Mr. DEFAZIO. Okay. Okay. You have 477 more employees than the industry average, but if you use their numbers, you don't have 477 more. Fine. But the point is, you have 1300 people; 150 are nonsecurity. They say 783 is the average.

Let's try the EUCG, okay? Since you don't like the INPO study. They give you a much higher number of staff. I guess—I don't know where they get these additional staff.

Are they attributing headquarters staff, people who sit around and handle the bond payments? How do they include the higher number?

Mr. COUNCIL. They do include bond, finance people, so forth. If you look at the EUCG study for large BURs, we are comparable with the rest of the industry in numbers of personnel.

Mr. DEFAZIO. How many people does WPPSS employ total?

Mr. COUNCIL. One thousand seven hundred, approximately.

Mr. DEFAZIO. One thousand seven hundred, okay. And you are saying 1300 of those can be attributed to the functioning reactor, and 400 are other. Have you looked at the "other" for reductions?

Mr. COUNCIL. Absolutely. And we will be in fact reducing in the future.

Mr. DEFAZIO. By how many and by when?

Mr. COUNCIL. We are going to go down by attrition. I use—I lose approximately 80 people per year.

Mr. DEFAZIO. Why have you chosen attrition? That is obviously easiest for the people. But is that best for the ratepayers or the upper-most efficient operation?

Mr. COUNCIL. No.

Mr. DEFAZIO. We are running it like a business, remember. Everything is run like a business.

Mr. COUNCIL. I am well aware of that. It does match, as the work gets completed, that does in fact match approximately what we have as a completion plan.

Mr. DEFAZIO. Okay. How about the 1300 people at the operating plant? When are we going to see the reductions there? How many, on what time schedule?

Mr. COUNCIL. Don't know that answer yet.

Mr. DEFAZIO. When will you know it?

Mr. COUNCIL. Approximately two years.

Mr. DEFAZIO. In two years, we will look at the 477 or 300 or whatever people more we have above the industry average. In the meantime, you will just pass those costs on to the region while the region is struggling and cutting everything else.

Mr. COUNCIL. No. I look at those costs each and every year. And as a matter of fact, we are attempting to reduce the costs each year.

Mr. DEFAZIO. What if BPA refused to pay your total bill, what happens?

Mr. COUNCIL. I shut the plant down.

Mr. DEFAZIO. Okay.

Mr. COUNCIL. I think you would be well aware of that. I wouldn't even have to worry about shutting it down. The Nuclear Regulatory Commission would do it for me.

Mr. DEFAZIO. They would do it for you if BPA mandated on you, mandated reductions on unnecessary staff?

Mr. COUNCIL. I didn't say mandate reductions in unnecessary staff. If there was no compromise in safety, yes, they would shut it down.

Mr. DEFAZIO. Well, are you telling me that all the other nuclear plants in the United States are operated unsafely because their staffing levels in comparable plants are significantly below yours? Should I get FERC in here to find out if there are not—

Mr. COUNCIL. Mr. DeFazio, I stated comparable plants to WBU2, a water boiler reactor of the 1200 megawatts vintage have approximately 1200 to 1250 people at their operating units. That is an easy number to check. I would be happy to forward it back to you.

Mr. DEFAZIO. Sure. The problem is we have three studies that find a difference with your numbers. But I would be happy—

Mr. COUNCIL. I will be happy to take those numbers directly from those studies for large boiling water reactors and give you those numbers, unvarnished by me whatsoever.

Mr. DEFAZIO. Okay. Now, what about this termination date? We are talking 1995. When is the termination date?

Mr. COUNCIL. I don't understand the question.

Mr. DEFAZIO. What is the specific date for termination?

Mr. COUNCIL. Oh, termination of units 1 and 3?

Mr. DEFAZIO. Uh-huh.

Mr. COUNCIL. They have been terminated.

Mr. DEFAZIO. Well, my understanding is there is some sort of holding open the final actions involved in termination, turning back the licenses and going to a restoration license or whatever's necessary.

Mr. COUNCIL. No, sir. We are trying to sell the units now. But during the period of this sale of assets and/or utilization of the units as a different project, such as plutonium burning and/or as a gas-fired unit, we have to preserve those assets in case somebody wants to buy the assets, in whole or in part. So in order to maintain the qualifications of those assets as nuclear qualifications, we have to maintain the preservation of such asset.

Mr. DEFAZIO. And how long do you expect that condition to pertain? How long will you look for buyers? I know in the past five, six years ago, you were looking at China and some other places. Now we have some new fantasies, Project Isiah. How long do we pay for this?

Mr. COUNCIL. I am sorry, we have no fantasies about Project Isiah. I do not support Project Isiah.

Mr. DEFAZIO. Well, then, how long before these alternatives are ever fully explored and you reach a final decision?

Mr. COUNCIL. The final decision as far as asset indication for plutonium burn on MP-1 and 2 is January 13, 1995. In the meantime, we are attempting to sell such assets.

Mr. DEFAZIO. Okay. January 13, 1995. Now, let's get into a subject that pertains a little bit to this: termination.

I mean, I have a question. One of the reasons why BPA has never terminated its involvement with the mothballing is because of the very large cost involved with termination. I understand in part that may require site restoration and so forth. My own idea is that we actually put a fence around these things and maybe even a high enough fence so we could charge admission for people to come in and look at these monuments to folly. They are not a danger to anybody. They are not radioactive in there. If you keep kids out so they don't fall in the hole anywhere, why not explore

those sites? Are you exploring any alternatives why—I understand this is pretty much under the purview of the utility commission in Washington State and State law. Are you exploring lower-cost alternatives should the plants be terminated?

Mr. COUNCIL. We are exploring all options with the Washington State Energy Facility Siting Council, yes.

Mr. DEFAZIO. All right.

Mr. COUNCIL. And hopefully, as long as you can prove that the site is safe for people that happen to wander in or want to play games there or whatever else, that it doesn't present a public health hazard, I am quite certain they will cooperate with us.

Mr. DEFAZIO. Okay. It seems like you could basically put a fence around it, maybe hire Pinkerton's or something.

Mr. COUNCIL. No. That is not what they have in mind. They have insisted on demolishing the cooling towers, taking down the cooling building and various others.

Mr. DEFAZIO. Why? What danger does that present to the public?

Mr. COUNCIL. They can rust. In fact, there are many many open hatches in the turbine building.

Mr. DEFAZIO. What if we have a fence and we keep people out?

Mr. COUNCIL. I have a fence now.

Mr. DEFAZIO. Well, double fence with dogs.

Mr. COUNCIL. Dogs, by the way, there are many utilities that have tried that and have been sued. Long Island Lighting is one.

Mr. DEFAZIO. Well, I would suggest that you should continue to pressure them and wouldn't necessarily accept their decisions, because it is pretty easy, I guess, to pass the costs off onto the region of the termination. But as a part of the region that doesn't have jurisdiction, I have a concern, and I think the more reasonable alternatives, particularly for plants that were never operated, there would be lower costs. So perhaps I will take that up with the Washington authorities.

Now, you have had some pretty high capital investments in the past and now you are projecting to have some lower ones in the future. 1993 to 1996, you are going to average \$60 million annually.

Is this because of past neglect, or why are they so high and so high above the average for that three-year period? And then you are going to get below the average in the future, you are saying.

Mr. COUNCIL. They are largely part of the General Electric settlement and the megawatt improvement program of Bonneville itself. And these were costs that were going to be spent, for instance, in the year 1992 but Bonneville asked us to put them off. And they are not all cash. They are a cost basis largely.

For instance, the General Electric settlement is no—does not involve cash. It involves adding to the cost basis of the plant only.

Mr. DEFAZIO. Hm-mmm.

Mr. COUNCIL. Largely where we have been is the plant capital itself has been on the order of \$16 to \$25 million. The remainder of those are megawatt improvement and noncash type capital.

Mr. DEFAZIO. Okay. You were telling us about the operating factors and how great everything was going. I saw some news stories not too long ago about an unanticipated outage that extended for some period of time because of something strange, a light bulb or something.

Mr. COUNCIL. Well, it was partially that. It wasn't a light bulb. It was a light fixture. And during this past August, it was a 10-year in-service inspection and hydrostatic testing of the unit. We hoped we could get it done in 60 days. It actually took closer to 90.

Part of what happened to us during that period of time was that we had a gross deterioration of our electrical penetrations that go through the primary containment. There are some 60 electrical penetrations carrying electrical signals, both in and out of that primary containment. Of those 60 penetration modules, each of which has upwards of 300 wire pairs, of those 60, we reworked 25 and replaced 10. For the next two refueling outages, we will be working some additional. During that period of time, we also discovered we had a crack on an internal component in the reactor vessel itself. That internal crack took six days to resolve.

During the period of resolution of that, in rotating a service platform over the reactor vessel, we tore off one of the lights because we do have to have underwater lights and TV cameras because we are working through 60 feet of water. And that light itself fell down and went through the suction to one of our pumps. And so we had to go in, open up the system and get into the pump to take out that light. That took an additional five days.

Mr. DEFAZIO. So the—this was 90 days. You say you are going to have to rework some of these through the wall components next time. Does that mean that the next outage is going to be also extended?

Mr. COUNCIL. We expect that next outage should be on the order of 45 days, and depending on the amount of capital that we have to put in, such as electrical penetrations, it may have to be extended to 60 days. I am hopeful we can hold it to much less than that.

Mr. DEFAZIO. Okay. What is the industry average on this age plant?

Mr. COUNCIL. On this type plant is approximately 60 to 65 days, is the normal refueling outage.

Mr. DEFAZIO. Okay. So the problems this time in part were the unanticipated replacement of some of those modules and then the problem with the crack and the problem with the light fixture.

Mr. COUNCIL. That is correct.

Mr. DEFAZIO. What was the crack?

Mr. COUNCIL. The crack was on a jet pump sensing line. There are 20 internal jet pumps to the reactor vessel. They basically measure the flow going through the fuel bundles. Four of the six—four of the 20 jet pumps are fully instrumented with two lines each and 16 have a single line. So you are only measuring the reference line. We found the crack on the backside of one of those single-instrument jet pumps.

Mr. DEFAZIO. So you replaced that one. Did you check all the others thoroughly?

Mr. COUNCIL. We checked all the others and did not replace that one.

Mr. DEFAZIO. You did not.

Mr. COUNCIL. No. Our analysis showed it would not crack further, that the jet pump would still indicate, and even if it did crack, it wouldn't present a safety consideration. After five days of

analysis, the NRC basically agreed with us, so we went back to put the reactor vessel back together with a crack.

Mr. DEFAZIO. Okay. All right, I don't have any further questions.

I thank you for traveling all the way back to provide testimony to the committee; I will look forward to your providing the analysis of the staffing levels in writing.

Mr. COUNCIL. Thank you.

[Editor's note.—See Appendix.]

Mr. ROBERTSON. Mr. Chairman, does the committee send out for sandwiches?

Mr. DEFAZIO. Well, I figure we would put you on now, and we could get done in time for a fashionably late lunch, or an early dinner. We have got both you and Mr. Pollock, and Mr. Wright as well. How much time would you require for your basic presentation?

Mr. ROBERTSON. I think I need about 10 to 15 minutes.

Mr. DEFAZIO. Okay. We will set it on 10, and if that isn't enough, we will then go with another 5. How is that?

Mr. ROBERTSON. Thanks.

I appreciate the time.

Mr. DEFAZIO. Okay. Go right ahead.

STATEMENT OF JACK S. ROBERTSON, DEPUTY ADMINISTRATOR, BONNEVILLE POWER ADMINISTRATION, DEPARTMENT OF ENERGY, PORTLAND, OR, ACCOMPANIED BY WALTER E. POLLOCK, ASSISTANT ADMINISTRATOR FOR POWER SALES, BONNEVILLE POWER ADMINISTRATION, DEPARTMENT OF ENERGY, PORTLAND, OR

Mr. ROBERTSON. Thanks again, Mr. Chairman.

My name again, gentleman, is Jack Robertson, Deputy Administrator of Bonneville Power Administration. I would like to respond to some of the questions and comments I have heard today as best we can. But I would like to start by making a couple of, I think, overarching and fundamental points.

The first point I would like to make again is the fact that we encourage and appreciate the review of the committee. You have had a series of task force reviews for us. This is a complicated and challenging period we are entering. We recognize that no one agrees with everything we do at any time, and we understand that you as the Chairman also have serious concerns about what we are doing. We believe strongly, though, in this kind of public review process and it will make us a lot better.

The one thing I wanted to leave with you is I think a fundamental and overarching concern is this: Bonneville is doing its best to try to deliver to the people of the Northwest what I think the people of the Northwest believe and demand the government give them in the 21st Century—to continue to strive to give them much higher value for far less cost.

We think this means a goal of delivering stable rates on our fundamental product for the balance of this century, while continuing to also deliver, one of the most aggressive and innovative conservation and fish and wildlife programs in the world. We recognize to an important degree the economic viability and environmental val-

ues of the Northwest depends on our success, and it is a big job ahead of us.

Let me talk first about a regulatory change. We have heard this today, and I just want to go through a couple of things quickly to make sure you understand the examples we think at least show the fact that, as most people agree, some change is on us. There is a question today about how much change. But to us the fundamentals look pretty clear.

First of all, I would like to make a couple of analogies. We have seen the deregulation that has occurred in the airline industry, in the natural gas industry, and in the telecommunications industry, but we have seen it other places as well.

One of the analogies that I think is most apt ironically for Bonneville in terms of our concern, is none of those, but is IBM. IBM was—is one of the great American corporations; it made its money, it has made its spot in the marketplace based on one fundamental concept, and that fundamental concept was that you could control central computing power. And in the course of its history, it made and grew into the biggest, one of the biggest corporations in the world, based on that fundamental premise.

IBM today is a far different corporation. I would argue that the reason it is now a far different corporation is because it did not anticipate a wave of change which occurred in two fundamental areas. One was the access of individuals to computing power, and the second one is the technological breakthroughs associated with vast amounts of power on work disks. The result of these twin changes of computing power and open architecture, fundamentally destroyed the basic tenants of what IBM had based its business on.

Similarly, if you look at the retail industry and you talk about Sears. Sears was a retail giant for the entire century, and passing back in the 19th Century. It was all things to all people. It marketed from a central concept. It delivered high value to high-end customers and low value and low-cost goods to low-end customers. But then as the retail environment began to get more competitive, the Nordstroms of the world and the high-end customers began to eat Sears' lunch from the top down, and the COSTCO's of the world and the wholesale-based customers began to erode it from the bottom up. The fundamental is now Sears, a formerly major institution, has lost fundamental market shares.

Now, the Northwest can't afford Bonneville to become obsolete and lose market shares similar to what has happened to IBM and Sears. We do not believe we are on the verge of a death spiral, and I want to make that clear. What we are trying to do is anticipate what we think is a combination of unique changes and events which are fundamentally affecting the electric industry. We want to do this to stay ahead of this change. We do not want to be toppled by a shock wave of change later on as happened with IBM and Sears, to some degree.

Now, what are the three elements of these changes? I just want to briefly go through them. We think they are in three areas: The generation competition we have talked about, and you alluded to earlier; the global competition in trade, which we think is increasingly an important aspect for competitiveness of the Northwest

economy; and finally, the transmission changes you alluded to in 1992 National Energy Policy Act.

If I can go quickly, I would like to go to Chart 1. Chart 1 shows the competitiveness of our product versus the competition. It becomes more and more severe as we have gone through the last two decades.

This has been well-publicized in the region. My purpose in raising it is not to pound it in the ground, except to make the obvious point that something fundamental is going on in terms of the margin of the change. We can argue amongst ourselves or even project whether the cost of alternative energy is going to go up faster than not, whether gas prices are going to become more costly, and so on, but the fundamentals of that chart are these: our price advantage a decade ago was 400 percent, compared to the competition. And in that chart today, that same split is 15 percent.

Customers—now, change associated with this, the petition we talked about, is in motion now. It is not some hypothetical change that might take customer share away from us. We think the signs of this are clear, and again, we want to respond to the signs. We don't want to stick our head in the sand because too much is riding on Bonneville staying competitive in the region.

You have talked about Clark County PUD recently signing a letter of agreement to purchase a 245-megawatt cogeneration unit. That would cost us, we think, about \$10 to \$20 million, if they go through with that. You indicated that we hadn't gotten notices yet on that and we wouldn't expect to get notices because of the provisions. But we think they are serious and they think they are serious from everything we have described.

Snohomish County PUD has requested resource proposals and received 88 responses for a total of 8,000 megawatts. This is a huge number. These are the same megawatts and proposals largely that come in our door when we asked for resource proposals. They are waiting outside as competitors to fundamentally go after Bonneville's load if we don't maintain our cost competition.

According to Snohomish, the cost is 27 to 32 mills, starting in 1997. We can have a debate on whether that is the right number or not, but the number is very close to Bonneville's base rate, we think. Twenty six of our customers have signed an agreement with power resource managers for a 600-800 megawatt package of alternative resources. A final decision on whether to proceed with this resource package is expected next year.

Washington Water Power and Sierra Pacific have announced a planned merger which could create another strong competitor for Bonneville inside the region for wholesale supply. In the Northwest alone, 1,400 megawatts of new generation are now in service, or under construction, and another 3,000 or 4,000 megawatts are being studied.

The FERC has approved more than 20 new power-marketing firms to buy and sell power in the wholesale market. Moreover, work is underway to establish a West Coast electric futures market. All of these we think are signs of a fundamental change. How fast is the change coming is a serious question. But we think fundamental change is on the way.

All of this, by the way, I think is excellent news for consumers. The cost of electricity is going to be very competitive. Bonneville is going to be in a much more competitive world; the prices will probably go down. The fundamentals are, if we can't compete, we cannot deliver the mission of Bonneville, which is vital to the region's economy and environment.

The second point is global competition. We talked earlier about the variable rate and I would just like to make this point. Up until the fall of the Berlin Wall, the variable rate for the DSIs was making the region about \$250 million. What we did not anticipate, and what I think few anticipated, was that the Berlin Wall would fall and the integration of the eastern and western economies would have to take place in the last few years.

The result of that, in simple terms was, during the period of worldwide recession, we had to integrate the aluminum production facilities. The vast aluminum production facilities of the former Soviet Union that was devoted to its defense industries in the western world and the commodity prices plunged. The result of that was what you see today, which is a leveling out of the variable rate in materials of its cost and benefits.

So, the global competition plays a huge factor in whether the Northwest can continue to regionally compete.

Finally, the third area is transmission access. We have talked about the changes of NEPA 1992. What factually will come from NEPA 1992, I think has been clearly stated here as uncertain. It is clear that the fundamental premise under NEPA 1992 is allowance for more transmission access increasingly as we move forward.

Now, again, I just want to say we are confident about our ability to stay ahead of these trends, but we have to recognize them and not ignore them.

The third chart, the one up on top which talks about rate increases, projected rate increases, are really the focus of my testimony today because it kind of puts in perspective the discussions we have had. We have talked about how different customer groups would or wouldn't benefit under the draft proposal.

What you see in the comparison chart is the fundamentals of how our product design would look before and after taking any actions. The upper path is the most current data. We would expect to need increases in our rates in 1996, as we indicated, of somewhere between 10 to 15 percent on that upper path. This is indicated in that first increase associated with the path.

With continued inaction, and again, this assumes that we do not act and assumes some actions we would take no matter what; but with continued inaction, we think this would total 40 percent by the year 2002, on the upper path.

Now, the earlier estimates that you talked about with Randy Hardy, you said he said was thrown out. This was really a reference point to this graph so at least you could see where it would be placed, and we have some more information to give about that, but that is basically the reference point that is indicated by the November 1993 data.

The business plan EIS, which you reviewed and based some of your comments on, was developed basically in October a year ago.

It had lesser numbers at the top. It also had less accomplishments at the bottom, and the differential was less than it is described here. But we think that has, as I think you are aware, first-cut data that was not anywhere near as sophisticated as the models we now have as we begin to apply ourselves in more details in the implications of the change.

So, the bottom two lines show, we think, what we can achieve—a goal of trying to flatten the rate through the year 2000. The bottom darkest line is basically the tier-1 rate plus shaping services, and again, we are trying to flatten it in real terms through the century. On top of that is basically what we think is a combination of tier-1 and tier-2 products which would come as close as we can to simulating today's PF rate. And that upper line, the second upper line goes up to 15 percent by the year 2002, the bottom line goes up to 10 percent in the year 2002.

So, the fundamental point here is from the bottom line to the top, we are talking about roughly a difference between 40 percent rate increase and 15 percent rate increase, if we can achieve the objectives of the Business Plan. We think that is significant; we think it will help the regional economy; and we think it will help keep ratepayers' rates flat. We think we can achieve that by also keeping our eye on the long term in the conservation program we are proposing, because we again believe we can deliver as much conservation as we can with the new program as with the old, just for less money and less up-front costs.

The other point that needs to be made by this graphic is even though we will have a continuing debate as we should about how the costs are split between customer groups, the fundamentals are that customers as a whole, if we are successful, should see substantial benefits in the way of additional monies remaining in the region for economic growth purposes and for conservation purposes as well.

Now, how are we going to get down to this bottom line? There are three fundamental areas. Let me go briefly through those: strict cost-management control; program reinvention; and finally, new products and services.

You are aware of the two tiers we have proposed, tier 1 and tier 2. Tier 2 is designed to reflect the cost of new generating resources and we expect these rates would serve about 10 percent of the utility existing load and any future low growth that they choose to have Bonneville serve. This tier-2 rate would compete directly with other power suppliers in the market.

We must also unbundle our products and services. We think in the unbundling of these products and services, there is a lot higher value in shaping specific products and services toward the unique needs of each utility. These unique products that they would buy from a menu of services in a willing manner, we think there is higher value that is added, and that is where some of the money comes from in terms of new revenues. And, we think that money will come from a willing buyer/willing seller basis.

We also fundamentally changed what we think is the hassle factor of doing business with Bonneville. I don't think we are a Soviet-style bureaucracy, but I get your point. Ironically, I think the Russians are coming out here next month for us to teach them how we

do public involvement, because we have been given exemplary status on that, which I am very proud of. But in any event, we have a focus now on our universities and constituent groups, Northwest tribes, States and local groups which we have never had before.

Finally, we are reducing costs and we believe we have to do this because, again, market forces leave us very little room to cover costs otherwise. With our project rates at the top of that schedule, we would expect to have a cost of 2.8 billion in 1996, and 3.3 billion by 2002. Under our changes, we would hope to hold the cost constant roughly, 2.8 billion through the year 2000.

Now, you have asked us specifically, and I am going to be real brief here, to talk about how we responded to the task force recommendations. And I am going to go through these and we can provide more of this information as you like.

First of all, we congratulate you and Senator Hatfield for introducing the refinancing legislation which we think will end one of the big uncertainties that hangs over the future of our rate questions, and that is this uncertainty about repayment reform, and we appreciate your efforts on that front.

We agree we need to cut positions and we are already reducing our work force and our objective is to go to at least 600 to 800 positions within the next few years. To date, we have already gone down. We have reduced over 260 positions from our VSI, the Voluntary Separation Incentive Program, and we expect to make greater progress as the business plan picks up. We agree that one in three needed to be terminated. We proposed that to the Supply System and the board voted to do that earlier this spring.

As you heard, I think from Mr. Council, Bonneville has initiated an effort to try to work with them directly to reduce their costs 3 to 4 percent annually over the next years. This will begin to more closely align those costs with what we believe to be the appropriate industry levels.

We are proceeding to implement the world's most costly fish and wildlife program and we think it is vital again to Bonneville's mission that we do so, and we get results for it. We have been consistent in the application of the fish program for the last 14 years, by the definition of the governors and the NW Power Planning Council that put it together. We have tried our best to respond to the region's program.

We are now responding to the needs of the National Marine Fisheries Service in enhancement of river operations for fish. As you know, this is a major program, and for the money we are spending as ratepayers and Northwesterners, I think we can all agree we need a world-class fish and wildlife program. We simply have to deliver this, because people are demanding that the value we are putting on this show up in the way of environmental benefits.

We agree that there needs to be a comprehensive analysis of economic costs and benefits to the Northwest region's aluminium industry. Bonneville and public utilities agree that the contractual mechanism should be developed, as was described earlier, which will require customers to develop integrated resource plans.

We believe strongly that the government corporation status, as you and I have discussed previously, has \$25 to \$35 million in ben-

efits. It is a very focused piece of legislation that has been discussed in the region in the recent months and we have to have that presented by the administration in the near future.

We agree that current rates for irrigators and aluminum companies must be reviewed to eliminate subsidies. We are addressing these issues in our business plan development and, in fact, are going further by reviewing all rates, including the residential exchange, the irrigation discount, the low-density discount and melded rates in an honest effort to assure that customers pay for the cost they place on the system.

Finally, on the reinvention of the conservation program, if I could have the final graphic, I want to make a couple of important points that I think are valuable with respect to Bonneville's reinvention. Now, you have heard that we have gone through a fairly comprehensive effort, we have created a conservation subgroup, we have worked with environmental council members, and so on, to try to shape this program so that the objective stays the same, and this graphic simply gets to that objective.

The objective before in the old plan was to achieve 660 megawatts, within the period of time described on the chart. That was done in a program which we borrowed a lot of money and we directly financed it or applied it with a series of grants, essentially, to utilities. There are overheads associated with that. It is a centrally designed and controlled system, and that way it does kind of look like a system from an older era.

We think that it can accomplish much, much better ends if we begin to decentralize that system, cut the overheads and allow conservation to become focused more on the unique needs of each customer utility, along with a tiered rate signal that we think is essential to its success.

The important point I wanted to make on this, Mr. Chairman, is the borrowing cap question, and this is something that I know people have worried about, but I want to make sure it is front and center in the debate. We will continue to discuss the best way to deliver a decentralized conservation program and achieve the 660 megawatts, because we plan to achieve them with or without the business plan suggestions.

The borrowing cap issue relates to the 1.25 billion that was previously appropriated and authorized by Congress for Bonneville's conservation borrowings. If we do not change our program, we blow through the borrowing cap in approximately 1999. To me, as a Northwesterner, that means that the issue of how we do conservation, whether conservation is valued, becomes a Washington, D.C. issue, because we would have to come back to Congress and ask for additional borrowing authority on the basis of our achievements.

Under our new proposal, and the way we have designed it, we think that we will maintain a 660-megawatt program and do so without going through the borrowing cap and without having to come to Washington D.C. for additional costs, and we think that adds tremendous value.

So to sum up, Mr. Chairman, and then we can get right into questions, I just want to say this—in the final report, as I was reading on the plane coming back out here, you made a fundamen-

tal point, and that was that in the final analysis, the Bonneville Power Administration's first responsibility is to serve the people of the Pacific Northwest.

Now, we want to pledge to you and to those people something very straightforwardly. And that is, to those thousands of North-westerners and the millions of people that are affected by Bonneville, we want to pledge a smaller, more efficient government, delivering greater value as we enter the twenty-first century, that is going to demand a great deal of all of us. We want to pledge to do everything we can within our powers and with your help to deliver fundamentally stable rates in our most important product lines, and the reason is because we want to stay ahead of changes in the industry so that we can deliver the fundamental values associated with our mission and what people have come to expect from Bonneville.

Finally, we pledge to do everything in our power at the same time to deliver world-class results in a comprehensive conservation and fish and wildlife program. And finally, to get and enhance the promise and the vision of the Pacific Northwest Power Act which we continue to believe is correct in its vision and can be applied in an innovative way as the twenty-first century approaches.

Thank you very much for your time.

[Prepared statement of Mr. Robertson follows.]

STATEMENT OF
JACK S. ROBERTSON
DEPUTY ADMINISTRATOR
BONNEVILLE POWER ADMINISTRATION
U.S. DEPARTMENT OF ENERGY
BEFORE THE
COMMITTEE ON NATURAL RESOURCES
SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS
U.S. HOUSE OF REPRESENTATIVES
AUGUST 9, 1994

Statement of John S. Robertson, Deputy Administrator**Bonneville Power Administration****August 9, 1994**

Chairman Miller, Congressman DeFazio, and Committee members, it is my pleasure to appear before the House Committee on Natural Resources. I am Jack Robertson, Deputy Administrator of the Bonneville Power Administration.

Today, I am prepared to provide the Committee with updates on several critical issues involving the future of Bonneville. Our goal is to become an exemplary Federal agency. We seek to become the epitome of good government aimed at delivering more value for less cost.

In my testimony, I will first discuss how the electric utility industry, particularly in the Northwest, is continuing to evolve into a more competitive marketplace. Next, I will address the draft Business Plan -- our roadmap for adjusting to this new competitive environment by managing financial risks and reducing agency costs, providing for more efficient and effective delivery of agency services (including conservation), and increasing focus on customer service. In closing, I will discuss the actions we are taking to implement the recommendations in the Majority Staff Report of the Bonneville Power Administration Task Force.

Evolution of a Competitive Market

The wave of deregulation that has swept the airline, natural gas, and telecommunication industries is now also fundamentally affecting the electric industry.

Deregulation has arrived at the wholesale level of the electric power industry. A strong, independent power production industry has recently emerged providing every utility with a

ready alternative to traditional wholesale suppliers such as Bonneville. Since the last hearing of the Bonneville Task Force, there has been considerable evolution of the electric utility market in the western United States -- particularly in the Pacific Northwest.

For Bonneville's customers, the average cost of power is currently lower than the marginal cost of alternatives such as buying gas-fired turbine generating capacity themselves, or buying power from outside the Region. The difference, however, between Bonneville's price and that of alternative sources of electricity is now much smaller than it has been historically when nuclear power and coal were the principal alternatives to BPA power (see attached graph). The competition is within 15 to 20 percent of the BPA rate. Customers are now considering several factors other than price. The financial stability and predictability of Bonneville as a supplier is a key issue with our customers. Some Bonneville customers are considering or planning to pay premium prices for power elsewhere in order to avoid unpredictable cost increases.

The prospect of competition for sales to Bonneville's customers appears increasingly real as time has passed. We believe that absent a significant change in direction, Bonneville's rates can become uncompetitive. While we understand that not everyone agrees with our assessment, it is clear that some of our customers are taking actions. For example, Clark County Public Utility District (Clark) has recently signed a letter of agreement to purchase the output of a 245 megawatt cogeneration unit. Clark is Bonneville's fifth largest customer and this purchase would displace half of this utility's load. If this resource is brought on-line, it will reduce Bonneville's revenues in the range of \$10 to 20 million annually.

Another Northwest utility, Snohomish County Public Utility District, issued a request for resource proposals and has received 88 responses totaling more than 8,000 megawatts. The National Energy Policy Act of 1992 opened access to transmission lines, bringing new players and new arrangements to the energy arena. A variety of resources are being offered, from new gas-fired resources in the Northwest to extraregional resources that

would rely on wheeling arrangements over Bonneville's system. This plethora of offers clearly has implications for Bonneville's ability to market its products both within and outside the Pacific Northwest.

In the Northwest alone, some 1,400 megawatts of new generation are in service or under construction and another 3,000 to 4,000 megawatts are being studied. The Federal Energy Regulatory Commission has approved more than 20 new power marketing firms to buy and sell power at market prices. Moreover, work is underway to establish a west coast electricity futures market.

While our rates are still competitive, customers must consider the future financial and business risks of relying on Bonneville when deciding whether to continue to buy power from us or choose other sources. Unless we take action to increase the competitiveness of our rates, we could face a loss of 1,400 average megawatts from Bonneville's 9,000 average megawatts load in the next few years.

Financial markets are also changing the views of electric utilities -- particularly those such as Bonneville with high fixed costs, and/or operating at the wholesale level where the greatest competition is occurring.

Several recent analyses by bond rating agencies and other financial institutions have reached similar conclusions about changes coming to the electric power industry. The message is that a utility's ability to survive will be based on favorably maintaining or achieving a competitive advantage in key risk areas. Three of the most common rating factors are cost structure and financial flexibility, relative cost of power, and customer alternatives.

Utilities such as PacifiCorp, Idaho Power Company, Washington Water Power, and Puget Sound Power and Light are viewed by financial analysts as likely to emerge as strong competitors. Most of these companies have fixed cost ratios of between 50 and 60

percent; average generation costs below the Western States Coordinating Council average, and generally low industrial load exposure. In comparison, Bonneville's fixed cost ratio is 80 to 85 percent. The fixed cost ratio is due primarily to a heavy debt load from our nuclear investment in the 70's and 80's, including two non-working plants, and a historical reliance on 100 percent debt financing for other BPA capital investments.

Bonneville's higher fixed costs reduce our flexibility to respond to price competition and still assure cost recovery. This situation would be further aggravated by any major loss of existing loads. It is unlikely that the power from large quantities of lost loads could be resold at similar or higher prices.

We are at risk in a number of areas. These risks spring not only from our agency's high proportion of fixed costs, but also from significant environmental cost exposure; price-sensitive direct service industrial customers; potential regulatory burdens and delays; and the vulnerability of certain small customers to merger or takeover. Because of these risks, Bonneville could be viewed as an unstable power supplier, business partner, or credit risk.

In August 1993, Standard & Poor's noted three factors critical to Bonneville's financial flexibility: rate-raising capability; reserves; and cost control. They concluded that the use of further Bonneville rate increases should be increasingly discounted as a viable alternative. This would leave the maintenance of adequate reserves and cost control as the two elements over which Bonneville can exercise primary influence to maintain its competitiveness.

While the industry is being significantly transformed by these and other trends, Bonneville is uniquely situated to carefully consider and respond to these changes. Bonneville has a renowned hydro-based power system that enables considerable operating flexibility at low cost, plus a strong transmission system which provides access to diverse markets and may be used to create new, competitive markets. The challenge that confronts Bonneville is

how to balance and preserve these strengths for the benefit of customers and other stakeholders given the strong forces of change.

Business Plan

Like a commercial business, Bonneville succeeds only if its customers buy its products. Until recently, our agency faced no real competition. Our prices were so low compared to other sources, that most customers saw no reasonable alternative. Today, for the first time ever, our rates are not dramatically lower than those of other power suppliers. And, at the same time, our costs -- particularly those for fish and wildlife -- have been increasing dramatically.

In 1993, our analyses revealed that we were planning to spend \$300 million to \$600 million more each year than we would likely receive in revenues if our rates were left unchanged. We are proposing to close this gap by exerting strict cost management and becoming market driven -- that is, broadening our revenue base by redesigning products and services to retain and build our customer base. The Business Plan is the pivotal element of the Competitiveness Project launched in February 1993. The plan will help steer Bonneville through the competitive challenges it faces to achieve its fundamental legislative mandates.

Bonneville believes implementation of the Business Plan is necessary for two key reasons. First, we believe that business as usual is likely to lead to a path of significant rate increases over the next decade. As our revenue base shrinks, we risk being unable to fulfill our legislative mandates. The Business Plan is our attempt to minimize or eliminate those projected rate increases.

Moreover, we believe that the type of fundamental change the electric utility industry is experiencing as a result of increasing competition compels a new approach to our business in addition to addressing the financial dimension of the business. We are trying to get in

front of these problems. We share the view of the Majority Staff Task Force Report that the goals of the Northwest Power Act are sound. We are seeking means to assure the objectives of BPA's existing authorities will continue to be carried out.

Marketing Strategy

Our draft Business Plan proposes new approaches to Bonneville's major programs including conservation, fish and wildlife, resource acquisition, and financial management. It includes new marketing strategies designed to give utility and industrial customers more choices, and highlights three business lines -- power, transmission, and energy services.

Bonneville's new marketing strategy has two key goals. The first is to stabilize its current business and revenue base. This goal will be secured through reducing or holding costs constant and by tiering rates - providing a stable rate signal to existing loads while allocating costs of serving new loads with competitively based price signals. The second goal is to unbundle Bonneville's products and services so as to provide customers a choice of tailored and flexible products to meet their individual needs. To accomplish this, we are "unbundling" or separately pricing individual power products while also offering full-service packages. We are also focusing on the distinct needs of customers through market segmentation, and have placed account executives in the field to work one-on-one identifying needs, negotiating contracts, and solving problems. Constituent account executives have also been established to maintain our critical links with Northwest Tribes, interest groups, and state and local governments.

The draft Business Plan envisions the new Bonneville as three linked businesses -- power, transmission, and energy services including conservation. Each of the business lines will be self supporting and together they will provide the full range of Bonneville products and services. Customers and constituents alike assisted us in addressing issues relevant to development of these business lines.

The power business line holds a key element of the Business Plan -- a two-tier rate proposal which will reflect the costs of existing and new resources. Most of Bonneville's customers' existing electricity needs would be served at the lower tier 1 rate. Tier 1 is designed to reflect costs of existing resources, including fish and wildlife. We expect that about 90 percent of firm loads now served by Bonneville would be at this level.

Tier 2, set at a higher rate, is designed to reflect the costs of new generating resources. Bonneville expects that these rates would serve about 10 percent of utilities' existing firm loads and any future load growth they choose Bonneville to serve. Tier 2 would compete directly with other power suppliers in the market. I would add that tiered rates give utilities a strong incentive to run their own conservation programs to avoid the higher tier 2 rate.

The transmission business line provides wheeling services and transmission for all power. Our goal is to remain the bulk power transmitter or "wheeler" of choice for Northwest and interregional power flows by providing fair and open access to our grid consistent with the requirements of Section 722 of the 1992 Energy Policy Act. Opening access will foster competitive power markets and help Bonneville sell its tier 2 and unbundled power products in those markets.

Bonneville's first priority will be to provide reliable transmission for its existing firm power and transmission obligations. If there are competing requests for new services over limited space, priority will go to Northwest loads in a manner that comports with all applicable laws. Transmission services will be provided at the lowest rates that recover total transmission costs, without placing undue burdens on existing customers.

Demand-side management is the first in what we expect will become a broad-based set of services offered under the energy services business line. Others will be added as customer needs become more clear. The demand-side management product line is part of Bonneville's new approach to conservation. It will include the agency's existing

conservation programs and portions of those programs, plus new services for peak-load management, as is now practiced in some other parts of the country. Demand side management products and services will be competitively priced with tier 2 service and unbundled products.

Direct Service Industry Loads

About one-fourth of Bonneville's sales are to aluminum smelters and other large, direct-service industrial customers. Bonneville is proposing to tier rates to the direct service industries (DSIs) in a manner consistent with tiering to publicly owned utilities.

As with rates for the publicly owned utilities, DSI rates would be tiered to send an appropriate price signal to promote more efficient resource acquisitions and conservation. Even if DSI loads do not grow, any portion of their load facing higher cost tier 2 service would have added incentive for more efficient power usage.

Our approach to tiering rates for the DSIs follows the approach for publicly owned utilities. But since the DSIs do not receive firm service for their entire load, a percentage of the DSIs' historical purchases would be used to determine a billing amount for any power sold at the tier 1 price. Each DSI can purchase any additional amount of service at the tier 2 price up to its contract demand amount.

Regarding follow-on contracts with the DSIs, Bonneville is contractually obligated upon request to attempt to acquire sufficient resources to serve the requests and to negotiate a power sales contract in good faith if sufficient resources are found. If those resources are not available, however, Bonneville is not obligated to offer new contracts.

In terms of resources available to serve the DSIs generally, Bonneville supports the development of integrated resource plans by the DSIs to assure that through proper

resource development, including cost-effective conservation, there will be sources of supply available to the DSIs.

Reducing Costs & Managing Financial Risks

As is true with any business, reducing costs and managing financial risk is key to remaining competitive. However, market forces are leaving very little room for Bonneville to cover its costs or otherwise increase revenues by increasing rates.

When Bonneville set its current rates, total costs were projected to run \$2.8 billion in 1996, increasing to \$3.3 billion by 2002. Since that time, certain costs have risen, such as power purchases due to drought, and mitigation costs for fishery impacts.

We are proposing to cut other costs by an average of \$279 million per year by 2002. The magnitude and direction of these reductions were determined by the Marketing Plan along with other aspects of Bonneville's competitiveness project, including the Function by Function Review. These cost reductions are based on two separate efforts. The first are general productivity improvements across all Bonneville activities. These reductions can be characterized as "doing what we currently do more efficiently".

The second area of reductions is in program reinvention, or fundamentally changing what we do. Reinvention efforts impact all Bonneville activities, with particular emphasis on Conservation, Fish & Wildlife, Sales and Customer Services, and Transmission Services. As a result of these reductions, our cost projections under the Draft Business Plan remain at \$2.8 billion for 1996, and will stay flat at \$2.8 billion per year through 2002.

Capital Sources

A recent report issued by the General Accounting Office criticized Bonneville's policy of borrowing for substantially all its capital programs, stating the agency leaves little

flexibility for meeting future challenges. The GAO pointed out that "Bonneville is more heavily leveraged than other utilities" and that "over 50 percent of BPA's revenues went toward debt-servicing costs in 1993."

Bonneville borrows from two lines of credit with the U.S. Treasury, a \$1.25-billion line for conservation and renewable resource acquisitions, and a \$2.5-billion line for transmission, fish and wildlife, and other costs. Prior to the Business Plan, Bonneville projected that the second credit line would be obligated as early as 1997, and the first by 1999.

For the conservation borrowing authority cap, we believe there is a solution to the problem of approaching the cap. We are proposing new approaches to financing conservation such as tiered rates and user-financed conservation energy service charges or other products allowing us to continue to support conservation within the current borrowing cap for the foreseeable future. Capital borrowed by Bonneville to invest in market transformation and related efforts will still be repaid through Bonneville power rates.

For the transmission and fish and wildlife borrowing authority cap, the draft Business Plan proposes to limit capital investments to those which best meet consistent Bonneville-wide criteria. This is expected to help us reduce capital spending. We also propose to pay for \$30 million a year of new capital investments through current revenues. We are also assessing other potential sources of capital such as third-party financing. Using these techniques, we believe we can avoid exhausting the transmission and fish and wildlife fund until 2001, but this is not a permanent solution.

Managing Financial Risks

A significant issue in the draft Business Plan is managing the agency's financial risks. Bonneville completed a 10-year Financial Plan in early 1993 that called for a 95 percent

probability of meeting all of our annual debt payments to the U.S. Treasury in full and on time. To achieve this repayment goal, Bonneville targeted reserves of \$535 million maintained over a 10-year period and an interim rate adjustment of up to 10 percent as a risk mitigation feature in Bonneville rates.

Since then, BPA's financial risks have increased substantially. Much more water is now stored and released for fish flow requirements. Persistent drought has increased Bonneville purchase power costs and significantly decreased power sales revenues.

Bonneville proposes to achieve the targeted reserves of \$535 million assumed in the draft Business Plan but because of these increased risks this level of reserves yields only an 85 to 90 percent certainty of making payments to the Treasury in full each year.

Reinventing Conservation Programs

Bonneville believes its conservation program is the flagship for the electric utility industry. The largest energy conservation effort in the world lies in the Northwest. With nearly 15 years of successful programs and investments exceeding \$1 billion, Bonneville has worked with the region to set up an infrastructure which has transformed public perceptions about energy use, and has led to the most energy-efficient building codes in the nation.

In building the region's infrastructure, our agency provided sizable cash incentives to utilities, industries, state and local governments, and Northwest consumers. That, however, was the 1980s. With the infrastructure in place, what is needed now is a new approach to conservation -- an approach that will work in the more competitive 1990s marketplace.

The new approach for the 1990s will not scrap the 1980s approach. We intend to keep what has worked best and build upon it. Under our new approach, conservation will remain unequivocally our resource of choice. We remain committed to achieving the megawatt targets set by the Northwest Power Planning Council, and have no plans to acquire new

generation beyond our existing commitments. Our goals are not changing. What is changing is how we achieve these goals. We are working with our customers and environmental groups to develop principles to guide our efforts, and are proposing a four-part approach in redesigning the conservation program.

The first involves tiered rates. With tiered rates, utilities will pay a lower rate for the bulk of their electricity load served with existing resources. Should they increase their loads on Bonneville, requiring our purchase of additional resources, they would pay a higher rate than for existing load service. The rationale is that new resources are much more expensive and the cost of these resources is not reflected when all new resource costs are averaged into a single rate. With tiered rates, utilities will have an incentive to run conservation programs thereby avoiding the high cost of increased consumption served at the higher rate.

Second are new Bonneville products and services. Rather than simply implementing Bonneville financed conservation programs, utilities can purchase our new products and services and tailor their own programs. This approach will simplify Bonneville programs and reduce overhead costs. Currently, a large portion of Bonneville's conservation investment does not go for the measures that save, but rather to administering programs that utilities could tailor and better run themselves.

Third, we are working with our customers, the Northwest Power Planning Council, and others to develop a system of decentralized Integrated Resource Plans (IRPs) that would ensure achievement of conservation targets. This approach to IRPs would include common criteria, independent tracking, and performance accountability. One key aspect to the success of such a decentralized IRP system is balancing customer choice against the Bonneville Administrator's ultimate accountability under the Northwest Power Act.

Fourth, Bonneville can help in transforming markets. Individual utilities cannot independently change government and manufacturers' policies and practices. Bonneville is making a strong

commitment to continue to take the lead on promoting appliance efficiency standards, technology improvements, and adoption of national and state efficiency codes.

To summarize, we intend to keep what's best from the 1980s approach and build on it to meet the needs of the 1990s. Conservation remains our resource of choice. We believe our approach provides safeguards by building in a transition period and allowing flexibility to make mid-course corrections to ensure that the conservation targets set by the Council are met. Utility customers and environmental groups will continue to play a key role in how the new program evolves.

Business Plan Schedule

In light of these ongoing radical changes in the utility marketplace, we are continuing to refine Bonneville's Business Plan. We want to assure the Committee that we are developing the Business Plan with significant input from interested regional entities. A Sounding Board comprised of Bonneville customers and other regional stakeholders was formed early in the Business Plan process to provide on-going advice and counsel.

Regional participation has been a critical element to development of the Business Plan. A year and a half ago, we initiated Bonneville's reorganization under the umbrella of the Competitiveness Project. We set our course with Strategic Business Objectives. A Function-by-Function Review sought out opportunities for accomplishing work more efficiently. The Marketing Plan identified customer needs and studied choices about how to meet those needs. Through Leadership EDGE (Empowerment, Diversity, Growth and Excellence) we are striving to develop excellence in managers, promote teamwork across the organization, and reinforce a strong customer and constituent orientation. All of this has been accomplished with significant and valuable public input.

A draft Business Plan was released in June. We are taking public comment through September 9th and plan to complete the Business Plan in November. We have lengthened

the comment period by three weeks in response to customer and constituent requests. This is an ambitious and demanding schedule, but it is necessary in order to reach conclusions which can be included in the President's budget submittal for fiscal year 1996 and the 1995 rate case for fiscal years 1996 and 1997.

We are listening and are being sensitive to regional parties. During the comment period we are meeting informally with customers, customer groups, government officials, public interest groups, and others on request. Over the past week, we have conducted three formal information and comment meetings, and have scheduled a wrap-up session towards the end of the comment period.

There is significant regional interest in our draft Business Plan. We have received supportive comments, but we have also heard concerns expressed about the scope and pace of the changes we are proposing. We acknowledge that our proposals represent a significant change in long-standing relationships.

But the changes in the utility industry continue to occur at an increasingly rapid pace. Bonneville is anticipating these changes and staying in front of them -- but barely in front. Absent significant actions now, we and our customers will face even greater disruptions later. By moving ahead aggressively to implement the Business Plan in the 1995 rate case and power sales contract renegotiations, we hope to avoid substantial rate increases and minimize the period of uncertainty.

If we are unable to begin introducing tiered rates and unbundled products in fiscal year 1996, we and our customers will face continued uncertainty. If we maintain the status quo, we would expect to need to increase our rates in fiscal year 1996 by 10 to 15 percent. The competitiveness of our rates is directly related to our ability to recover costs, and therefore to our ability to repay Treasury on time and in full in the future.

We will continue to engage the region in these discussions, and we remain open to revising our Business Plan and implementation schedule. However, I want to stress the potential consequences of delay -- extended disruption and uncertainty throughout the Northwest utility community.

If utility markets unfold as we project, and Bonneville is unable to make the adjustments necessary to compete successfully, these issues may require Congressional action to resolve. We believe we are on the right track, and if we can maintain our current momentum, we expect to stay ahead of our competitors and secure our position in the evolving west coast energy market.

Implementation of Majority Staff Recommendations

As indicated in the Majority Staff Report, Bonneville is at a crossroads. We recognize the issues the report raises and believe the Task Force produced numerous useful outcomes. The Northwest economy needs a healthy Bonneville and this report helps by focusing attention on our situation. No one disagrees that we need to change.

As a result of the competitiveness efforts we initiated over a year ago and the recommendations contained in the Task Force Report, we are making great strides in adjusting to this more competitive industry. I would take this opportunity to discuss some of the specific actions we have taken.

I will reiterate the first of the report's findings -- the goals of the Northwest Power Act remain sound. Bonneville remains fully committed to the Northwest Power Act -- particularly with respect to energy conservation and fish and wildlife. Our agency needs to become more competitive, but we will not do so at the risk of sacrificing the region's commitment to conservation and renewables and rebuilding salmon runs.

Consistent with the recommendations in the Task Force Report, a debt refinancing bill has been introduced which can resolve the repayment reform debate and not lead to any significant increases in Bonneville's rates.

Contrary to our earlier view, Bonneville agrees with the Task Force that a tiered wholesale electric rate should be only one element of the agency's conservation acquisition strategy. Consistent with requests from conservation interest groups, we are now proposing to retain regionally subsidized conservation through market transformation activities. We have also agreed to maintain our energy conservation programs, but will finance them through an energy service charge rather than through power rates.

We are pleased to report that in response to Bonneville's urging, the Washington Public Power Supply System's Full Board of Directors voted to terminate Washington Nuclear Projects 1 and 3 on May 13, 1994. The Supply System has begun the termination process by advertising the sale of the projects and starting the planning process for termination in the event that no buyers of the projects as a whole are found.

With regards to Washington Nuclear Project No. 2, Bonneville and the Supply System have agreed to have substantive discussions this fall on the setting of specific cost and performance goals. We have requested that the Supply System reduce their budgets by approximately 3 to 4 percent annually for the next few years until their costs are more closely aligned with what we believe to be industry levels.

Bonneville is proceeding with implementation of both the Regional Council's Strategy for Salmon and the National Marine Fisheries Service recommendations for avoiding jeopardy to the continued existence of listed salmon stocks. We absolutely agree that Bonneville must remain committed to the conservation and fish and wildlife goals of the Northwest Power Planning Council. The draft Business Plan focuses our programs on results and providing greater certainty, not on dollars spent.

Bonneville agrees there needs to be a comprehensive analysis of the economic costs and benefits to the Northwest of the region's aluminum industry. We are, in fact, attempting to conduct cost of service analysis for all customer groups to gain a better understanding of where costs are incurred on our system.

Bonneville and its public utility customers agree that contractual mechanisms should be developed which will require customers to develop integrated resource plans. We are committed to developing this mechanism collaboratively with our customers.

Bonneville has proceeded cautiously with the government corporation proposal. We are addressing the "side effect" concerns with interested parties, and will continue to seek regional consensus before proceeding with legislation.

With respect to the proposed cost savings identified in the Task Force Report, there was approximately \$150 million in savings identified. Of this amount, over \$90 million is associated with costs which BPA does not directly control, that of the Supply System and the Bureau of Reclamation Power Rate.

Of the remaining amount the vast majority is in the category of reviewing current rates for irrigators and aluminum companies to attempt to eliminate subsidies. We are addressing these issues in our Business Plan development and in fact are going further by reviewing all rates including the residential exchange, the low-density discount and melded rates to attempt to assure that customers pay for the costs they place on the system.

The Business Plan proposes real change in the way Bonneville conducts business with its customers. At the July Task Force hearing in Portland, much discussion was focused on the "hassle factor" associated with doing business with Bonneville. It was a frustration expressed by our customers and stakeholders alike. That's exactly why we are streamlining our functions and moving to become more customer-focused and results-

oriented in all of our business dealings. To our customers and stakeholders we are saying, "We hear you."

We have completely reorganized the agency aimed at improving customer and constituent service. Customer and constituent account executive positions have been created and it has been made clear to all employees that everyone in the organization works to support the account executives. Granted, these types of changes do not occur overnight and do not occur without some pain. We believe, however, and the Portland hearing made this eminently clear, that this type of fundamental change is necessary.

The Portland hearing was also especially important to us in terms of initiating internal actions. We are well on our way to reducing our total workforce by 600 to 800 positions. To date, we have reduced our Bonneville personnel by more than 260 positions.

Conclusion

This testimony is one in a series of progress reports. Much remains to be done and a number of opportunities remain for involvement of our customers and constituents.

By becoming more market-driven, customer-focused, cost-conscious, and results-oriented, Bonneville can expand the benefits it has provided the region for the last 57 years, without fundamentally changing the agency's mission.

I reiterate that goals of the Northwest Power Act remain sound. Bonneville needs to be more competitive; however, we will not do so at the risk of sacrificing the region's commitment to conservation and rebuilding salmon runs.

In closing, I will reiterate that Bonneville's competitiveness is critical on a number of fronts -- both regional and national.

Our competitiveness is critical to the Pacific Northwest regional economy because we provide nearly half of the electric power and three-fourths of the high-voltage transmission in a very electricity-dependent region. Nearly 3 million people and over 1.2 million jobs in the region depend on Bonneville power.

Our competitiveness is critical to our customers because the competitiveness and survival of many of the 150 utilities and large industrial customers our agency serves in the region is closely linked to Bonneville's rate levels. Likewise, businesses and industries served by these utilities depend on an economic power supply.

Bonneville's competitiveness is critical to the environment because we contribute over \$300 million per year, including obligations and foregone revenues, to fish and wildlife, in addition to tens of millions for clear air, clean water, and hazardous waste cleanup.

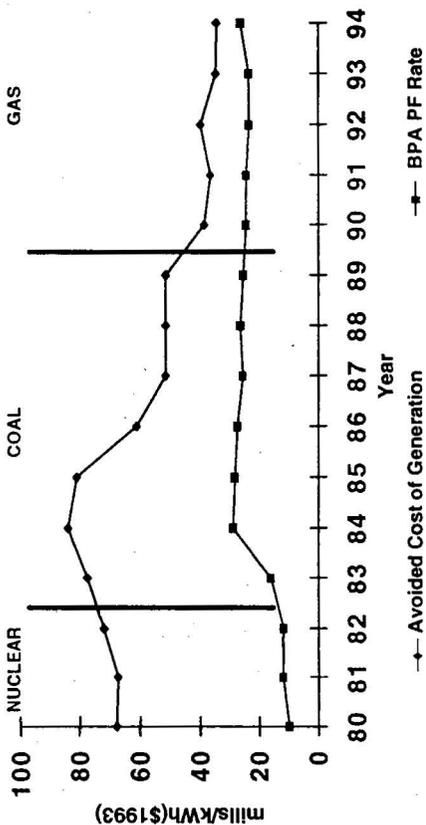
Further, Bonneville's competitiveness is important to U.S. taxpayers for operations and maintenance, principal and interest annual payments of approximately \$700 million we make to the U.S. Treasury.

In our invitation to testify, the Task Force requested that we respond in more detail to some specific points. You will find our responses attached to this testimony.

We welcome this opportunity to share our progress in creating a new Bonneville and look forward to your input, and to sharing future progress reports.

I would be pleased to respond to any questions you may have.

AVOIDED COST OF GENERATION VS. BPA AVERAGE RATE



NUCLEAR: based on actual cost of Washington Public Supply System
 COAL: based on studies by Kaiser Engineers Power Corporation, among others
 GAS: based on studies by Fluor Daniel Inc., among others

Bonneville Power Administration's (Bonneville) Responses to
Pre-Hearing Questions
Representative Peter DeFazio
August 9, 1994

QUESTIONS FROM REPRESENTATIVE DEFAZIO

Question 1: Please discuss BPA's competitive position at present and over the next ten years. What are the competitive threats? What are BPA's competitive advantages?

Answer: BPA faces many serious competitive challenges over the next 10 years, but the real competitive test will be over the next few years, when our customers will be making long-term choices about their business relationship with BPA. At present, BPA's average cost of power remains below the marginal cost of the competition (2.7 cents per kilowatt hour compared to 3.2 cents per kilowatt hour.) But BPA's price advantage has dropped from over 400 percent 10 years ago to roughly 15 to 20 percent now, and BPA's customers are wondering how much further that trend will go.

To succeed, we will have to deal successfully with a number of competitive challenges, including: (1) a steep decline in the cost of alternative power sources; (2) increases in our costs and uncertainty about how high some costs will ultimately go; (3) many capable and aggressive alternative suppliers knocking on our customers' doors; (4) deregulation of the wholesale power business which has virtually eliminated the market power BPA used to have; and (5) dissatisfied customers who would currently

prefer to do business with other suppliers. BPA's high proportion of fixed costs and seriously depleted financial reserves add to the difficulty of responding to these challenges.

The Draft Business Plan details the challenges listed above. Since the draft was published, some additional developments have reinforced the seriousness of the situation we face:

- More detail on the offers made to Snohomish Public Utility District have surfaced. Snohomish has several offers of firm power delivered to its system with prices starting in 1997 of 27 to 32 mills per kilowatt-hours. Many suppliers are offering guaranteed prices.
- 26 of our customers have signed an agreement with Power Resources Managers (PRM) for a 600 to 800 MW package of alternative resources to be managed by PRM. A final decision on going forward with this resource package is expected next year.
- Washington Water Power Company and Sierra Pacific have announced a planned merger that would create another very strong competitor for BPA.
- In terms of plant efficiencies only, new advancements in combustion turbine technology have been announced that promise to move single-cycle efficiencies from the current 40 percent to 48 percent and combined-cycle

efficiencies from the current 48 percent to nearly 60 percent of the total BTUs available from the fuel. In addition, these new turbines will offer smaller unit sizes, greater operating flexibility, and lower emissions at no increase in cost.

BPA's substantial competitive strengths include the large hydro system which has essentially zero fuel costs and zero air emissions, more operational flexibility than most utilities, ownership of 80 percent of the regional transmission grid, and a highly skilled workforce. Our challenge is to continue to leverage these strengths to overcome the challenges we are now confronting. That is what we are attempting to do in the Business Plan.

Question 2: How likely is it that BPA's rates will be uncompetitive when compared to alternative generation sources in the 2002-2003 rate period under each of the alternatives presented in the Business Plan DEIS? What analysis has BPA done to support its views?

Answer: The analysis conducted for the Marketing Plan indicated that the most-likely scenario was that our rates should stay below those of competing power sources to year 2003 and beyond, if we succeed in our efforts to control costs, offer more choice of products and services, and improve our customer service as proposed in the Draft Business Plan (and in the Market-Driven alternative in the Business Plan DEIS).

It is becoming increasingly clear that customer perception of BPA as a supplier vs. competitors is the key to our competitiveness. Many customers will not wait until 2003 to find out if BPA offers the best deal. They are acting now based on their current assessment of BPA vs. the competition. Even though long-term analysis of our rates may show that we are likely to be the lowest-cost supplier, we still can suffer major load loss if our customers see other suppliers as offering less risk, better service, and/or more stability, particularly when the long-term analysis shows only a relatively small cost advantage for BPA.

A key question about the Business Plan Draft Environment Impact Statement (DEIS) alternatives is the amount of risk they create for BPA's competitiveness. While we have not quantified this risk probabilistically,

the analysis we have done suggests that the Status Quo alternative would create more risk of noncompetitiveness because it would entail higher costs, less focus on customer service, and less customer choice about products and services. The BPA Influence alternative would provide many of the features of the Market-Driven alternative, but due to somewhat higher costs and conditions on BPA services, it poses a greater risk that BPA's rates and market position would not be as competitive. The Minimal BPA alternative could make our rates more competitive because it would entail drastic cost cuts at the expense of fulfilling parts of our mission. The Maximum Financial Returns alternative would be designed to maintain competitive rates, but would tend to exploit BPA's lower-cost services to increase net revenues. The Short-Term Marketing alternative might provide competitive rates, but at the cost of greater uncertainty of BPA loads and future rates.

The rate analysis in the DEIS shows relatively small differences in rates among the alternatives. However, that rate analysis did not include all the factors that would affect the rate differentials, because the focus of the DEIS was more on physical environmental impacts than on rates. For example, the DEIS rates analysis for the Status Quo alternative did not account for the impacts on rates of the load loss caused by the alternatives. Nor did it fully account for all the additional revenues likely to be achieved

under the Market-Driven alternative. If these factors had been included in the analysis, the rate differentials would have been substantially larger. The final EIS will address these additional factors.

Question 3: BPA's Business Plan asserts that BPA will lose at least 1400 aMW of load if the actions proposed in the plan are not implemented. However, the analysis contained in the Business Plan DEIS concludes that under the status quo only 599 aMW of firm load will be lost. How do you reconcile these figures? How likely is it that the BPA Business Plan's "death spiral" scenario, in which BPA loses more than 7000 aMW out of its present load, will actually take place?

Answer: The differences in load loss projections between the Business Plan and the Draft EIS are summarized in the accompanying table. The load losses expected under the DEIS Status Quo alternative included 213 average megawatts (aMW) of nonfirm DSI load losses in addition to 251 aMW of utility load losses and 348 aMW of firm DSI load losses, for a total loss in the DEIS of 812 aMW. The 1400 aMW load losses described in the Business Plan include 450 aMW of retail wheeling and self-generation. The Draft Environmental Impact Statement (DEIS) did not assume retail wheeling, because that would require regulatory changes that the EIS team did not include in the "no-action" alternative. (The final EIS will probably incorporate retail wheeling as a factor in load loss for the Status Quo alternative.) The other differences between the DEIS and the Draft Business Plan are a difference of 39 aMW in the total amount of direct service industry (DSI) load loss and about a 99 aMW difference in utility load loss due to somewhat more conservative assumptions in the DEIS about independent utility development of energy resources. These differences stem from the fact that load loss assumptions for the DEIS

had to be established early to allow time for the more comprehensive assessment of resource development, operations, and physical impacts.

These amounts are shown in the accompanying table:

Comparison of Business Plan and EIS Load Losses (aMW)

Type of Load Loss	Business Plan "Business As Usual" Case, by 2002	EIS Status Quo Alternative Load Changes in 2003
Public Agency Non-BPA Generation	350	231
Shift of BPA Load Obligation to Public Agencies (Independent Conservation Programs)	not listed separately	20
DSI Non-BPA Generation	600	348 (firm load)
Subtotal: BPA Firm Load Loss	950	599
DSI Non-BPA Generation for Nonfirm Load (Top Quartile)	not listed separately	213
Retail Wheeling	450	none assumed
Total	1400	812

It is unlikely that BPA would lose 7000 aMW of its present load. The "Extreme Potential" Market loss figures are merely intended to illustrate the extreme upper bound of market loss potential, given possible conditions conducive to market loss in the industrial sector and the generating capacity currently being studied by developers in the region. Though this scenario is unlikely, it is no longer totally implausible. Its plausibility reinforces the significance of the challenge BPA faces.

Question 4: The Task Force report discussed what it called the BPA "hassle factor." Described the actions you are taking to reduce the difficulties customers experience in their dealings with the agency.

Answer: BPA has set achieving customer satisfaction as its first Strategic Business Objective. Our early steps to reach that objective are as follows:

First, the reorganization now underway at BPA created a Sales and Customer Service Group. This group replaces the old Area Office structure with account executives charged specifically with improving our business transactions with the customer utilities and direct service industries. Each account executive is assigned several utilities and/or direct service industrial customers with which to deal in a much closer relationship than has hitherto been the case. The primary goal of each account executive is to improve the agency's response to customer needs.

Specifically, there are five basic business transactions with BPA that are the core of business between BPA and its customers. They include: (1) power contracts, (2) transmission and transfer contracts and agreements, (3) demand side management (conservation) agreements, (4) new and modified points of delivery, and (5) operations and maintenance agreements.

In each of these areas, the account executives will have the ability to create agreements with the customers, based on each customer's individual need, for the services available from BPA. This mechanism should reduce the majority of difficulties customers have with the agency in their day-to-day dealings. The account executives should have direct knowledge of each customer's particular circumstances. Finally, the customers should have no difficulty finding answers to their questions, and should have no question about the agency's concern for each customer's business health.

We are also revising rather dramatically the systems and processes backing up delivery of products and services to the customers through the account executives. In contrast to former practices that forced the customer to deal extensively with BPA's internal processes to meet a need, we will make those systems and processes support the account executives' direct dealing with the customers. This should reduce most of the remaining difficulties the customers experience in dealing with BPA.

We believe our conservation program should remain the flagship for the electric utility industry. Our new approach for the 1990's will build on successes of the 1980's approach. We intend to keep what has worked best and build upon it. Under our new approach, conservation will remain our resource of choice. We remain committed to achieving the megawatt

targets set by the Northwest Power Planning Council, and have no plans to acquire new generation resources beyond our existing commitments. Our goals are not changing. What is changing is how we achieve these goals. We are working with our customers and environmental groups to develop principles to guide our efforts.

We also intend to track, in a much more businesslike way, our progress toward making our customers' business with the agency easier, and adjust as necessary toward that end.

We do not intend, however, to equate reducing the "hassle factor" with always being able to give each customer exactly what he or she wants. We do intend to ensure that our business transactions are quicker, smoother, and more satisfactory to the customer. We also intend to ensure that each business arrangement with a customer meets as closely as possible both the customer's need and BPA's statutory obligations.

Question 5: BPA estimates unspecified administrative savings of \$100 million per year for the market driven alternative, but not for any other alternatives. Please describe the savings you anticipate. Would new legislative authority be required to achieve these savings? If not, why could they not be obtained under any of the other alternatives?

Answer: The \$100 million administrative cost savings were not included in the Status Quo alternative because this alternative was intended to represent conditions without the changes proposed in the Draft Business Plan. The Environmental Impact Statement (EIS) estimates were rough and some of the savings probably should have been shown and would have been achievable under the other alternatives. This modification will be made in the final Business Plan. We expect to achieve these savings through reductions in staffing, increased productivity, procurement efficiencies, better use of equipment and management of property, as well as increased performance from our contractors. While much of these savings can be captured administratively in the short run, Bonneville believes permanent administrative savings cannot be assured unless BPA obtains appropriate legislation. We will need legislative authority to achieve all of these savings in a timely manner and maintain them over time.

Question 6: Actions proposed in BPA's Business Plan, such as tiered rates, unbundled services and conservation reinvention, taken together are likely to shift costs between customer categories. For example, all customers now bear part of the costs of regional conservation investment, but many will see those costs decline under the actions proposed in the Business Plan. Others will likely see their overall costs increase. What cost shifts does BPA anticipate as a result of the proposed actions in the Business Plan DEIS? Can BPA quantify those changes for different customer groups?

Answer: BPA customers as a whole would be substantially benefited by the cost reductions and other changes proposed in the Draft Business Plan. As BPA customers now have many choices about how they meet their needs, how they are affected will depend largely on their own choices. This makes it very difficult to predict how any customer or even class of customers will be affected by the changes we are proposing.

To allow customers to make their own assessments of how they are affected by some of the proposals in the Business Plan, we are developing a Tiered Rate Impact Model jointly with our customers. This model should be available for use in September 1994. In addition, BPA has recently developed and will make available to its customers an analytic tool that calculates the retail cost of utilities paying directly for the conservation resources within their service territory and compares that to a scenario where BPA continues to rate-base the costs of a regional conservation program.

Question 7: Under the tiered rate and unbundled services scenario described in the Business Plan many preference customers will be purchasing a “rebundled” package including tier 1 and tier 2 power, as well as shaping services. Will the price of shaping services for such customers be cost-based and, if not, how does that satisfy BPA’s cost-based rate-making mandate?

Answer: BPA rates in total will be cost-based, consistent with Section 7 of the Northwest Power Act and other applicable statutes. Shaping services will be priced within that context.

Question 8: The Business Plan DEIS estimates that, compared to the status quo, the market-driven alternative will yield about 40 aMW of utility-sponsored conservation as a result of a tiered rate's price signal, 22 aMW as a result of fuel switching, and 130 aMW as a result of independent utility programs. What elements in the market-driven alternative contribute to the 130 aMW of additional utility sponsored conservation?

Answer: The total regional conservation is the same under both status quo and the market-driven approach. Both the status quo and market driven approach have embedded the same 130 aMW of conservation savings. In the status quo approach these savings were to be obtained through the retail utilities operating (and paying through their wholesale power bills) BPA's existing conservation programs. Under the Market Driven approach the public utilities will acquire approximately 130 aMW of conservation savings with their own funds. The large generating public utilities are expected to acquire roughly 100 aMW. This estimate is based upon our review of these utilities' existing conservation plans (prepared in late 1992) and supplemented by recent discussions with staff from these utilities pertaining to their likely response to BPA's Conservation Reinvention. These utilities indicated that they would most likely continue to fund their conservation programs to the level that made sense for their specific situations. The conservation savings estimates are assumed to be spread across consuming sectors consistent with each utility's previous local conservation plans. However, many utilities feel that they are capable of delivering the right "mix" of conservation for their utility more efficiently and cost-effectively

under the market-driven alternative than under the current BPA system. Cost savings mentioned by these utilities have included lower incentive levels and access to tax-free financing. The remaining public utilities served by BPA are expected to acquire nearly 30 aMW through similar, independent actions.

The 40 aMW of price-induced conservation is a direct result of end-consumer efficiency actions in response to retail tiered rates. Our analysis indicates that some of BPA's retail utility customers are likely to pass along tiered rates to their retail consumers in response to BPA's wholesale tiered rates. In addition, the 22 aMW of fuel switching reflects the lost conservation potential associated with a total fuel switching response to tiered rates of 150 - 200 aMW.

Question 9: What steps is BPA prepared to take if the plan's expected conservation achievements are not fulfilled? How many years of underachievement will be allowed to pass before BPA takes steps to improve regional conservation acquisition?

Answer: BPA, working with customers, Northwest Power Planning Council, and constituent groups (Northwest Conservation Act Coalition, state energy offices, Natural Resources Defense Council), is currently developing a collaborative and mutually agreeable system for tracking the region's conservation acquisition efforts. A component of this system will entail periodic review and assessment of whether the region is acquiring the appropriate level of conservation resources. During this review, if it were determined that the region is falling short of our conservation goals, a temporary mid-course correction would be implemented. This correction would remain until we are assured that the pace of regional conservation acquisition is, and will likely remain, consistent with our goal. The specific components underlying this mid-course correction are also being developed by BPA, its customers and constituents.

Question 10: Does BPA need new legislative authority or any changes in existing authorities to implement its conservation reinvention plans?

Answer: BPA does not need new legislative authority or any changes in existing authorities to implement its conservation reinvention plans. The Draft Business Plan proposal for conservation reinvention merely reshapes the way in which BPA will achieve its conservation goals. In this way, BPA plans to utilize scarce conservation dollars in the most efficient way possible.

The Northwest Power Act authorizes the Administrator to determine the mix of conservation measures that will most efficiently and economically meet the Act's conservation goals, as defined by the Council. The Act gives BPA broad flexibility to carry this out in a variety of ways.

BPA believes it can achieve its share of the Council's conservation goals while reducing dollar expenditures on conservation. By doing so, BPA will not only achieve the goals of the Northwest Power Act with respect to conservation acquisition, but will also be operating in a businesslike manner to assure the Pacific Northwest an economical supply of electric power, as the Northwest Power Act requires.

BPA would consider offering loans as a future demand side management product. Each appropriations act for the past several years has contained language prohibiting BPA and other agencies from making loans or loan guarantees, even though BPA is otherwise authorized to do so. BPA is developing suggested language for the Fiscal Year 1996 appropriations bill that would allow us to offer loans.

Question 11: What are the implications of the Business Plan for the development of renewable energy resources?

Answer: Under the Status Quo, BPA is conducting several demonstration programs for wind and geothermal development. It is expected that these projects will be equally valuable in a market driven future. In fact, BPA customers with extensive transmission costs to reach their service areas may see advantages in small scale, on site renewable generation. BPA intends to address the needs of those customers through expertise gained in the current renewable demonstrations. It is also possible that there may be a market for "greenpower" products in Tier 2. BPA is just beginning to explore these alternatives, and what specific mix of wind and geothermal products best achieves these goals consistent with our overall objective of minimizing future expenses.

Question 12: In the Business Plan DEIS, it is correctly stated that BPA has no statutory obligation to serve the DSI load after the current contracts expire. Does BPA plan to conduct a comprehensive review of the costs and benefits to the region of the DSIs as a means toward developing alternative rate structures and contract provisions for that customer group? Why is there no discussion in the Business Plan of alternative contractual arrangements for the DSIs, such as increased interruptibility, greater reliance on nonfirm power sales or seasonal sales.

Answer: The Northwest Power Act required BPA to offer initial contracts, but did not address the question of service under subsequent contracts. However, BPA's 1981 Direct Service Industry (DSI) contracts obligate BPA to attempt to provide service by purchasing sufficient resources to serve any DSI request for follow-on service. The 1981 DSI contracts imply a BPA good faith obligation to try to provide continued DSI power service.

BPA is conducting a DSI cost of power service study. We intend to address the 1995 net cost of power service to the DSIs based on the estimated 1995 cost allocation to the DSIs, the seasonal and hourly benefits of DSI loads, and the value of DSI stability reserves. We also intend to estimate the value of BPA power to the DSIs, as well as the potential BPA margin for the DSI segment. The study should help to clarify issues such as alternative DSI rate structures and contract provisions.

One of the purposes of the Draft Business Plan was to close the anticipated BPA revenue gap through customer load retention. Under the "business-as-usual" scenario, BPA was at risk of losing up to 750 aMW of DSI load

to alternative power sources such as combustion turbines and retail wheeling.

Our current intent is to try to shape product and services offerings to DSIs so that both BPA's business needs and the DSIs' needs are met. The Northwest Power Act does require that DSI rates be equitable in relation to rates paid by industrial customers of public agency utilities. This requirement will guide pricing proposals for DSI rates. We do not know yet what specific products and services will yield the best economics for BPA as a supplier and the DSIs as customers, but we should be able to define this for the final Business Plan. There will also be ample opportunity for interested parties to participate in the discussion about DSI service through the rate case. We anticipate that issues such as greater interruptability or seasonal sales will be addressed during power sales contract renegotiations.

In both the business plan and the upcoming rate case, our goal is to provide rates to the DSIs comparable to rates paid by public utility industrial customers.

Question 13: How does BPA justify its proposed treatment of new public power entities under its tiered rate proposal?

Answer: “Section 5(b) (1) of the Northwest Power Act, 16 U.S.C. § 839c (b))1) obligates BPA, if requested, to offer to sell power to Pacific Northwest publicly-owned and investor-owned utilities to meet their firm power needs.” This obligation extends to newly formed preference customers. We are proposing that if the original customer purchased or could have purchased, either directly or indirectly, some of its power from BPA at the Tier 1 rate, the newly formed customer should purchase a similar amount of power at the Tier 1 rate. When a new customer is formed from existing public preference customers in a merger, the new customer will get the sum of the original customers’ Tier 1 amounts. When a new customer is formed from an existing public preference customer by dividing the service territory, the new customer will get a pro rata share of the existing customers’ Tier 1 amount. Since this approach combines or divides the original Tier 1 billing amounts of existing customers it will not affect other customers’ Tier 1 billing amounts.

When a new preference customer is formed from an Investor Owned Utility (IOU) service territory we are proposing that the new customers’ Tier 1 billing amount would be calculated based on a pro rata share of the residential and small farm loads in that portion of the IOU’s service

territory which formed the new preference customer. This approach divides the original residential exchange Tier 1 billing amount of the IOU with the new customer. Many of BPA's public preference customers have advocated that the new customers' Tier 1 billing amount be calculated based on the total load (residential and small farm plus commercial and industrial load) in that portion of the IOU's service territory which formed the new preference customer. We believe that this could create a greater incentive than would otherwise exist for new customers to form if a large industrial or commercial historical load, which would be used in developing the Tier 1 billing amount, went away. In addition, this proposal would result in less stable shares for existing preference customers.

Question 14: What is BPA's expected schedule for implementing its tiered rate proposal? Is BPA prepared to take an alternative course if regional support for BPA's tiered rate proposal is lacking? If so, what alternatives is BPA considering?

Answer: BPA is planning to propose the implementation of tiered rates in its 1995 Rate Case. Rates developed during that rate case will go into effect on October 1, 1995. In all likelihood there will be disagreements about the details of tiered rates, and we intend to use the current regional tiered rate workshop process and the 1995 Rate Case to consider any alternatives presented to BPA's tiered rate proposal.

Question 15: What opportunities exist for BPA to expand its sales of power outside the region and the profits from those sales? Should Congress consider providing any new authorities that would allow BPA to maximize its returns on the sale of power surplus to regional needs?

Answer: Several years ago, greater opportunities to sell surplus power outside the region existed than do today. Even so, BPA had difficulty marketing its surplus at favorable prices during the 1980's. The days of such a demanding extraregional market for surplus BPA power are gone -- victims of the decline of the California economy, the construction of huge amounts of new nonutility generation in the southwest, and the steep decline in gas prices. Even with the continued scarcity of nonfirm hydro, prevailing wholesale prices for energy have recently fallen to levels within the high teens to mid-20 mills/kWh range for transactions between the Northwest and California. The more surplus power BPA attempts to sell, the lower the price tends to go.

There is still an extraregional market in which BPA will participate, but it is unlikely to fully replace the loss of revenues created by loss of Northwest load. Prices for surplus BPA power would be somewhat higher without the required termination of delivery provisions which are required by the Northwest Preference Act. However, we do not believe that the limited, additional revenues would justify revisitation of such a fundamental aspect of preference to BPA power at this time.

Mr. DEFAZIO. Okay. Thank you.

There were not a lot of items in total agreement here today, but we did seem to come to some consensus on something, which I don't believe was in the original business plan which would be to basically go to a market-based system on the value of reserve and allow bidding by other interested parties than the aluminum industry.

Do you think that is something that we can get consensus from?

Mr. ROBERTSON. It is an interesting idea and Walt and I were talking about that. I would like to have him answer the question, if he may.

Mr. DEFAZIO. Yes.

Mr. POLLOCK. Mr. Chairman, I think some of the reserves ought to be priced according to what their availability is at and sold by other parties in the marketplace. There may be others that should be required of customers obtaining service from us or other utilities. So, I would be hesitant to say all reserves ought to be priced at market, because there is a statutory requirement for the DSIs to provide certain reserves to the region through Bonneville where we are uniquely—where they are uniquely able to provide them. So, in general, the market should determine the value of these products and services, but I think there might be some exceptions when it comes to the DSI reserves and we would like to, I think, provide you some follow up information on that.

[The information follows.]

BPA's system needs stability and operating reserves. Stability reserves are used to protect the transmission system from catastrophic impacts resulting from loss of a major power facility, particularly large transmission lines linking the Pacific Northwest and Pacific Southwest Interties. Operating reserves ensure that a utility has enough generation to meet its load even if it suddenly loses a resource. There are two types of operating reserves, spinning and non-spinning.

The Northwest Power Pool (NWPP) requires each member utility to carry operating reserves equal to 5 percent of its on-line hydro generation and 7 percent of its on-line thermal generation. Under current Northwest Power Pool criteria, spinning reserves must be in the form of on-line unloaded generation. Non-spinning reserves may be either (1) generation that can be brought on-line within 10 minutes of a system disturbance, or (2) load dropping that can be accomplished in the same time frame.

The DSI's currently provide a portion of BPA's non-spinning operating reserves. Because of the adverse revenue and customer service impacts of dropping load, BPA used these reserves as a last resort. They are used primarily during cold snaps and fish flushes. There are discussions underway that would potentially allow restriction rights to be counted as spinning reserves. (Restriction rights are BPA's right to utilize the DSI power reserves by cutting them off.)

BPA builds its system to meet BPA reliability criteria, which are based on Western States Coordinating Council (WSCC) reliability criteria. Utilities are expected to be able to provide continuous electrical service to their loads during "credible" system emergencies. Loss of both DC Intertie circuits is considered a "credible" system event. BPA can withstand loss of the DC Intertie (both circuits) during export conditions and during import conditions when DC line loadings are less than 1500 MW, without relying on the DSI stability reserves. However, BPA needs the DSI stability reserves in order to import between 1500 and 3100 MW on the DC circuits and still meet the WSCC and BPA reliability criteria.

While BPA does not need the DSI stability reserves to maintain AC import capability ratings, these reserves are needed in BPA wants to continue importing at those ratings during an outage of one of the three AC lines (to protect against an outage of another line). BPA would also likely need the DSI stability reserves if the AC import ratings were increased relative to today's values.

Based on the preceding discussion, BPA feels that the DSI's are ideally suited to provide BPA stability reserves, probably up to 1800 MW for parts of each year to

maintain BPA's power import capabilities. BPA's operating reserve needs may be purchased on the competitive market, which also includes the DSI's.

Mr. DEFAZIO. What do you mean? One reserve in particular?

Mr. POLLOCK. Yes. One in particular. The stability reserves, which are the—is the capability of these large loads to be immediately tripped 100 percent, or to be brought back on slowly if there is a massive power outage in the Northwest. Those are uniquely able to be provided by large industries with these capabilities, and there was some recognition of that in the history of the Regional Power Act.

The other types of reserve, the plant, the labor reserves and what we have called forced outage reserves, I think are more amenable to the approach that you are suggesting.

Mr. DEFAZIO. Okay. Well, I would urge review of all of that and would look forward to a more detailed response.

This—there was a rather raging controversy over this 7(c)(2) delta. What is that? Can you tell us?

Mr. ROBERTSON. Walt?

Mr. POLLOCK. I will give this a shot. It will take a minute or two. But Section 7(c) of the Regional Power Act is the portion that attempts to describe to us how we should set the DSI rate. And I think you have heard other witnesses describe the basic process that is called for in Section 7(c), which is to—which is really linked to the rate that a DSI would have been served at, had it been served by a public agency. That was the underlying logic, and in my opinion, that Congress used in the Regional Power Act.

So, what it told us to do is, you take the generally applicable rate that we sell to the public agency, and then you add to that a margin or markup which would be typical for a public agency, and you deduct or adjust that for any changes in the character of service and the value of reserves. When we do that computation based on the Regional Act directives and then apply to that the history of the variable rate, in our view, we come out at the end of the variable rate period in 1996, roughly where we otherwise would have been had we not had a variable rate, and in either case, we would have complied with the Section 7(c) rate directives.

Now, there was another question that came up that I think you asked, Mr. Chairman, about the wholesale power rate design study, and I think there was a \$300 million number that you referred to, and that is—with the earlier witnesses. That is a different issue and a different number.

Mr. DEFAZIO. Well, tell us—

Mr. POLLOCK. In the course of developing the rates—it is actually in the course of developing the public agency rates, we stack up the resources that we have in our system, and we put the DSIs in the stack, in this particular rate design step, after we put the public agencies. And what you were seeing in that wholesale power rate design study is in effect a what if?

What if the DSIs had been stacked after all of the public agency loads and had to pay the next higher resource cost in the stack, how different would it have been?

Now, what we actually do in the rate design is we set the public agency rate and then reiterate through the process several times to get to the result Congress told us to get to in 7(c). So the whole-

sale power rate design number is really an irrelevant number to the questions you were asking the earlier panel about whether we have made money or lost money.

Mr. DEFAZIO. Well, after the term of the initial contracts, which were required by the act, isn't what you just described the future condition required by the act; that is, didn't the act anticipate that they would be served by BPA and would require resources or other resources, other than Federal base system resources would serve their load? Wasn't that what the act says?

Mr. POLLOCK. Not exactly, no, sir. The way I would characterize what the Act said about the DSI rate was between 1980 and 1985, it was set to recover the net costs of the residential exchange. From 1985 on, irrespective of the term of any contract, the 7(c) rate directives apply. They are not tied to the duration of the contracts. So whatever new contract we write, if we write one with the DSIs, would have to also comply—

Mr. DEFAZIO. So there is an inherent contradiction in the act where you have the 7(c)(2) rate process, and on the other hand, you have got the language pertaining to what resources would serve them and the future.

Mr. POLLOCK. There certainly are two parts you can interpret differently, but we think the 7(c) rate directives are pretty clear about how we set the—

Mr. DEFAZIO. I mean, you know, clearly the act says, Federal-based system goes to preference customers; right?

Mr. POLLOCK. With respect to supply.

Mr. DEFAZIO. Right. And we have been very careful in drafting, or you have, this business plan to say this is not an allocation of resources, but merely a way of pricing power.

Mr. POLLOCK. Yes, sir.

Mr. DEFAZIO. Yet, when you put the aluminum companies or the DSIs altogether, including the aluminum companies, into tier 1, we are essentially allocating then part of the Federal base system.

Mr. POLLOCK. Mr. Chairman, that is the way some of the customers have viewed it, and if I were—if I could, maybe take a minute to summarize the principal comments and concerns we have heard so far about—

Mr. DEFAZIO. Sure, go ahead.

Mr. POLLOCK [continuing]. How we are doing this tier 1 and how we are implementing the rate directives?

Mr. DEFAZIO. All right. If you can do that in a minute, it will be a miracle.

Mr. POLLOCK. I will try. Issue number one is did we pick the right amount of DSI power to allocate tier 1 and tier 2, and some have said, and expressed concerns that 85 percent of the historic load is too high, and that is a question we have gotten a lot of comment on and we will take a look at.

The second question we have heard is why should there be an allocation of tier 1 in perpetuity to the DSIs, because the public agencies will grow. And when the public agencies grow, they will be disadvantaged, not with respect necessarily to the supply of power, but with respect to the price. That is a substantial issue, we are going to take another look at that.

Issue number three has to do with the sizing of tier 1 vis-a-vis public agencies and the residential exchange and how we treat the formation of new publics. So as we have—we put a proposal out in the business plan, and we are getting a lot of comment on it, and those three issues are really where the most comment is coming and we have committed to take another look at each one of those, and we will do that in the next two months.

Mr. ROBERTSON. I should add, Mr. Chairman, I think I heard you indicate that you had an interest in the potential of us assessing the continuation of some variant of the variable rate in through of a tier 1 allocation. If I understood you correctly, that is another one we will be looking at.

Mr. DEFAZIO. I wouldn't discount that as a possibility. I mean I am willing to admit it is a totally unique load and maybe it needs to be treated uniquely rather than melded over into this tier 1 with everybody else, because I think that is creating not only concern with the preference customers, but it also makes the whole thing at this point at least in terms of the analysis that has been provided an imponderable in terms of where the rate shifts are occurring and who is paying, and treating them with a variable rate might be preferable.

Mr. Pollock, on the point of the new publics, boy, I don't know. I mean, I am not a lawyer, but I don't know how preference, as I read it in the act, would allow us to have two categories of preference customers. You know, those that were and those that will be, who have different entitlements. It seems that probably the law would require that all preference customers be treated alike.

Mr. POLLOCK. I think that is what we attempted to do. So I agree with you conceptually. What we sought to do in the Business Plan, and some would argue we didn't achieve it, was to treat all preference customers on an equal footing, and what that meant is, when a new preference customer were formed, that there would be a reallocation of the amount of tier 1 power entitlement from a rate perspective to accommodate that new customer, which meant it would come out of the hides of existing customers, unless something were freed up somewhere. And that is where the DSI issue begins—

Mr. DEFAZIO. Right. It raises two issues: the DSI issue, but also the exclusion of industrial load; that is, the new preference rate would only pertain to residential and farm load if it was formed out of an exchange utility. I mean, I have talked to some of the exchange utilities, and of course they think that is great, because it removes any threat of public formation out of their service territory.

On the other hand, the Federal law wasn't set up that way, and I think they have other arguments to make, and/or they certainly can defend themselves against such utilities, and have. So I am questioning why that exclusion is in there, why, you know, if I pick up a service territory that I have got to draw lines that exclude all of the industrial load, or if I take the industrial load, I am going to have to tell them, by the way, if we include you in our new public service territory, your rates are going to go up.

Mr. POLLOCK. Mr. Chairman, I can tell you why we did it, but we are getting a lot of opinions about whether we did it right. The

objective that we stated in the business plan was that tiered rates not significantly alter the incentives that currently exist for the formation of new preference customers. So we wanted to hold things constant.

Mr. DEFAZIO. But you wouldn't—here I have to disagree with you, maybe in your expanded remarks. I would say you are dramatically altering it, because today if I form a preference utility, I get a preference rate for my industrial, my farm and my residential. If I form it out of an exchange utility or anything else, and you are saying you want to keep the playing field level; I don't see that at all. I mean, you got some other bizarre stuff we are proposing over here with the cap and all that. I suppose you are trying to pay it off over here somehow. But I think we are creating an equity over here and you are not creating a level playing field in order to balance off some of the other things you are doing with the exchange. I don't know.

Mr. POLLOCK. I think, Mr. Chairman, the only difference is that tier 1 allocation collectively, for all the publics, would go down, and some have argued that is different than it exists today, because the same situation would—there wouldn't be any change in the new preference agency formed today than there would under this tiered rates proposal. I think that is an issue we are taking under advisement and we haven't concluded. So, I think you are raising a legitimate question.

With regard to the exchange loads, I just want to comment a little more on that. The reason we said that if a new public agency forms out of an investor and a utility service territory, only the residential and rural loads would be eligible, because we were trying not to alter the competitive balance that exists today for the incentive for public agencies to form out of IOU service territories. We have also gotten a lot of comments on that issue.

Mr. DEFAZIO. Right. Well, I am sure you will also have some lead on that. I believe it is probably illegal, I mean whether or not you could make a case for being desirable, I believe it is probably not legal to have two categories of preference customers. But in any case, we will see as you further develop that.

On the exchange, I mean, the current exchange program, and this came up in one of our earlier hearings, would seem in some ways to discourage efficiency. That is, an exchanging utility, you know, if they were to become extraordinarily efficient or more efficient than they have been, they can drop off the exchange roster, essentially. They go below the line there for the exchange. This would seem to me to be perverse; that is, those who perform better or more efficiently don't get the exchange, and those who perform less well do get the exchange. How would you be addressing this issue? Do you think that is an issue, and if it is an issue, how are you addressing it? I got to tell you, I have read your new exchange proposal and I don't understand it.

Mr. ROBERTSON. Well, let me make a couple of points about the nature of the exchange. If it is perverse, it is perverse both ways. That is to say, if we are successful in securing our flat rates, we are going to have to pay more in terms of exchange costs unless we come up with some kind of mutually agreed upon flattening of the exchange cost. If we have more than \$1 billion in exchange

benefits that have been put through throughout the region, mostly in the State of Oregon, as a result of the act, so it is a fundamentally important aspect of essentially guaranteeing rights for farm and rural, and homeowners.

I will say this, that you are right, if a utility becomes more efficient, they don't get as much of an exchange benefit from Bonneville for their homeowners and small farms; they still get a benefit for their industrial and commercial systems, which are not covered by the exchange according to the Act.

Walt, do you want to add anything to that?

Mr. POLLOCK. Just an additional point or two. The concern you have is a real one to us as well, Mr. Chairman, and we have some limited abilities to reflect a new competitive circumstances, and I will enumerate a couple.

First of all, there is a provision in our exchange contract that permits us, if we have a lower-cost supply of power than the supply we are receiving from the utility with whom we are exchanging, to buy that, instead of taking the exchange power. We have already given notice of that action and it is called an in lieu—

Mr. DEFAZIO. The delivery, essentially.

Mr. POLLOCK. Yes. The Utah Power portion of Pacific Corps, and now they have the choice of either matching the price or having us buy from an alternative lower cost supplier. We will consider doing that with other utilities where the costs of the power coming into our system is high and we think we can do better. But we have a seven-year notice provision in the existing contract that limits our ability to do that.

We also have a methodology that was extensively developed and litigated a few years ago that we think constrains the bounds within which we can work. But within those boundaries, we expect to exercise fully our contract rights and any other abilities we have to manage the net costs of the exchange. And we think that is appropriate.

Mr. DEFAZIO. Okay. On the issue of the negotiation of the contracts by the first of the year, one point was raised by Mr. Scott, actually, in his testimony of two precedents. What I am trying to get at here is whether or not that is a realistic time line and whether or not we need to be working a little harder on the backup plan as was raised by some of the other questioners. And Port Astoria, Oregon versus Hodel, and Forelaws on Board versus Johnson. In both cases, apparently an EIS was required on new contracts. How are you going to address that and get these contracts done by the beginning of the year?

Mr. POLLOCK. Two parts to that. One is how are we going to get the contracts done, and I think second is—

Mr. DEFAZIO. Well, that is a different issue altogether, accompanied by an EIS analysis of the contracts which can't be done until the contracts are basically formulated.

Mr. POLLOCK. The EIS can be done before the contract details are formulated, and that is what we are attempting to do.

Mr. DEFAZIO. Well, but if it is like the EIS that was done on the business plan, it won't pass a laugh test. I can't start asking questions, having read the thing, and have the administrator, after five or six points, admit to me, well, in fact, those are all very good

points and those are all tremendous inconsistencies and problems and, in fact, it is because it is a useless document. An EIS has to have some reference to reality and actual real-world impacts, and that one apparently did not.

Now, you are telling me it was developed last October, although it was given to me four weeks ago. I guess maybe I could have had a draft of it in November and spent my Christmas vacation reading it, and it would have had the same numbers in it. That is kind of disappointing to me.

I don't know why it didn't change, and why should—if you published it, you didn't publish it with a disclaimer saying that this is a useless document, don't bother reading it, the numbers are out of date and it is totally useless. So my question is, you can't do that with the contracts of these legal precedents. You can't just throw out an EIS that is meaningless, that has no meaningful analysis of what is going to happen in the region without—

Mr. POLLOCK. I think we differ on that point, Mr. Chairman.

Mr. DEFAZIO. So you can do one that is meaningless?

Mr. POLLOCK. No. The analysis and the EIS is an excellent environmental impact statement and we stand by it, and I think what the Administrator told you was that the rate numbers shouldn't be relied on in this EIS with precision. Because what the EIS is about is assessing the environmental impacts of alternatives.

Mr. DEFAZIO. Well, you can't assess the environmental impacts, if you don't know the disparate impacts on your customer groups and which ones might then be provoked into going out and buying thermal resources or which ones might be provoked into inducing more conservation, or this or that, and if we don't know the distribution among the customer classes, we can't even estimate those things, or if we do estimate them, it is not very useful.

Mr. POLLOCK. I think we do know from the EIS what the relative impacts are.

Okay. Then who is going to pay the additional bill, since no one else can answer that question, we are going to raise 10 to 15 percent additional revenues next year under your proposed tier grade proposal. Tell me who is paying the additional 10 to 15 percent.

Mr. ROBERTSON. Let me make a couple of points on that. First of all, the EIS's numbers that were a part of the EIS as we are showing on that chart, did have a range in them that we thought was relevant about a year ago. And the range expanded based on the new numbers we knew we would be getting in as the analysis began to get more and more sophisticated. And we are simply at a stage now where our analysis—

Mr. DEFAZIO. No offense, Jack, but how are you going to be a real time competitor if in analyzing rate impacts you are a year out of date? If we are going to compete, I would assume that, you know, we have to do a little better than saying, well, we published this and it is a year out of date.

Mr. ROBERTSON. I get your point. It is an important point about the movement of a rapid, competitive marketplace and how Bonneville's rates are going to interact with it, and you have got a good point about how relevant EIS information is going to be at any given stage. We are getting to the point now, though, as we designed ourselves into this process, that we are getting to more rel-

evant information and the analysis is becoming far more sophisticated.

The interactive models are beginning to work in terms of how they interact with load formation. And they just weren't part of the original EIS, and as the EIS goes along with this, it will begin to get more sophisticated as well.

The idea is that these things track together as we begin to make the decision-making point and as we enter into this expanded discussion process, that we have discussed earlier on with you, Mr. Chairman. I think that you will find that information will come out by the end of the month that will be helpful in this study and we will also begin to make clear how these interrelationships work.

Now, you asked about who is going to pay the bill, who is going to pay the revenues associated with this, and who is getting the rate increase. I think that is what your bottom line was. I want to make a couple of points, because Walt can best answer that.

A tremendous percentage, a significant percentage of this rate stability that you see us having, going through the next rate case and the avoidance of the 10 to 15 percent rate increase, comes from deeper cost cuts, which would effect—

Mr. DEFAZIO. Okay. Now, would you detail which deeper cost cuts and how much they are, that you can't make under the current system?

Mr. ROBERTSON. The current system, we think—

Mr. DEFAZIO. Because there were some assumptions there, it seemed to me, you were going to achieve under, no matter what, because you assume the status quo, you are not reducing personnel.

Mr. ROBERTSON. Let me direct you to the chart, because you indicated earlier that the top line was a worst case. It is not a worst case top line. There are lots worse scenarios than that.

We think that is a reasonable line, based on some load loss expectations that I think Walt can describe better than I. We start from a point where those charts begin to demarcate. We start from a point basically after we have cut \$200 million in our program levels already; those were the cuts associated with post-rate case discussions last year.

So we started through our review, function-by-function review, and we found \$200 million in cuts. Fundamentally, from that point forward, based on getting down to the bottom line, we are going to need to cut or change about \$297 million per year in terms of helping in addition to Walt's new revenues that he is going to describe in a second. The combination of those things gets us hopefully to the goal of flat rates.

Mr. DEFAZIO. Let's focus on reductions for a moment.

The 297 per year, okay, if we had to do an interim rate case, what percentage of that 297 can you capture? These are now not new revenues, these are cost reductions?

Mr. ROBERTSON. We can give you more specific information on this. We would begin to go for cost reductions in the \$50 to \$100 million range. We would look at the percentage of our Treasury repayment and see whether or not we could afford to reduce that, which we don't like to do, because that tends to leverage the repayment reform issue back on to the Northwest delegation.

Mr. DEFAZIO. So you are saying somewhere in there, there is between \$247 and \$197 million of cuts that somehow you can't make without tiered rates and those things?

Mr. ROBERTSON. There are some that we can make on the top line, and they are not significantly shown in that line, but I cannot get down to the flat-rate line with the cuts without the addition of the other revenues.

Mr. DEFAZIO. I need to know what those things are, Jack. What are those things that—conservation is one of them. How much? How much of the 247 to 197 million is conservation?

Mr. ROBERTSON. Okay. Walt that is details.

Mr. POLLOCK. I was going to suggest, Mr. Chairman, we can give you that for the record. Conservation is one. There are a whole series of things.

Mr. DEFAZIO. Well, if you could give me just a few of them, you know, penciled on the back of a napkin here. I am just curious. I mean, I am—you know, I just want to know what the worst case here is. I mean, if we have to go into an interim rate case, what cuts can't you make and maybe are there ways that we could deal with that? So I need to know what they are.

Mr. POLLOCK. We can give you that, Mr. Chairman. I don't have it on the tip of my tongue.

[The information follows:]

Average 1996–2002 cost reductions associated with BPA's conservation reinvention are roughly \$84 million, relative to BPA's 1993 Rate Case. Of this amount approximately \$34 million is expensed dollars and \$50 million is debt service associated with foregone capital borrowing.

Mr. POLLOCK. The reason is we are doing this a dollar at a time, and there are probably two dozen areas where we are attempting either to get new revenues or to reposition products to get revenues that were not being paid for or to cut costs. And you really have to go down them one by one and judge the feasibility.

Let me give you a few examples.

Mr. DEFAZIO. I am trying to divide cost from revenue. Let's deal with cost first, because that is the one that is more puzzling to me, and then we'll deal with revenues. Deal with cost first.

Mr. POLLOCK. Well, in the cost area, we are proposing very deep cuts in all BPA programs, and that is not only transmission services, as you pointed out; we think that by reinventing conservation, we can reduce the cost of those programs in 1996, 1997. We think by reinventing fish and wildlife, we can reduce what otherwise might be the costs of those programs.

You can ask the question: Could we reinvent those programs without all of this? And the difficulty is, this is webbed together in a way that maybe none of us like all that much, but every particular party with an interest here wants to know what is happening on the other side of the equation. You want to know what we are going to do with the irrigation discount, for example. And others do as well.

Mr. DEFAZIO. That is just one of many questions I have, sure. Summer rates, special summer rate, I guess if you want to irrigate in the winter, you are going to have to pay a higher rate, but I don't know of anybody that does that. So it sounds like you are going to have to continue the discount.

Mr. POLLOCK. But when people are asked to take a cut in one area, they immediately look in another area and say why are you still spending money there; or why aren't you doing what you need to be doing there? Every constituent of Bonneville asks that, every employee of BPA asks that. So while we can give you that information, it is very difficult to engage in a very meaningful discussion of, well, let's just do part of this.

Now, I think I can give you some instructive information on what the parts are and how likely we will be able to attain them. For example, you really can't reinvent conservation and achieve the cost reductions without tiered rates. You need the tiered rates to reinvent conservation. So that is why I am suggesting these things are hooked together in a way that needs to be fully appreciated.

Mr. DEFAZIO. Well, I understand some of those things are hinged together. On the other hand, it would be useful to have, these are what we expect in terms of cost savings, so we can assess what of those could be gained in that way, or alternate ways if we come to worst case.

I worry, particularly having heard the Public Power Council testimony and others saying: We want to see, you know, all the major issues of these contracts resolved before we move ahead on January 1st with the rate case. And I am just saying I have some doubts about whether that rather ambitious schedule can be met.

I mean, again, I am sort of prejudiced by looking at little things like what happened to EPUD for three years on a conservation power plant contract. But maybe you can renegotiate every contract with every major user in three-and-a-half months, maybe the agency has changed that much. Maybe everybody has been spending their summer vacation and they are all there working on it today. I don't know. I am very doubtful.

Do you think that the EIS that was provided for the business plan is adequate for new contracts? It doesn't mention contract issues.

Mr. POLLOCK. Yes, it does, Mr. Chairman.

Let me respond maybe for a minute to what I view to be the adequacy of the EIS question.

This is an EIS that examines seven alternatives, including not only the two you focused us on a minute ago, but another five that go over a much broader range. Our responsibility when we take an action is to have an EIS that competently annualizes the environmental consequences of the action.

So the question is, when we finish these contracts from a principled standpoint and the major issues in December, will the EIS have contemplated the outcome and adequately considered the environmental consequences? I think the answer to that is yes, but we won't know until we get there. Because we knew it when we went into this EIS, and that is why we scoped it so broadly, to examine alternatives not only including these two, but much more extreme in both directions. So I think we will have an adequate EIS, but it is our responsibility to determine that when we get to December. And if we don't, we will have to supplement it.

Mr. DEFAZIO. Well, I mean, you know, I sort of suffer from having read through it before the Administrator told me I shouldn't

bother. And you know, I guess maybe I am—where are the alternatives on, say, the DSI contracts discussed in the EIS?

Mr. POLLOCK. Under at least one alternative in the EIS, there are major losses of DSI loads and that could be driven by an unfavorable contract.

Mr. DEFAZIO. Yes, but that doesn't exactly seem to me to go to some of the issues we talked about here, continuing the variable rate, not continuing the variable rate, bidding out VORs, those sorts of things and what impacts that might have. Those haven't been anticipated.

Mr. POLLOCK. But the key question for the EIS is whether the environmental impacts of the result have been analyzed. So if we have an alternative that contemplates a major loss of DSI load in this EIS, which we do, then the question is, did that anticipate the outcome, whether we get there through unfavorable contracts or higher rates? So that is the test that an EIS has to measure up to, not did you get the proposed action exactly right when you put out the draft.

Mr. DEFAZIO. What—I am learning about EISs. What water assumptions? Do we make the same exact water assumptions under the status quo and/or interim rate as we do under the tiered-rate proposal?

I just want to make sure we are using constants here, underlying this. Are we using the same assumption regarding the water conditions under both of those proposals? Are the water conditions assumed—are they underlining this all the same?

Just sort of in reading this, I got an idea that we are sort of prejudicing when we leave out administrative savings out of the status quo. I think, well, gee, that means we are kind of prejudicing things toward this tiered-rate alternative, because I don't see why we couldn't get the administrative savings in either one.

So I am wondering if there are other assumptions that might be prejudicing these things. Could you tell me? Are there any other major varying assumptions, particularly the most major one which has to do with what are the flows going to be on the system?

Mr. POLLOCK. I don't think that there is—there are differing assumptions about how we operate the system. But I don't think there are any different assumptions about the statistical probability of water years.

Mr. DEFAZIO. Okay. I just want to know, you know.

Mr. POLLOCK. I know, Mr. Chairman, you have obviously gone through this in some detail, but there actually is about a 6-page table in the middle of the EIS that describes in detail the alternatives by issue. That is, what have we assumed about each issue or each of the various alternatives, and it runs for about—starts on page 2-17 and runs through 2-26. So there is a lot of detail in here that I think will answer most of those questions.

Mr. DEFAZIO. Went through that. I don't know. I guess I just had a different idea about an EIS. I thought an EIS had to do with pretty specific Federal actions in a real world best case, I mean, best analysis applied to that. And you are telling me that if we had to stumble upon covering the loss of DSI load in one of the alternatives, whether it is intentional or not intentional, no matter

what gets us to that, we don't need to analyze the different things that lead us to that, just what the ultimate result was.

Mr. POLLOCK. I guess the way I would characterize it, at least my view of NEPA, Mr. Chairman, is it requires us, as a Federal agency, to be informed of the environmental consequences of the action that we are about to take. That is the most fundamental role that an EIS provides, and that is the test that it has to meet, that it has to have competent environmental information for us about the action that we take, and we tried to put a broad enough range of alternatives in so we would have that information.

Mr. ROBERTSON. I would like to say another point that I think gets to the issue you raised, Mr. Chairman, and also I believe Mr. Duncan raised this morning about this issue of whether our analysis prebiases, or seems to prebias us toward a certain outcome. We have tried to be as straightforward as we can about this, and we have gone through a fairly—a very open public process, and we are now going to go through a longer one to make sure that if there are any biases that are seen here, we certainly hear about that from both our customers, the interest groups and the congressional committees giving us oversight.

Biases in this would fundamentally undercut our ability to deliver what we think is important. If they are there, we need to find them. It is possible there are—it certainly wouldn't be our intent as an organization. We are trying to do the best we can to reflect a reasonable set in a competitive world that is unfolding in front of us.

Mr. DEFAZIO. What about this issue of transmission which the last panel sort of deferred the question? Your communication with FERC regarding terms and conditions versus costs? Where are we at on that?

I mean, where does that fit into this whole puzzle? I mean, you know, there are sort of varying analyses of how transmission is either going to be applied to cause you to be threatened by competition; we have heard analyses of where, you know, transmission and unbundling is going to be used to increase revenues.

I have had other conversations where it is going to be used to basically to in a way help, you know, stave off competition, because of the unbundled services of people and the pricing category to be put in place. I mean, where does your interpretation of what is required in your little provision in the misbegotten Energy Act of 1992 put you on transmission and how does that pertain to this puzzle?

Mr. POLLOCK. Well, first, most generally, we view the transmission business as something we are good at; we do well and we want to provide more transmission in the future, not less. And we believe that the industry is moving towards open access transmission, Bonneville has been in the leadership role in that approach, and we intend to stay there.

We do not want the availability of our transmission to be an impediment of the fully functional power market, nor do we want it to be a leverage point to force customers to buy from us, and we have told our customers that and I expect that policy to be carried forward.

That means that if a customer wants to buy from an independent power producer or buy additional power from BPA, we will treat the request for transmission from a new provider, the same as we would as if we were competing for the load ourselves. So that is first and foremost principle here. We want to provide transmission; we will treat ourselves with regard to competing for new loads like we treat others. Now, there may be instances when transmission is not available to us or anybody else and we will do something about that.

With regard to the Energy Policy Act, at least my interpretation of the Energy Policy Act and you are obviously probably more familiar with it than I am, was it put BPA on a roughly equivalent footing with other utilities in terms of transmission with a couple of exceptions.

Mr. POLLOCK. One, is it didn't change our transmission rate-making, that is the Section 7 provisions of the Regional Act and the FERC authorities and the judicial reviews. And second, it preserved regional preference to transmission. And those are the two fundamental differences with respect to Bonneville from any other utility.

We are subject to FERC jurisdiction if there is a matter that is to be adjudicated. One of the reasons we have joined the Westwide Regional Transmission Group is we are willing to engage in a voluntary utility organization to open up transmission access. So I have—I don't see that as a significant impediment to our customers' desires to have options here. I was a little puzzled by some of the discussion in the last panel.

Mr. ROBERTSON. Mr. Chairman, your question I think was more specific, because you have this dichotomy, how can we open up transmission in one case and then guarantee essentially we can help achieve the conservation, for example, objectives of utilities.

Mr. DEFAZIO. That is the question I had from the beginning.

Mr. ROBERTSON. And I guess Walt can fill in here, but my response is with the principle we have got in terms of achieving the conservation objectives and of reinvention. It is based on an accountability principle that we are going to invent, along with this subcommittee, that we are working with at the Council and others. The accountability principle is the mechanism that Bonneville will put in place to assure that the objectives of the 660 megawatts that we talked about earlier are there. Accountability can be achieved in various ways. Transmission might be one of those.

Other ways have been suggested—including a loss of tier 1 resources similar to that which wasn't achieved under the IRP. We are looking at a host of ways to do this, and I think perhaps what has happened is transmission may have been seen as the only way in which that accountability can be achieved. I think there is a package of possibilities there that we are going to work with the region on.

Mr. DEFAZIO. You mentioned something about getting WPPSS staffing to more appropriate levels. I had this exchange with Mr. Council, I think you were here, where I have access to only three studies, and those three studies find that they are overstaffed. And he just says adamantly he is not going to reduce his operating staffing until a couple years from now, no matter what. I mean, is

BPA so sanguine about the staffing levels? He also claims that he is basically a low-cost provider here and we shouldn't be concerned about it anyway.

Mr. ROBERTSON. I have had a number of conversations with Mr. Council directly on our needs to assure that in these fundamental cost areas that we have to get control. We work with the Corps, the Bureau, the supply system, the Power Council and others to try to assure that they are delivering higher and higher productivity as time goes on.

For us, that means fundamentally that we would like them to try to eat 3 to 4 to 5 percent of inflation per year. The objective is—Mr. Council's point is he is worried about the NRC license and the issue of safety. Obviously, we are all worried about safety first in the nuclear plant.

The fundamental issue here is progress can be made. We have encouraged him to work on that. Our mechanism for achieving progress with the Supply System is the net billing contracts, which does give Bonneville a total ability to not agree to a budget in total submitted by the Supply System. But, it is not a very elegant management tool. And so we are in this position of having a thing that was written 20 years ago that is a comprehensive review of the budget, but it is not a line-by-line item review. So we have to work with them and these other parties in a partnership way to try to get to these objectives. In my view, and I think Mr. Council would agree, everybody with large organizations can make productivity improvements. The question is how, when, and how fast can we do it.

Mr. DEFAZIO. Well, you know, the President is confronted with that situation often. Congress sends him a bill, he might not like parts of it, particularly an appropriations bill, and he has a right to veto it. Sometimes you got to use a veto. Particularly if someone hasn't been paying any attention to you for two decades, and they tell us we won't even think about that for another two years and is sanguine about those costs.

I mean, 3,400 people, you know, that is—you know, I mean, when we are talking about these kind of margins, you are talking about rate increases, I would assume that adds up to, you know, maybe a percent, I don't know, maybe a little more.

Mr. ROBERTSON. It is all very significant money, particularly when we feel like every dollar at this point is very important to our maintenance of stable rates. So I agree with you, that is an important factor. And we need to get as efficient as we can.

I will tell you that the contract mechanism, if we say no to a budget, goes to what is called "prudent utility practice." This means basically we have to go to a third party to determine whether we were right or the Supply System was right in terms of our decision.

Mr. DEFAZIO. Well, I am going to assume since you are so much above the average that you are not going to get, if it is an arbitration, an arbitration that requires them to hire more. So maybe we want to roll the dice. I don't know. But I mean, he has taken a very, very hard line here. I know he is paid twice as much as the Administrator, so he is twice as good, I guess. But I am disturbed at that recalcitrance.

Mr. ROBERTSON. I hear you.

Mr. DEFAZIO. And that is a concern I raised with Mr. Jura for a number of years, and I raised it with Mr. Hardy, and I just really think that, you know, you would find more backing out there than perhaps you anticipate for finally getting tough with, you know, the supply system, so-called.

A little bit of discussion, conservation. You know, I am not—again, when we talk about the transmission and how we are going to—you know, I mean, I raised that question before, both in terms of tier 2 and in terms of driving people to conservation, which is, you know, okay, I get this much in my tier 1, now I am either going to buy tier 2 or I am supposed to be inducing conservation.

I mean, first off, there are the equity issues of people who made a tremendous amount of conservation investment, whether it is funded by you or themselves or anybody else, have fewer immediate and easy gains to get. Other people have done nothing, and there are utilities that have done nothing, have some gains they can capture rather quickly. I mean, that is a concern.

But secondly, there is a concern about how we are really going to drive this thing, whether we are driving it through transmission and costs there or other agreements, or whether we are driving it through IRPs that have some sort of enforceability and penalty against the tier 1 allocation. I don't know. But I—at the moment, I have a doubt about triggering a great amount of conservation, particularly the high levels we have been getting, with just a market signal.

You know, there is a big market signal in this area, sort of like 9, 10 mills, I don't know what it is, I mean, there are very high electric rates in the Northeast, and they go up dramatically in the summertime to induce people not to use their air-conditioning so much. It doesn't do any good. So, you know, I am not quite so sanguine about getting the very desirable regional goal of cost avoidance and conservation and the environmental goals that come with that, just through market price signals. So what are we going to supplement it with?

Mr. ROBERTSON. I agree with you on that. I don't think you will find anybody at Bonneville saying that the market price signal alone will accomplish this level of conservation. I wouldn't agree to that, I don't believe it.

The market price signal is an important mechanism which can induce, we think, a much more innovative tiering program which borrows less money against our borrowing cap for the purposes of Federal borrowing: But also I think this also allows for a decentralization of the programs, a guarantee hopefully based on this accountability mechanism we are going to come up with of the 660 being achieved, before and after, and in the bargain creating, I think, more innovative programs, decentralized programs with less overhead, less central controls.

You talked about the overheads of Bonneville. We have overheads, like any other agency. And if we can minimize those overheads and accomplish the megawatts—

Mr. DEFAZIO. What was that figure?

Mr. ROBERTSON. We are trying to get the information on that. That might be a combination. We are just—the answer is, I don't know, but we will provide it for the record.

Mr. DEFAZIO. Okay. We would like that for the record.

[The information follows:]

In FY 1992 BPA's administrative costs as a percent of Direct program expenditures were 16 percent. This figure declined to 15 percent in FY 1993. This number increases to 29 percent and 26 percent, respectively, if Corporate overheads and Indirect Program costs are included.

Mr. ROBERTSON. Yes, that is a big—but overheads, if you look at fish and wildlife programs and you ask what are the overheads of fish and wildlife agencies or other States, Federals, basically, they range between 70, in some cases, 30 to 70 percent. You have got an overhead problem throughout the delivery of our systems, it is very significant, that we all have to get to.

Bonneville has its overheads, but so does everybody else. So the more we can decentralize these programs and get more innovative out there in the field, I think the more megawatts that will be achieved.

Walt, you want to add anything to the tier effect we are going to have out there?

Mr. DEFAZIO. Let me add, it is a small proportion of it that you think comes through the market price signals.

Mr. ROBERTSON. Yes, it is a small portion, but then we add to that, we are continuing to fund market transformation which will be codes and the kind of things that we can do only on a regional basis. Then we are going to propose the energy service charge, and we convert what now looks like approximately \$200 million a year and pull down from our borrowing capital, which we go through in 1999. Now we convert it to a loan program that we think we have—we want to get authority to do what we think we can accomplish. That ironically, it is much easier to give money away in our authority than it is to loan money and get money back for it. But we think we can achieve that.

If we add that layer cake of objectives together with the tiered signal, and then get the innovation and decentralization going, we think it could be quite a powerful market change. And we think it might shape the conservation acquisition of the 21st Century and get it out of this more centralized control. Even if we continue to succeed on this, it is clear that we have a political issue coming up ahead of us with regard to the borrowing cap.

Mr. POLLOCK. Mr. Chairman, we don't need to go through it now, but we can submit for the record, we have a chart here that actually shows the components that Jack was just describing. And there is some numerical detail on page 57 in the business plan.

But we would be glad to just supply you this chart, that graphically shows it for the record.

[The information follows:]

BPA's current goal, based on the Council's Regional Plan, is to achieve 660 aMWs which includes all cost-effective conservation between 1992 and 2003.

The major sources of contributions to meet regional and BPA conservation targets are existing programs and other contractual obligations, utility-initiated programs, and BPA DSM products and services. Current projections are that lesser accomplishments will be made with market transformation and tiered rates. Table 2-3, BPA Conservation Goals and Accomplishments, on page 57 of the Draft Business

Plan give specific year-by-year specific accomplishments and projects. The components of the sources are described as follows:

Accomplishments. BPA has accomplished 79 aMWs from FY 1992–1993 programs and another 55 aMWs are projected to be achieved through codes and standards put into place since the target was established.

Existing Programs. BPA's current regionwide programs including Super Good Cents, Energy Smart Design, Energy Savings Plan, Waterwise, Weatherwise, Water Heating, Appliance Efficiency and Manufactured Home Acquisition Program will achieve 96 aMWs through FY 1995.

Additional special contracts BPA put into place over the past few years are expected to achieve 101 aMWs of savings. These include energy services company contracts, targeted acquisition programs, utility power plants and others. Most are expected to be completed by FY 1997.

Utility-initiated DSM. Many utilities indicate that they will run their own conservation programs in their service territories. The large generating utilities (Snohomish, Clark, Tacoma, and EWEB) are projected to acquire 100 aMWs of conservation beginning in FY 1996. Other utility segments are projected to achieve about 30 aMWs of conservation.

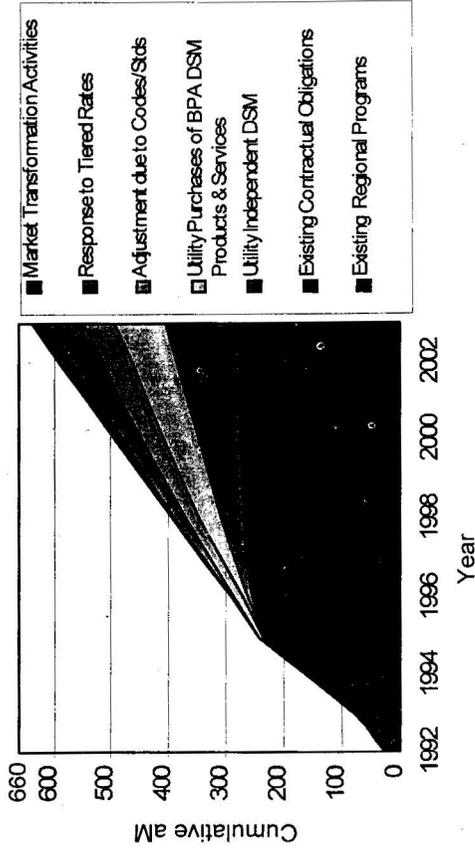
BPA DSM Products and Services: Energy service charge (ESc) results are projected to achieve conservation in mostly large industrial and commercial firms outside of the large generating utilities. In addition to the 50 aMWs projected for ESc, an initial set of products and services was analyzed as a proxy for the future business line with projected accomplishments of 37 aMWs.

Tiered Rates: The impact of tiered rates was assumed to result in 40 aMWs of conservation, based on the assumption that about 50 percent of end-use consumers see a retail tiered rate structure from their utilities as a result of BPA's wholesale tiered rates initiated in FY 1996. An additional 22 aMWs would be the result of end use consumers choosing an alternative fuel which would result in less conservation potential.

Market Transformation. Based on initial analysis BPA expects that at least 27 aMWs would result from market transformation efforts.

The calculations leave BPA 28 aMWs short of achieving the 660 goal, however, the numbers cited are intentionally conservative. BPA is confident that the proposed conservation reinvention is a viable approach to accomplish all cost-effective conservation for the region.

BPA CONSERVATION ACQUISITIONS 1992-2002



Mr. DEFAZIO. Okay. And then where are we at in terms of discussions with the customers about enforceable IRPs?

Mr. POLLOCK. We are right in the middle of that discussion. As you heard a little earlier, I think from Angus and some other witnesses, that we are working with the Council, with customers, with public interest groups, to try to figure out how to manage each component of this plan. If you go to the Senate report language or the way we have described it in the Business Plan, there is a component that has to do with planning, and the integrated resource planning.

We are working on that to figure out how we do it, what the standard is, who does it, how is it done. We are also looking on—at the independent performance review and there are two or three ideas about how to do that. And we are looking at the accountability mechanisms. And there are two or three ideas about how to do that. One of them is that—is the transmission idea. I have got some misgivings about that, frankly, that I have got to admit to you, but it is on the table for discussion. There is also the possibility of changing allocations of tier 1 or providing incentives or disincentives. I think all of those are in play right now in that discussion group.

Mr. DEFAZIO. Okay. Yes, the Senate report does reference a meaningful performance accountability mechanism incorporating penalties for poor performance and benefits for good performance. I mean, carrot-stick kind of thing.

Mr. POLLOCK. Yes, and we are being guided by that report in terms of what this approach needs to embrace.

Mr. DEFAZIO. Okay. I am—oh, all right. Going to ask you this. I will just read it. I am tired. I would like more detail on what specific measures BPA—most of my colleagues just do it this way anyway. I would like more detail on what specific measures BPA is considering taking in the event its conservation reinvention plans fail to deliver the expected savings.

How long do we wait before acting and what will BPA do to make up the difference?

Mr. ROBERTSON. Okay. We will give you that. You want the detail right now?

Mr. DEFAZIO. How long will it take?

Mr. ROBERTSON. As Walt indicated, we are in the middle of inventing how we account for this. As part of that we will also have to have some kind of a benchmark which will determine that we are on the path and we are making enough progress to achieve the 660 megawatt goal.

[The information follows:]

BPA has been working with utility customers, the Northwest Power Planning Council, states, and interest groups to further define the tiered rates and conservation reinvention proposals. Currently a plan has been devised which calls for customers to prepare local conservation plans that describe their approaches to developing all cost-effective conservation in their services territories.

BPA will monitor implementation of the plans according to regionally developed verification and evaluation standards and will remain responsible for mitigating any persistent shortfalls that may occur during implementation by customers. A performance accountability mechanism is currently being developed that incorporates penalties for poor performance and benefits for good performance with respect to conservation acquisition.

BPA's conservation reinvention is based on utilities making choices. BPA will no longer rely on centralized decision-making. Through tiered wholesale rates, utilities will see the right price signals so that informed choices will be made.

BPA fully expects that this approach will enable BPA to achieve our share of the region's conservation goal, but BPA is prepared to adjust our approach if necessary to ensure continuous regional conservation achievement at or above the Council's target.

The one thing I want to leave with you on this issue, because it is very important, is we are pledging to achieve the same amount of conservation with the reinvention that we would have achieved before. That is our obligation to you. We have to achieve that. And we will have to get back to you as we design the accountability mechanisms, I think.

Mr. DEFAZIO. Okay. And since I raised conservation, this is another thing from the beginning when I talked about designing tiered rates, and I would like you to think about this a bit, I have raised it with Mr. Hardy. And that is—and why there is a particular concern with Mr. Wolberton's study and/or your analysis internally, which I haven't seen, about the, you know, the costs of some of these things on growing public utilities. And that is, you know, growth, responsible growth is good. You know, we want to grow responsibly. I am an Oregonian, we have zoned our whole State so we can grow responsibly and not become Los Angeles. So my question is, how do we discriminate between types of growth? And wouldn't it be desirable to construct something to do that?

Someone who wants to grow sloppily and inefficiently, who hasn't taken conservation measures, who isn't pushing their customers on to gas, where gas is available and other things, how do we account for that as opposed to some areas that have taken extraordinarily rigorous measures, as Seattle or EWEB or someone else, to induce conservation and to grow—but inevitably to grow, because people are moving there and grow responsibly.

I mean, it seems to me, I know this is a difficult question, but I think it is something that needs to be addressed. And, you know, we shouldn't just say everybody is penalized because everybody has to buy their additional power out of the same tier 2 if they are growing responsibly or they are growing irresponsibly.

Mr. ROBERTSON. I want to make one point.

Mr. DEFAZIO. Or I should say growing in an energy efficient manner and growing in an energy inefficient manner, less judgmental.

Mr. ROBERTSON. The fundamental idea to get to the issue of tier 2 and the question of how this will be dealt with, the fundamental idea of having an accountability mechanism in the question of the conservation acquisitions and the targets that might be established, is fundamentally a mechanism which can be described as making sure that people who grow efficiently, get rewarded, and those who choose to do something else, don't. So I think we are trying to precisely—

Mr. DEFAZIO. So it doesn't assume—the problem is I look at a lot of this and since we are cutting off the tier at a certain point in time, I am assuming here is my load, I have chosen one year out of these five years that I am allowed to choose, probably for growing utilities the most recent year, having to do with weather conditions, whatever they find is to their advantage, but as soon as

I exceed whatever kilowatt, megawatt over that, I am paying in tier 2, I am saying that it shouldn't just be—I understand what you are saying, I applaud that, but I am saying you also should maybe look at whether this is a static allocation or determination.

Mr. ROBERTSON. Okay, yes, I hear you, but I think the fundamentals here we are after are to do what you are suggesting. I don't think we can achieve the 660 without a viable accountability mechanism, in any event. I want to make one other quick point about fast-growing publics and those who have contributed to energy growth in the last—or energy efficiency in the last decade and a half.

We are extremely proud of the energy conservation program of the last decade. We had to begin a program from nothing as a region. The Council put together a plan, we worked it out over a complex decade, and we spent over a billion dollars largely in the fast-growing public areas, but also in the industrial sector, to create a mainline program that has become a benchmark for the industry, not just in this country but elsewhere.

What we are trying to do with this reinvention is simply take what worked best with that program and apply new standards to make it more responsive to markets for the 21st Century. For the fast-growing publics, a lot of that was financed I think, and willingly financed, by Bonneville through the Council's program, and we are proud of the results of that.

Mr. DEFAZIO. Okay. Well, I want to thank the last witnesses representing BPA and certainly all the other witnesses who testified. I mean, to me, perhaps we are moving in a direction that will raise my level of confidence and others. We need an analysis of the range of the issues and the contracts, the impacts of tiered rates.

I think it needs to be done in a very open and public way so that we can discuss the relative merits. And, you know, that we understand where costs are being shifted, where to, where from, and what it means to us as a region in the future. I guess at this point, I would have to agree with the Public Power Council testimony, which was: Don't go forward if we don't know what we are going forward with and we don't have it right.

We got one thing horribly wrong, which was WPPSS and notices of insufficiency, and that was given to us by the last generation, and our generation is going to pay for it until the day we die. I want to be sure that our generation doesn't stick the next generation with another series of mistakes that may have been adopted in a very well-intentioned manner under a false sense of urgency.

I think an extraordinarily well-thought-out, balanced, and fair plan that doesn't go into effect for 18 months or 24 months or whatever is going to be better than one that is rushed through because of the exigencies or the perceived exigencies of competition and the market. This is not the last hearing we will have on this, I am sure, and we will have more opportunities for further discussion and I hope to do the next hearing out in the region so we can get a little bit more public involvement.

So again, I thank you, I think all the testimony was good, and look forward to continuing the discussion.

The committee is adjourned.

[Whereupon, at 3:02 p.m., the subcommittee was adjourned.]

APPENDIX

AUGUST 9, 1994

ADDITIONAL MATERIAL SUBMITTED FOR THE HEARING RECORD



WASHINGTON PUBLIC POWER SUPPLY SYSTEM

P.O. Box 968 • 3000 George Washington Way • Richland, Washington 99352-0968 • (509) 372-5000

June 9, 1994

RECEIVED

JUN 15 1994

The Honorable Peter DeFazio
U.S. House of Representatives
1233 Longworth House Office Bldg.
Washington, D.C. 20515

WASHINGTON, DC 20515

Dear Representative DeFazio:

Subject: **CONGRESSIONAL TASK FORCE REPORT ON
BONNEVILLE POWER ADMINISTRATION**

A Congressional task force headed by Oregon Representative Peter DeFazio recently released a report on the Bonneville Power Administration's (BPA) operations and finances. The report addresses BPA business practices and includes recommendations for cost-cutting measures.

The Supply System is mentioned in several places throughout the report, with references to costs associated with Plant 2 operations, preservation of WNP-1 and -3, and our proposal to use Plant 2 and WNP-1 to dispose of the nation's stockpiled weapons-grade plutonium. Comments in respect to these projects are particularly focused on ways the BPA could reduce spending.

While some of the task force's recommendations have merit and may warrant consideration, others would interfere with the Supply System's ability to continue safe, reliable and cost-effective operation of Plant 2. Additionally, several statements in the report are inaccurate. For example, the report states that Plant 2 costs are "far higher than the nuclear industry average for similar plants." In reality, Plant 2 costs for the last several years have either been below or very close to the average for nuclear plants of its type operating in the U.S. today.

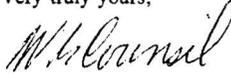
I take particular exception to the "wasteful spending" reference to the Supply System. For the last two years, Supply System budgets have remained level and been approved by both the Supply System Executive Board and BPA. All Supply System expenses are substantiated by a well justified need to sustain safe, reliable and cost-efficient operations.

Where we are in agreement is that trimming Supply System costs where appropriate remains a top priority for Supply System management. We have tasked ourselves with a three-year get-well program to improve Plant 2 operating performance and the general way we do business. Without increasing budgets as other plants have had to do, we have made good progress so far in improving Plant 2 performance and will continue until we become one of the nation's top nuclear power plants. Coinciding with this effort, we're working to identify ways we can become more efficient and then incorporate these methods and processes into our routine work practices.

The Honorable Peter DeFazio
Page 2
June 9, 1994
CONGRESSIONAL TASK FORCE REPORT

I'm convinced that through continued performance improvements, the Supply System will earn more positive comments in such future reports.

Very truly yours,

A handwritten signature in cursive script, appearing to read "W. G. Council".

W. G. Council
Managing Director

WGC:SJS:pp

cc: Supply System Executive Board
Supply System Board of Directors

U.S. House of Representatives
Committee on
Natural Resources
Washington, DC 20515-6201

September 8, 1994

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 THOMAS J. BARLOW III, KENTUCKY
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 RICHARD H. BAKER, LOUISIANA
 KEN CALVERT, CALIFORNIA
 SCOTT MENNIS, COLORADO
 RICHARD W. POMBO, CALIFORNIA
 JAY DICKEY, ARKANSAS

JOHN LAWRENCE
 STAFF DIRECTOR
 STANLEY SCOVILLE
 GENERAL COUNSEL
 DANIEL VAL RISH
 REPUBLICAN STAFF DIRECTOR

Mr. William G. Council
 Managing Director
 Washington Public Power Supply System
 P.O. Box 968
 3000 George Washington Way
 Richland, Washington 99352-0968

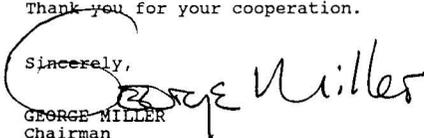
Dear Mr. Council:

Thank you for your letter of June 9, 1994, regarding the Committee on Natural Resources May 1994 Majority Staff Report entitled "BPA at a Crossroads" and the testimony you delivered before the Subcommittee on Oversight and Investigations regarding the Report on August 9, 1994. Your letter asserts that portions of the Report regarding wasteful spending by the Supply System are inaccurate but does not include specific data in support of these assertions.

In order to assess the basis of the assertions you have made regarding the accuracy of the Report I request that you respond to the attached questions. I would appreciate receiving responses to these questions no later than October 3, 1994. Please provide a copy of your response to Representative Peter DeFazio, who, as you know, chaired the Task Force responsible for the BPA Report and the August 9, 1994, Subcommittee hearing.

Thank you for your cooperation.

Sincerely,


 GEORGE MILLER
 Chairman
 Subcommittee on Oversight and Investigations

cc: The Honorable Bob Smith, Ranking Member,
 Subcommittee on Oversight and Investigations

The Honorable Peter DeFazio, Member,
 Subcommittee on Oversight and Investigations

Questions for the Washington Public Power Supply System

**Follow-up to Oversight Hearing on the Bonneville Power
Administration**

**House Committee on Natural Resources
Subcommittee on Oversight and Investigations**

August 9, 1994

WNP-2 Staff Levels

1. The following table shows nuclear plant staffing according to the latest industry survey by the Institute of Nuclear Power Operations. As the table indicates, on-site staff (minus security) averages 783 for a plant the size of WNP-2; that is about 200 fewer than reported at WNP-2 by the Washington Public Power Supply System in its own response to the INPO survey. The INPO survey's total for off-site staff averages 322 for the 46 U.S. nuclear utilities, while the Supply System's survey response reported 432, even though most other nuclear utilities operate more than a single unit. What is the Supply System's analysis of these statistics? Are they a legitimate indicator that WNP-2 on- and off-site staffing is higher than the industry average?

Average Nuclear Plant Staffing (permanent positions)					
	Total U.S.	Per 1,100 MW	Per utility (46)	Per plant (69)	WNP-2 INPO response
On-site staff minus security	72,487	783			989
Security	8,621			125	137
Off-site	14,796		322		432
Total	95,904	1,229			1,558

Source: 1993 Survey of Nuclear-Related Employment in United States Electric Utilities. Institute of Nuclear Power Operations. INPO 93-007. October 1993.

2. The attached chart shows a staffing comparison of WNP-2 with four other nuclear units of similar age and size, based on data from the Electric Utility Cost Group (EUCG). The chart indicates that WNP-2's staff level is nearly 400 above the average of the other four units, and 300 higher than the average when WNP-2 is included. Does the Supply System believe those units provide a good benchmark for WNP-2 staffing and costs? If not, please provide EUCG staffing data, including off-site numbers, for the nuclear units that you believe are most comparable to WNP-2.

3. The consulting firm Tim D. Martin & Associates (TDM), which helps nuclear utilities manage their staff levels, has developed a staffing database that is based partly on its own investigations of utility corporate structures, rather than entirely on utility self-reporting. The TDM database includes all regular

utility employees at nuclear plants, all off-site corporate support staff, and all long-term contractor staff (defined as being on the job at least 6 months). The attached summary of the database indicates that the total average staffing for a 1,000 megawatt General Electric reactor is about 1,100. To make that figure more comparable to WNP-2, 10 percent adjustments could be made for WNP-2's larger size (1,100 megawatts), its status as a single-unit plant, and the Supply System's status as a single-plant utility. The resulting average staff level of 1,400 compares with the Bonneville Power Administration's count of permanent on- and off-site WNP-2 staff of 1,881. How does the Supply System account for such a large difference?

4. The attached table from Bonneville shows total WNP-2 staffing rising by 89 from December 1991 to March 1994. Why did that increase take place?

5. Supply System Managing Director William G. Council testified at the hearing that WNP-2 staffing was higher than he would prefer. If current staffing is too high, what does the Supply System believe is the optimal staff level? Does the Supply System have a plan to reach that level? If so, what is the timetable for that program, and how will the reductions be achieved? How much will WNP-2's annual costs be reduced?

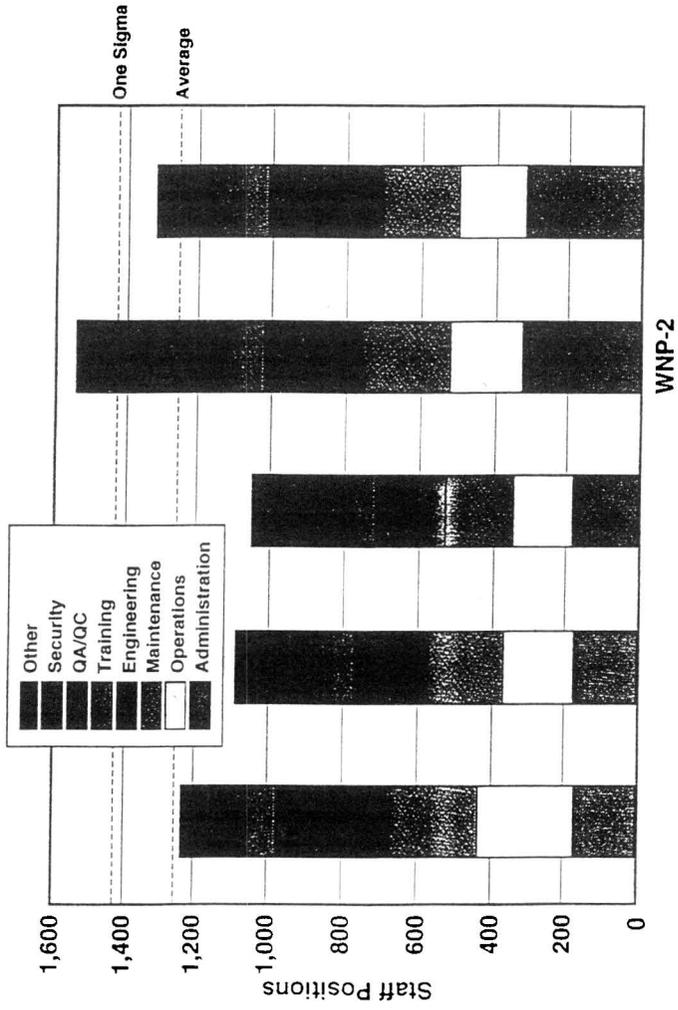
6. At the hearing, Mr. Council testified that staff reductions could force him to shut down WNP-2 for safety reasons. Please elaborate on that assertion. How rapidly and deeply could WNP-2 staff be reduced without threatening safety? Aren't there similar plants that operate safely at substantially lower staff levels?

Capital Costs

1. According to information provided by Bonneville in December 1993, expenditures on WNP-2 "special capital" projects after 1996 were expected to total \$8.1 million. However, in April 1994 the Supply System estimated that special capital expenditures after 1996 would total \$32.4 million. What is the reason for that increase? How firm is the latest schedule, which indicates that all special capital projects will be completed by 1999?

2. Capital additions at U.S. nuclear plants have averaged \$25 per kilowatt of capacity per year during the past five years, according to the Utility Data Institute. That is about \$27.5 million per year for a plant the size of WNP-2. The Supply System's April 1994 projection shows regular capital additions averaging about \$32 million per year through the end of the 1990s, in constant FY1995 dollars, and rising to about \$40 million a year from 2000-2004. Why will such a relatively new plant as WNP-2 require above-average capital additions during the next decade? Does the Supply System have any plans to reduce those scheduled expenditures?

Total Staff Positions



030924.12
Nov 1992

Figure 3

EUCG

Selected Units For Comparison With WNP-2

SIZE, MW	TYPE	YEAR	SALP RATING	CAPACITY FACTOR %
1150	P	85	1.71	78
1100	B	88	1.71	74
930	P	84	1.43	78
1140	B	84	1.71	60
1150	P	85	1.71	77

Table 2

SUPPLY SYSTEM STAFFING

The March WNP-2 Headcount to Megawatt Ratio has increased from 1.72 to 1.8 employees per megawatt (1,924 employees /1,086 megawatts), which reflects some staffing-up for the outage. Since December 1991, there have not been reductions at WNP-2; however, there has been a total reduction of 42 in the corporate areas (corporate allocation to WNP-2 is down 24 and corporate headcount for all other projects has been reduced by 18).

The program for 'Reduction Of Reliance On Outside Services' was initiated in January of this year by Vic Parrish. Contractor headcount (excluding outage contractors) charged to WNP-2 has decreased slightly to about the same level as it was 18 months ago. Vic has invited all managers to initiate reviews and controls of the use of contractors to "help reduce the cost of power to BPA and the ratepayers of the Northwest." Last month, Planning and Control staff met with the various managers to get commitments for contractor staff reductions. The current forecast shows planned reductions of 7 in May, 16 in June, and 45 in July.

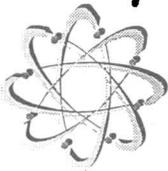
The table below, based upon data reported in the Supply System Monthly Reports, tracks actual total staffing from December 1991 to the present.

Supply System Staffing	DECEMBER 1991	MARCH 1992	MARCH 1993	MARCH 1994	Variance Dec 91 - Current Month
OUTAGE START DATES		4/18	5/1	4/30	
WNP-2					
Regular & Project	1,243	1,247	1,252	1,313	+ 70
Temporary	23	67	43	43	+ 20
Corporate Allocation	322	322	312	298	-24
Total Supply System	1,588	1,636	1,607	1,654	+ 66
Contractors	247*	254	345	270	+ 23
Total WNP-2	1,835	1,890	1,952	1,924	+ 89
All Other Projects					
Supply System	169	175	168	151	-18
Contractors	9*	5	11	14	+ 5
Total Other Projects	178	180	179	165	-8
GRAND TOTAL	2,013	2,070	2,131	2,089	+ 76

Footnotes:

- All data is based on actual headcount extracted from Supply System Monthly Reports.
- The "All Other Projects" section is composed of all Supply System staff charged to WNP-1, WNP-3, WNP-4/5, HGP, Packwood, and 9 percent of corporate.
- Numbers are as of August 1992, because reliable non-outage support contractor data was not available until then.

Source: Bonneville Power Administration



**BAD NEWS . . . IT HAS STABILIZED
 AT VERY HIGH LEVELS**
 (Staffing for Standard 1000MW Plant)

FUNCTION	B&W	CE	W	GE
Plant	392	376	315	360
Technical	193	177	177	180
RAD/ Environmental	59	61	51	60
Nuclear Assurance	74	105	106	102
Services	254	276	280	257
Management	33	36	36	43
Clerical	96	96	95	98
Total	1101	1127	1060	1100

Source: TDM Analysis



1100 of 1000 MW by companies



WASHINGTON PUBLIC POWER SUPPLY SYSTEM

P.O. Box ~~958~~ 3000 George Washington Way • Richland, Washington 99352-0968 • (509) 372-5000

September 30, ~~1994~~

The Honorable George Miller
Committee on Natural Resources
U.S. House of Representatives
Washington, D.C. 20515-6205

Dear Representative Miller:

Enclosed are responses to the questions raised in your September 8 letter (enclosed) regarding the Supply System and Plant 2 operations. One of our concerns, as expressed in several exchanges of information between the Supply System and your staff, is how Plant 2 is compared with other operating nuclear plants of similar type. Every plant is unique in its specific design, location, political environment and organizational form and authorities.

As a joint operating agency in the state of Washington, the Supply System operates under very specific authorities and requirements of the state. Because we are a single plant operator with one customer, Bonneville Power Administration (BPA), we do not have a traditional electric utility infrastructure and corporate organization to provide the plant administrative support. This support is not included in the nuclear industry comparison data, but because BPA pays our total costs, these administrative costs must be paid by the region's ratepayers and included in BPA's costs. These differences are mentioned only to help clarify why it is difficult to make exact comparisons between operating plants.

The Supply System recognizes the importance of being compared with other plants throughout the industry and we do so on a monthly basis. One such comparison that was pointed out by Mark Holt in his January 24, 1994 memo to the House Natural Resources Committee, was that the Supply System's costs in calendar years 1989 through 1992 were approximately equal to or below the industry average.

We also recognize that our future in today's competitive market will be dependent on our ability to cut our costs below the industry average. Toward this end, I initiated a program last month to reduce our fiscal year 1995 costs by approximately ten percent. We expect our current year's operation and maintenance costs to be \$10 to \$15 million below our fiscal year 1994 costs.

We are in agreement that costs must be lowered and believe that our current initiative will put us on a path to become more efficient over the next few years.

Very truly yours,



W. G. Council
Managing Director

RESPONSE TO GEORGE MILLER'S QUESTIONS**A. WNP-2 STAFF LEVELS****1. Institute of Nuclear Power Operations (INPO) Statistics on Manpower.**

QUESTION: *What is the Supply System's analysis of these statistics? Are they a legitimate indicator that WNP-2 on- and off-site staffing is higher than the industry average?*

ANSWER: The Supply System, like every other nuclear operating plant, submits staffing numbers to INPO in various categories, including the general groupings of on-site and off-site per the table displayed in your questions. The data in the first and last columns are verifiable from the INPO report. We assume the averages combine all plants of all vintages and sizes and an attempt is made to normalize the data by plant size. These averages are useful as broad general observations but cannot be used for specific plant comparisons. The most realistic comparative data from the INPO staffing report is to compare "on-site" data for like plants. In Attachment 1, we have compared the INPO staffing data for on-site employees for large single unit BWRs which entered commercial operation in the mid-to-late 1980's. This chart shows that our on-site staffing levels are in the middle of the group of six plants. The off-site data is also displayed, however we feel this data is very inconsistent and cannot be used for valid comparison.

2. EUCG shows staffing levels 300-400 higher than others.

QUESTION: *Does the Supply System believe those units provide a good benchmark for WNP-2 staffing and costs? If not, please provide EUCG staffing data, including off-site numbers, for the nuclear units that you believe are most comparable to WNP-2.*

ANSWER: The Electric Utility Cost Group (EUCG) is an ad-hoc utility group which has collected nuclear power plant cost and manpower data over the past eight years. The database is proprietary with the data to be for the sole use of submitting members. Data is categorized by work functions with staffing data provided on an equivalent staffing basis and includes contractors. On-site and off-site are not reporting categories for this database. Using the same six plants described above, we have looked at the latest information which is for reporting year 1992. Attachment 2 shows

a graph of this data. Plant 2 falls in the middle of the range for the staffing data collected by the EUCG for the aforementioned set of plants. The average equivalent staffing number is 1352 and the Supply System number is 1310 for direct work functions.

3. **TDM database predicts 1400 staffing vs 1881 reported by BPA.**

QUESTION: How does the Supply System account for such a large difference?

ANSWER: Tim D. Martin & Associates (TDM) also has a proprietary database of which we have no detailed knowledge and therefore have a very difficult time analyzing any results or conclusions from that data. Your letter states that the database "includes all regular utility employees at nuclear plants, and off-site corporate support staff, and all long-term contractor staff". Based on our experience in discussing staffing with other utilities, we have not found any utility that includes allocations of corporate functions as part of total staffing for a plant as is reported by the Supply System and BPA.

4. **BPA report shows total WNP-2 staffing increasing to 89 from December 1991 to March 1994.**

QUESTION: Why did that increase take place?

ANSWER: The increase in staffing of 89 from December 1991 to March, 1994, is the result of many shifts and changes in the organization. In that time period there has been a reduction in corporate support to Plant 2 and increases in plant operations, maintenance and capital programs. In the operations and maintenance areas, the plant placed increased emphasis on reliability as addressed in my testimony. Operations and training are targeted areas. Other areas with increases are health physics and plant chemistry. In the capital area, we have been working on megawatt improvement projects and implementing a large construction contract settlement. Work on these projects have also increased staffing to the plant.

5. WNP-2 staffing higher than Managing Director would prefer.

QUESTION: *What does the Supply System believe is the optimal staff level? Does the Supply System have a plan to reach that level? If so, what is the timetable for that program, and how will the reductions be achieved? How much will WNP-2's annual costs be reduced?*

ANSWER: During my testimony, when I stated that staffing levels are higher than I prefer, I was primarily referring to the number of contractor support personnel, however, some reductions can also occur in Supply System staffing levels.

An optimal staff level is very difficult to define due to the complexity of operations, uncompromising demands for safety and the challenging regulatory environment in which we operate. As stated in my testimony, we are on a three year "get well" program in which the first year has achieved some excellent operational results. Ideally, we would like to sustain and institutionalize this good performance before entering into staff reductions. However, due to the increased competitiveness of the industry at this time, we are reducing year-round contractor support to about 80 contractors. (This number could be smaller but we must maintain adequate staff to support an annual outage cycle.) We are also looking at reducing the Supply System staff in areas where managers feel they can take some business risk but with no risk to the safe operation of the plant. The estimated annual budget reductions as a result of this effort is estimated to be \$10-15 million for the current fiscal year.

6. Staff reduction could force shutdown.

QUESTION: *How rapidly and deeply could WNP-2 staff be reduced without threatening safety? Aren't there similar plants that operate safely at substantially power staff levels?*

ANSWER: If staff reductions are ordered without reducing the work and fully evaluating the impact to safety, then the plant safety could be jeopardized. The level and time period for staff reductions must be carefully considered with close attention paid to current regulatory changes, the experience and training of the staff and the physical condition of the plant. Items of work which have an impact on staffing levels include the attention received from the NRC. For example, in 1993, Plant 2 had more NRC attention

than any other nuclear operating plant in the nation. In 1993, according to a NRC report, they expended 16783 hours on Plant 2 compared to the mean of 7515 and an average of 6792. This attention requires considerable staff time to prepare information, answer questions, provide follow up and resolve concerns. Industry "rule of thumb" is that the utility spends 25 hours for every hour of attention by NRC.

Regarding similar plants which operate safely at substantially lower staff levels, we are aware of one in our databases. This is a highly rated plant for some time with an excellent operating record. We are striving to achieve that standard of excellence. However, as shown by the EUCG data in Attachment 2, we are close to the staffing average of similar plants and are striving to reach the best of the group. Another comment regarding similar plants is that none operate on a 12-month fuel cycle as we do. This means that each year we must plan, schedule and execute an outage which increases work and reduces the amount of generation Plant 2 can achieve. In a non-outage year, other plants can achieve a 100 percent capacity factor while our theoretical limit is 83 percent. This operating characteristic, which is required for integration with the hydro-dominated Federal Columbia River Power System, does increase work and staffing levels.

B. CAPITAL COSTS

1. "Special Capital" projects increase by \$24.3 million in new estimate.

QUESTION: What is the reason for that increase? How firm is the latest schedule, which indicates that all special capital projects will be completed by 1999?

ANSWER: According to our Fiscal Year 1994 Long Range Forecast, "special capital" projects past Fiscal Year 1996 are estimated to cost \$11.7 million and in April 1994, the same forecast for Fiscal Year 1995 has estimated costs beyond Fiscal Year 1996 to be \$32.4 million. The reason for the increase in future Fiscal Year 1995 is a delay in the implementation of some projects so we can closely evaluate the cost-benefit of each project, the schedule in which the project can be successfully implemented and the impact such an implementation has on the outage length. A common period comparison of the two referenced plans (FY95 through FY99) shows the FY94 forecast to be \$77.7 million while the FY95 version is \$83.9 million. The difference of the two estimates is

primarily deferral of work planned but not executed in FY94. All special projects may not be completed by FY99 if the schedule and cost-benefit analysis does not support such a completion schedule.

2. Routine capital additions higher than industry average per Utility Data Institute (UDI).

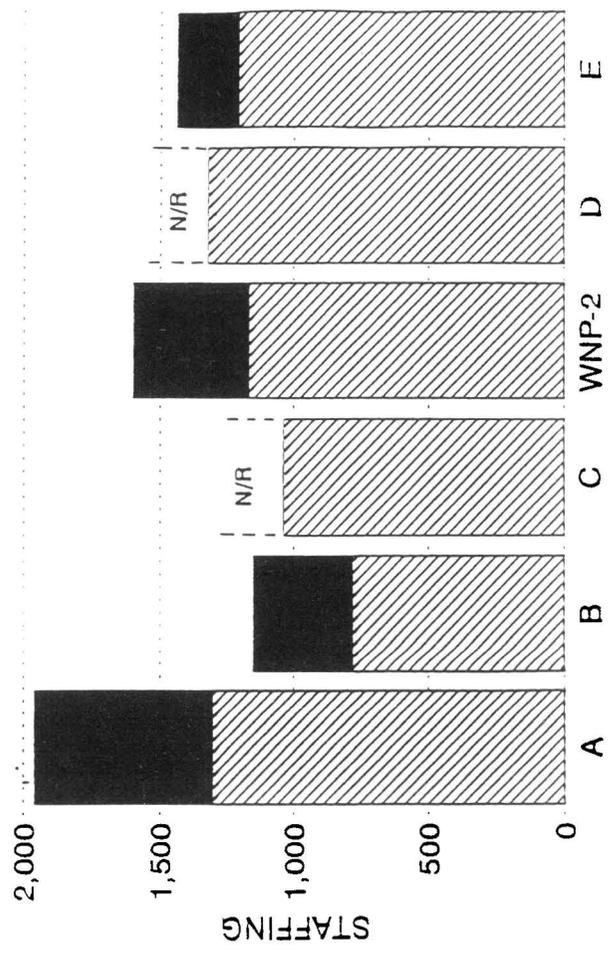
QUESTION: Why will such a relatively new plant as WNP-2 require above average capital additions during the next decade? Does the Supply System have any plans to reduce those scheduled expenditures?

ANSWER: In speaking with a representative of the Utility Data Institute (UDI), we found that the capital numbers in their report are industry-wide averages obtained by calculating the change in plant capitalization from year to year. According to our property accounting records, Plant 2 total capitalization over the first 10 years of operation averaged \$13 million per year or \$11.38 per megawatt installed capacity. For Fiscal Years 1992, 1993 and 1994 the plant capitalization change was \$14.7 million, \$33.3 million and \$12.5 million respectively. UDI stated that the change in capitalization between 1992 and 1993 (their latest data) is \$33 per kilowatt hour. For a 1,150 megawatt facility such as Plant 2 that would equate to \$38 million. This is higher than current Plant 2 plans. Once again, without understanding how each utility submits this data and what is/is not included, we do not consider the data accurate enough on which to base capital spending decisions.

In regard to why Plant 2 needs to have such a large amount of capital additions, the plant will have operated 20 years by 2004, which is not a "relatively new" plant. Much of the equipment was procured in the 1970's which means that the equipment may be as much as 30 years old by 2004. According to our depreciation schedules, 10.5 percent of the plant in service (which is \$338 million) has an expected life of 20 years or less. Although depreciation schedules do not dictate equipment life, they do provide a guideline for expected replacements. In addition, not all of the capital is to replace old equipment but is used to provide upgrades and to implement regulatory required changes. Even with the above information, the Supply System is trying to reduce the level of capital expenditures in the future. When we believe this can be realistically achieved, the Long Range Forecast will reflect lower capital costs.

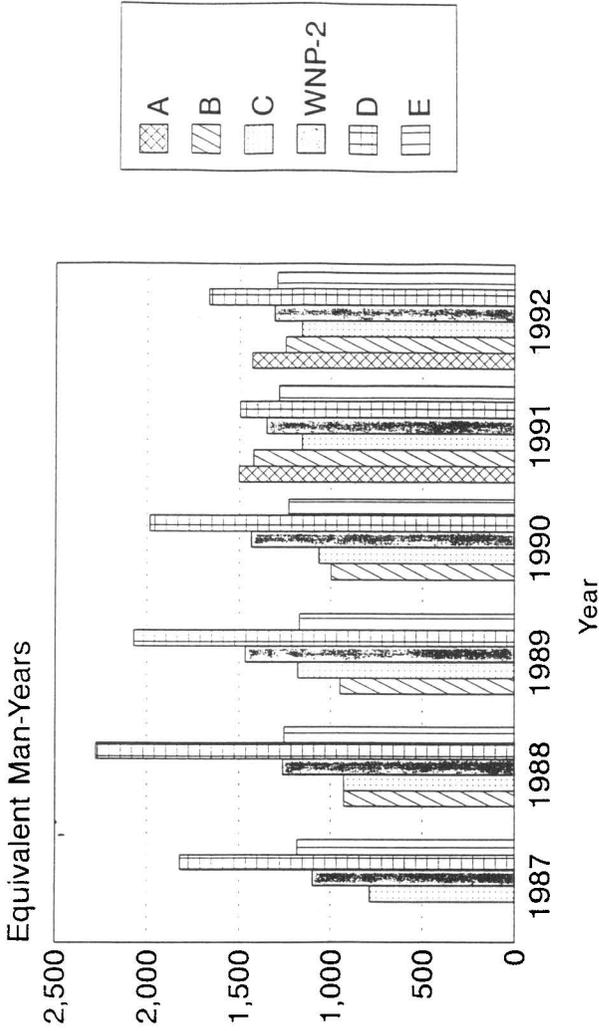
INPO'S 1993 STAFFING COMPARISON

 ON SITE STAFFING
  OFF SITE STAFFING
 N/R = NOT REPORTED



Comparison with other late vintage, single unit BWR Plants

LARGE UNIT BWR'S EUCCG DATA BASE



Comparison with other late vintage, single unit BWR Plants

COMMITTEE ON WAYS AND MEANS
SUBCOMMITTEE ON HEALTH
SUBCOMMITTEE ON HUMAN RESOURCES
CHAIRMAN
COMMITTEE ON STANDARDS OF
OFFICIAL CONDUCT
COMMITTEE ON DISTRICT OF COLUMBIA
CHAIRMAN
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AND HEALTH
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EDUCATION

JIM McDERMOTT
7TH DISTRICT, WASHINGTON

CO-CHAIRMAN
CONGRESSIONAL URBAN CAUCUS
CHAIRMAN
CONGRESSIONAL TASK FORCE ON
INTERNATIONAL HIV/AIDS
VICE CHAIRMAN
ARMS CONTROL AND FOREIGN
POLICY CAUCUS
ELECTED REGIONAL WHIP, ZONE 2

Congress of the United States
House of Representatives
Washington, DC 20515

September 8, 1994

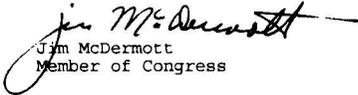
Chairman George Miller
Subcommittee on Oversight
and Investigations
1324 Longworth
Washington, D.C. 20515

Dear Mr. Chairman:

On behalf of Seattle City Light, I would like to submit the following testimony to be included in the record for the August 9 hearing concerning, "BPA at the Crossroads," the Majority Staff Report from the BPA Task Force.

Thank you for your assistance.

Sincerely,


Jim McDermott
Member of Congress

Office of the Mayor
City of Seattle

Norm Rice, Mayor



Testimony of Mayor Norm Rice on
"BPA at a Crossroads"
The 1994 Majority Staff Report of the
Task Force on the Bonneville Power Administration
Before the Subcommittee on Oversight and Investigations
House Committee on Natural Resources
Washington, D.C.
August 9, 1994

I would like to thank Chairman George Miller for this opportunity to discuss the Bonneville Power Administration's (BPA) competitiveness project, and I commend Representative Peter DeFazio for his thorough investigation of this issue as Chair of the Natural Resource Committee's Task Force on BPA.

The release of "BPA at a Crossroads," a report of the Natural Resource Committee, has contributed greatly to the Pacific Northwest's understanding of the challenges facing BPA as it struggles to "reinvent" itself. I share many of the report's findings and I look forward to working with BPA, fellow utilities, my constituents, Congress, and the Administration to identify a role for BPA in the Pacific Northwest that permits the agency to guard its competitiveness and fulfill its responsibilities to the region.

First, I want to express my wholehearted support for BPA's efforts to improve its competitiveness and customer service, known as the Competitiveness Project, the most commonly stated purposes of BPA's "reinvention." The entire nation will benefit from a more competitive electric utility industry and it is wise for BPA to respond to new opportunities for competition brought forth in the 1992 National Energy Policy Act. Also, the Pacific Northwest will benefit from a reinvigorated BPA that is leaner, less bureaucratic, and more responsive to the public.

As the process of reinvention unfolds, however, I am deeply concerned by BPA's apparent narrow view of its role in the Pacific Northwest. To date, the process has been dominated by a model of competitiveness the principal purpose of which is to minimize the kilowatt hour price of electricity in the short run, and to maximize short-run revenues to the agency. These goals exclude much of BPA's mission.

The American people have empowered BPA with special responsibilities of governance that transcend those expected of a private corporation. These responsibilities are not just a matter of trust, but are contained in the federal laws governing management of the Pacific Northwest's power system. In particular, we expect and the law directs BPA to employ its ownership of the Federal Columbia River Power system so as to safeguard our environment, promote conservation and efficiency in the use of electric

Mayor Norm Rice
August 9, 1994
Page 2

power, encourage the development of renewable resources within the Pacific Northwest, protect and enhance fish and wildlife resources, and foster cooperation and coordination among the region's electric utilities.

I am particularly concerned that the Competitiveness Project appears to reject a fundamental agreement I thought the Pacific Northwest had firmly established with the passage of the Regional Power Act. As part of a sensible strategy to purchase "least-cost" resources, BPA committed to an aggressive pursuit of energy conservation as its resource of highest priority. Under its Competitiveness Project, however, BPA proposes to replace its aggressive and direct involvement in the planning and acquisition of energy conservation with a passive approach that relies on "market forces." It is doubtful that this new strategy will achieve the conservation acquisition called for in the Regional Power Plan and BPA's 1992 Resource Program.

The City of Seattle's direct experience with energy conservation contrasts with BPA's new approach. Since 1987, City Light conservation programs have saved 2 billion kilowatt hours of energy, with Seattle residents paying for nearly three-quarters of this accomplishment. These investments have been an integral part of our resource strategy and have boosted rather than thwarted City Light's competitiveness by enabling us to avoid the high costs and uncertainty associated with building new thermal resources.

The Pacific Northwest has traditionally contributed toward the purchase of energy conservation in the Seattle area because this investment makes sense for the region as well. No energy resource is cheaper than conservation and nowhere is it more plentiful than in the central Puget Sound area. Each kilowatt hour of energy saved in Seattle means an additional kilowatt hour of affordable energy is available for consumption elsewhere in the region. These savings reduce the region's reliance on sources of electricity that cause harm to our environment.

In 1992, BPA formally recognized the value of Seattle's conservation resources when it agreed to increase financial support for City Light's conservation program. In exchange, City Light agreed to increase its acquisition of conservation to help the region achieve conservation targets. The City's commitment followed a promise of direct financial assistance from BPA. In 1993, our cooperation bore fruit when BPA exceeded its conservation target by nearly one-third, saving 50 megawatts of energy across the region. Seattle contributed 9 megawatts, or 18 percent, of that region-wide total, enough to supply power to 36,000 residential customers for one year.

Despite BPA's withdrawal of support for our programs, Seattle will not abandon its aggressive pursuit of conservation and the region will continue to benefit from our efforts. Our commitment has been to meet all of Seattle's projected increase in demand for electricity through conservation measures until the year 2003--not through building more dams or burning more fossil fuels.

Mayor Norm Rice
August 9, 1994
Page 3

While our resolve remains, BPA's withdrawal of support for our programs casts doubt on the city's ability to fulfill its commitment. In dollar terms, BPA's proposal will mean an annual loss of about \$20 million for Seattle's conservation programs. In real terms, its effect means that much energy conservation will be left undeveloped in Seattle, the city offering the region its most abundant and affordable opportunities for energy savings.

The diminished importance of energy conservation at BPA also threatens the success of regional efforts to save energy. In 1991, the region completed a formal energy planning process, as required by the 1980 Northwest Power Planning and Conservation Act, in which BPA was assigned responsibility for acquiring 660 megawatts of energy conservation. BPA formally committed to achieving a minimum of 660 megawatts of energy conservation in its 1992 Resource Program. By BPA's own estimate, its "market reforms" will lead to savings that fall short of its 1992 commitment for energy conservation. Where the region will find the additional resources and effort needed to fill the void of BPA's virtual absence in regional conservation efforts is a troubling and as of yet unanswered question.

Whether the Pacific Northwest is ultimately able to achieve its minimum targets for energy conservation is a secondary concern. The most important question for the region is how far beyond the "minimum" could we have achieved, as witnessed in 1993, had BPA maintained its resolve and financial commitment to energy conservation? How many power plants would we have avoided building? How much healthier would our environment be? It is my sincere hope that fifteen years from now our children will not be reviewing our legacy and asking these same questions, with no ability to affect the outcomes.

Although Seattle cares deeply about energy conservation, other aspects of Bonneville's Competitiveness Project may have far greater financial impact on the City. In addition to the loss of \$20 million in conservation funding, a recent study completed on behalf of the Association of Public Agency Customers concluded that BPA's new rate structure will shift about \$200 million in annual costs from the Direct Service Industries, composed of the region's aluminum companies, to public utilities throughout the Pacific Northwest. Also, BPA's Business Plan projects the agency will receive an additional \$231 million in revenues from new charges for its products and services. Public utilities with generating facilities, such as City Light, appear to be likely candidates to absorb the vast majority of these cost shifts.

Before BPA can expect the public to support its plans, the agency must be more forthcoming with information about who will be paying how much for these shifted costs. City Light has no specific information about likely rate increases to result from BPA's reinvention, yet until recently BPA was prepared to begin a formal rate case

Mayor Norm Rice
August 9, 1994
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next October to implement its proposed changes. The decision to postpone the rate case until next January is welcome, but does not solve the problem. BPA's business plan recently revealed that the full financial impact of the proposed changes will not be known until 1999, the year in which BPA hopes to phase in the last of its new charges for energy services.

If BPA's competitiveness is truly at risk, I urge it to look more closely at other methods of cutting costs, and the postponement of the rate case provides a good opportunity to do so. In particular, the Natural Resource Committee's BPA Task force recommends \$150 million in potential annual budget savings in addition to BPA's current plan to cut its conservation budget and increase rates for its services. Among others, the savings include \$110 million in cuts associated with management of the Washington Public Power System's nuclear plants, whose total annual costs amount to 25% of BPA's entire budget. In addition, the Committee urges BPA to reevaluate its calculation of a credit applied to the electricity bills paid by the Direct Service Industries. An updated calculation using today's interest rates would save BPA \$40 million each year.

Decades ago, the citizens of Seattle made far-sighted investments in hydroelectric generation that has blessed the city with stable and low electric rates. While we are proud of this legacy, the cost of maintaining and upgrading our hydroelectric system and financing our conservation programs have recently led to sizable rate increases. In 1993, Seattle's rates were increased by an average of 12.6%, and its average rate for industrial customers was higher than four of the seven large regional utilities which the City uses as a basis for comparison. Another rate increase is scheduled next year and by 1998, our rates are expected to be one-third higher than their 1992 levels.

As difficult as these rate increases will be on the citizens of Seattle, they do not include BPA's withdrawal of support for conservation or other costs that will be shifted to the City under BPA's "reinvention" proposal. Although the amount of the additional costs Seattle will bear as a result of BPA's changes is undetermined at this time, early indications are that it will be significant. For this reason, I must conclude that BPA's "reinvention" plans, as currently configured, will impose an unacceptably heavy burden on Seattle and its economy.

Many aspects of BPA's Competitiveness Project are praiseworthy and should be implemented without delay. For example, decentralizing the administration of conservation programs is a sensible move that will reduce overhead and result in programs that are more responsive to local customers. Likewise, BPA proposals to operate more efficiently and simplify its organizational structure will reduce costs and improve the performance of the agency.

Mayor Norm Rice
August 9, 1994
Page 5

I must oppose, however, other aspects of BPA's reinvention plans and recommend that their implementation be delayed. For example, "reinvention" of conservation calls for a series of changes that appear unable to match the tremendous accomplishments of the conservation strategies they will replace. Also, other cost savings offered by BPA amount to little more than shifts in costs that appear to be distributed inequitably throughout the region.

The Northwest Power Act was enacted under the premise that those who share in the benefits of the system shall also in meeting its goals. Perhaps inadvertently, BPA's "reinvention" of itself fundamentally alters that assumption. In essence, through its proposed changes, BPA hands out a portion of the federal system to its customers, and in doing so, releases them from the responsibilities of contributing to efforts to conserve energy and meet new load growth. The net effect is that the growing municipalities in our region, such as Seattle, will shoulder all these costs.

I am concerned that such a dramatic recasting of the Power Act's purpose should originate from BPA and occur with such little examination of its implications. In common with BPA and other utilities throughout the region, Seattle City Light is adjusting to intensified competitive pressures. The entire region will benefit from efforts to cut costs and surely we can identify a fairer distribution of existing costs. However, I firmly believe that in the end, continued cooperative management and development of the region's energy resources is the most effective means of helping BPA and all Pacific Northwest utilities remain competitive. In its current form, the Northwest Power Act assumes the same.

I pledge to work together with the region, the federal government, and Congress to seek reform of BPA in a manner which preserves its competitiveness, respects its responsibilities, and balances fairly the costs of these changes throughout the region. Unfortunately, BPA's efforts to date fall short of this challenge.

As a first step, I offer the following suggestions. First, the entire process should be delayed until all communities have a better understanding of how much BPA's "cost cutting" measures will raise their rates. Second, BPA should introduce "market-forces" as a supplement to its conservation programs, not a replacement. Finally, the region must look more closely at all possible cost cutting opportunities and the Committee's report offers appropriate suggestions to begin this scrutiny.

The decisions we make today influence more than tomorrow's rates and revenues. Our actions will have a profound effect on the quality of life and choices we leave for our children. With this imperative in mind, I am confident that as a region we can find a better solution. I would like to thank Chairman Miller for this opportunity to testify and Rep. DeFazio for his tireless work on these issues on behalf of the Pacific Northwest.

Comparison of WNP-2 Staff Levels With Industry Averages

Mark Holt
Congressional Research Service
August 8, 1994

Comparing staff levels at different nuclear plants can be difficult, because utilities vary in their reporting of nuclear-related employment, both at plant sites and at headquarters. However, the databases located for this review indicate that staffing at Washington Nuclear Project No. 2 (WNP-2), near Richland, Washington, may be significantly above average.

Institute of Nuclear Power Operations (INPO) Survey. All nuclear utilities are asked by INPO to fill out a questionnaire indicating on- and off-site nuclear-related employment. The Washington Public Power Supply System (WPPSS), which operates WNP-2, believes other utilities undercount their nuclear staff for the INPO survey, particularly off-site positions. WPPSS also doubts that all security personnel, who are often contractors, are counted at all sites. In response to those objections, only the INPO data for on-site, non-security staffing is used here; a rough calculation based on plant capacity yields an average of 783 workers for a reactor the size of WNP-2.¹ WPPSS says its permanent WNP-2 staff, excluding security, totals 1,167² — almost 400 more.

Electric Utility Cost Group (EUCG). Data collected by the EUCG is intended to be more rigorously uniform than the INPO survey, although WPPSS believes that staffing at other utilities is still underreported. A chart provided by the Bonneville Power Administration (BPA), based on EUCG data, shows total staff positions at WNP-2 at about 1,550, while comparable staff at four other plants of approximately the same age average about 1,175 — also nearly 400 lower. Even if WNP-2 is included in the average, its staff level is 300 higher.

Tim D. Martin & Associates (TDM). One of the primary activities of the consulting firm TDM is to help nuclear utilities manage their staff levels. For each client utility, the firm identifies all nuclear-related staff throughout the organization, including all regular utility employees at nuclear plants, all off-site corporate support staff, and all long-term contractor staff (those on the job at least 6 months). A database developed from that information indicates that the total average staffing for a 1,000-megawatt General Electric reactor is about 1,100.³ Allowing 10 percent adjustments for WNP-2's larger size (1,100 MW), its status as a single-unit plant, and WPPSS' status as a single-plant utility results in a rough baseline of about 1,400 employees. BPA's count of permanent

¹ 1993 Survey of Nuclear-Related Employment in United States Electric Utilities. Institute of Nuclear Power Operations. INPO 93-007. October 1993.

² Analysis of WNP-2 Staffing and Capital Expenditures. WPPSS Financial Management office. May 18, 1994.

³ Nuclear Industry Costs. Tim D. Martin & Associates, Inc. Presentation to U.S. Council for Energy Awareness. November 29, 1993.

WPPSS staff and contractors allocated to WNP-2 totals 1,881⁴ — nearly 500 more.

Potential Savings. According to BPA, which pays all of WNP-2's costs, the average annual cost per staffer at the plant is \$64,573. Reducing WNP-2 staffing to average industry levels, as indicated by the data discussed above, could therefore save about \$20-30 million per year.

⁴ Chart provided by James Lewis, BPA Nuclear Project Office Director. July 28, 1994.

103d Congress }
2d Session }

COMMITTEE PRINT NO. 7

BPA AT A CROSSROADS

MAJORITY STAFF REPORT
OF THE
TASK FORCE ON
BONNEVILLE POWER ADMINISTRATION
OF THE
COMMITTEE ON NATURAL RESOURCES
OF THE
U.S. HOUSE OF REPRESENTATIVES
ONE HUNDRED THIRD CONGRESS
SECOND SESSION



MAY 1994

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May 1994

MEMORANDUM OF TRANSMITTAL

COMMITTEE ON NATURAL RESOURCES,
 U.S. HOUSE OF REPRESENTATIVES,
 WASHINGTON, DC.

*To Members of the
 Committee on Natural Resources
 of the House of Representatives*

The Bonneville Power Administration Task Force has submitted the following report entitled *BPA at a Crossroads*, which is hereby made available to all members of the committee. This report summarizes the results of the most comprehensive congressional oversight of BPA since the passage of the Pacific Northwest Electric Power Planning and Conservation Act of 1980.

I commend Representative DeFazio, Chair of the committee's Task Force on the Bonneville Power Administration, for his fine work on this report. Representative DeFazio's understanding of the extremely complex issues surrounding the Columbia River power system is unparalleled in the Congress. His understanding and insight may well be the key to resolving the many difficult challenges facing BPA and the Northwest region in the coming years.

I am particularly impressed by the work that Representative DeFazio has done to uncover potential reductions in BPA costs and power rates that would not sacrifice BPA's commitment to energy efficiency and the conservation of the Northwest's wildlife resources. As Representative DeFazio's report points out, the energy efficiency and wildlife conservation programs have received disproportionate criticism over their costs, despite the fact that other areas of BPA's budget offer large savings potential. The Washington Public Power Supply

(III)

JOHN LAWRENCE
 STAFF DIRECTOR
 STANLEY SCOVILLE
 GENERAL COUNSEL
 DANIEL VAI HISH
 REPUBLICAN STAFF DIRECTOR

IV

System nuclear reactors are perhaps the best example of such possible budget savings. Better management of these facilities offers large potential savings that have received relatively little scrutiny.

The report also finds that the "project power" rates for the Bureau of Reclamation's Columbia Basin Project reduce power costs to one-tenth of one cent per kilowatt hour of electricity, which is less than one twenty-eighth of the price paid by other BPA customers. This cut-rate price for power imposes considerable costs on the economy and environment of the Northwest by increasing the price other BPA customers pay for power and encouraging excessive use of water. Excess water use leads to diminished flows that not only impede the effort to restore salmon stocks but also reduce power generation.

The recent work of the committee on ecosystem management is borne out by the Report's findings regarding the need to implement the basin-wide *Strategy for Salmon* adopted by the Northwest Power Planning Council. These salmon conservation measures exemplify the need to look at activities across the ecosystem and involve all stakeholders in achieving a sustainable environmental and ecological status for the Northwest.

Again, I praise Representative DeFazio for bringing these issues to the attention of the committee, and I look forward to working with him and other Members of the Pacific Northwest congressional delegation on these matters in the future.

Sincerely,



GEORGE MILLER
Chair

U.S. House of Representatives
Committee on
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 Washington, DC 20515-6201

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May 1994

MEMORANDUM OF TRANSMITTAL

COMMITTEE ON NATURAL RESOURCES,
 U.S. HOUSE OF REPRESENTATIVES,
 WASHINGTON, DC.

*To the Honorable George Miller, Chairman,
 Committee on Natural Resources
 of the House of Representatives*

I am formally submitting the original of the Bonneville Power Administration Task Force report entitled *BPA at a Crossroads*.

Sincerely,



PETER DeFAZIO
 Chair
 Bonneville Power Administration Task Force

(V)

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LIST OF ABBREVIATIONS

aMW	Average megawatt
BPA	Bonneville Power Administration
BuRec	Bureau of Reclamation, U.S. Department of the Interior
CBO	Congressional Budget Office
cfs	Cubic feet per second
Council	Northwest Power and Planning Council
CRITFC	Columbia River Inter-Tribal Fish Commission
CRS	Congressional Research Service, Library of Congress
DSI	Direct service industries
EIS	Environmental impact statement
EPUD	Emerald People's Utility District
ESA	Endangered Species Act
FTE	Full time equivalent
IRP	Integrated resource plans
kwh	Kilowatt-hour
mills	One-tenth of one cent or one one-thousandth of one U.S. dollar
mW	Milliwatt
MW	Megawatt
NCAC	Northwest Conservation Act Coalition
NMFS	National Marine Fisheries Service
PF-rate	Priority firm rate
PMA	Power Marketing Administrations
PNCA	Pacific Northwest Coordination Agreement
SOR	System Operation Review
VOR	Value of reserves
WAPA	Washington Area Power Administration
WPPSS	Washington Public Power Supply System

TASK FORCE CHAIR'S SUMMARY

The Bonneville Power Administration (BPA) supplies about one-half of all the energy consumed in the Pacific Northwest. It controls about 80 percent of the region's high voltage transmission capacity. By any measure, BPA is central to the region's economic well-being.

BPA is at a pivotal point in its 57-year history. The ground is shifting under the agency's feet, upsetting political and economic arrangements that have served the region since the passage of the Pacific Northwest Electric Power Planning and Conservation Act (Northwest Power Act) in 1980.

The following are among the significant challenges facing the agency:

- ▶ Increasingly deregulated and competitive energy markets are prompting BPA to reexamine its structure and mission. The agency is considering, and in many cases moving to implement, major changes in its structure and the manner in which it seeks to fulfill its mandates.
- ▶ Threatened and endangered Snake River salmon runs, and the decline of other Columbia River stocks, pose an extraordinary challenge to the agency and the region.
- ▶ Continuing pressure from Washington, DC to alter fundamentally the financial compact between the Federal Government and BPA adds another degree of uncertainty to a world increasingly defined by uncertainty.

The agency's last great shakeup occurred in the 1970s and early 1980s when the region bet heavily—and mistakenly—on nuclear power. The fallout from that series of bad decisions is reflected in every Northwest ratepayer's electric bill.

Between 1979 and 1984, BPA wholesale electric rates increased by 600 percent. That whopping rate hike was the direct result of BPA's decision to invest in three nuclear power plants owned by the Washington Public Power Supply System (WPPSS). Between 15 and 25 percent of every Northwest residential electric bill is dedicated to paying for one ailing and two uncompleted nuclear power plants in the State of Washington.

The Northwest Power Act, with its emphasis on comprehensive energy planning and regional resource development, grew out of the WPPSS fiasco. The Northwest Power Act created the Northwest Power Planning Council (Council), appointed by the Governors of the four States in the region—Idaho, Montana, Oregon, and Washington—and charged it with developing regional energy and fish and wildlife mitigation plans. Today, there are many who ask whether energy planning and regional resource development make sense in an increasingly competitive and deregulated energy market.

The Northwest Power Act's requirement to protect, mitigate, and enhance fish and wildlife populations affected by the hydroelectric facilities on the Columbia River system is also being challenged—though the challenges are more subtle.

The BPA Task Force set out to answer some not-so-simple questions: How has the Northwest Power Act withstood the test of time? Is BPA doing a good job of implementing the Northwest Power Act's provisions? And how

can we continue to enjoy the benefits of regional planning and coordination in the brave new world of more open and competitive energy markets?

This report's findings include the following:

- ▶ The Northwest Power Act sought to encourage conservation and efficient energy use and promote the development of renewable energy resources, thus assuring the Northwest an adequate, efficient, and economical supply of power. It requires BPA to protect, mitigate, and enhance the Columbia River basin's fish and wildlife populations and requires that fish and wildlife receive equitable treatment with respect to power production. The Northwest Power Act's goals remain sound.
- ▶ A more competitive BPA could better achieve the Northwest Power Act's goals. However, the region's long-term interest in promoting efficient energy use, developing renewable energy resources, and rebuilding the Columbia River basin's incomparable salmon stocks should not be sacrificed in order to minimize electric rates in the short term.
- ▶ A significant factor driving many of BPA's utility customers to consider alternative energy sources is the BPA "hassle factor." BPA's customers are legitimately dissatisfied with BPA's bureaucratic processes and cumbersome decisionmaking. However, BPA's focus seems to have shifted largely to the issues of price, and away from the customers' concerns about unwieldy BPA processes. BPA should refocus its efforts on responding to its customers' legitimate concerns about BPA's bureaucratic tendencies.
- ▶ BPA's conclusion that its rates are imminently uncompetitive is not supported by the analysis in its Draft Marketing Plan or by testimony presented during the task force's hearings. That is not to say, however, that BPA's interest in maintaining its competitive position is not prudent and appropriate. Rapidly changing energy markets could ultimately pose a significant threat and already offer alternatives to BPA-supplied power for some of BPA's utility customers. Therefore, BPA should make every effort to become a more efficient provider of conservation and energy resources while continuing to satisfy its statutory mandates.
- ▶ The task force staff identified up to \$150 million in achievable annual savings, most of which are not being prominently discussed by BPA as part of its Competitiveness Project. In addition, BPA has identified another \$66 million in annual savings it could gain through greater administrative efficiency—without any new legislation. More than \$50 million of the savings identified by the task force staff are associated with the WPPSS' three nuclear power plants, only one of which was ever completed.
If all of these savings were achieved, they could lead to a BPA rate *decrease* of 8 percent.
- ▶ A tiered wholesale electric rate should be one element in BPA's conservation acquisition strategy. However a tiered rate—by itself—is not likely to provide an incentive sufficient to cause utilities to make substantial direct investments in conservation and energy-efficiency measures.
- ▶ BPA must provide a stable, long-term financial commitment to conservation if the region expects to reach the energy-efficiency goals set out in the Council's Conservation and Electric Power Plan. The agency should not abandon direct investment in energy-efficiency measures, retreat from its fish and wildlife responsibilities, or decrease its

commitment to improve delivery of services in favor of untried "market mechanisms" until those mechanisms are proven to be widely effective.

- ▶ BPA needs to conduct a comprehensive analysis of the economic costs and benefits to the Northwest of the region's aluminum industry, known as the direct service industries (DSIs). Based upon this analysis, a new rate structure should be designed for the DSIs that equitably balances the interests of the DSIs and all other regional ratepayers. Furthermore, BPA must prepare for the very real possibility that some of the individual DSIs may not survive the competitive challenges facing the industry in the near term.
- ▶ Those who benefit from the power provided by the Columbia River hydroelectric system bear a responsibility to further the efficiency goals of the Northwest Power Act. Therefore, BPA's public utility customers should be required to prepare integrated resource plans (IRPs). These plans should be consistent with regionally developed guidelines stressing long-term, least-cost approaches such as conservation and renewable energy resources.
- ▶ A properly structured proposal recreating BPA as a government corporation could be a benefit for BPA and the region. However, the Clinton Administration should proceed very cautiously in developing a proposal to convert BPA to a government corporation. No clear consensus supporting such a proposal emerged from hearings held by the Department of Energy and the Northwest Power Planning Council earlier this year. There are legitimate concerns that the "side effects" from the enactment of a government corporation bill could conceivably cause harm far in excess of any benefits that might result from the legislation.
- ▶ The goal of debt-restructuring legislation—to stabilize BPA rates and resolve the "repayment reform" controversy—is sound. The repayment issue should be resolved in a manner that will not lead to any significant increase in BPA electric rates.
- ▶ The Northwest must unite behind a single vision for salmon recovery if the purposes of the Northwest Power Act are to be achieved. To the extent a regional consensus on salmon recovery exists, it is represented by the Northwest Power Planning Council's *Strategy for Salmon (Strategy)*. The *Strategy* is a comprehensive plan for rebuilding healthy and genetically diverse anadromous fish populations throughout the basin. It is aimed not only at recovering listed stocks and making future listings unnecessary, but at producing harvestable numbers of fish for both Indian and non-Indian harvesters. The *Strategy* was developed within the region with strong public participation and merits the region's support.
- ▶ No matter what measures are proposed in any future Endangered Species Act (ESA) recovery plan or biological opinion governing operation of the Columbia River system, the BPA and other Federal agencies continue to bear a responsibility to implement the *Strategy*. The *Strategy* should not be delayed while ESA recovery plans are developed or National Marine Fisheries Service's (NMFS) biological opinions are litigated. The National Marine Fisheries Service should work closely with the Council to ensure that its proposed actions are consistent with the *Strategy*.
- ▶ The causes of salmon decline are numerous, although the development of the Columbia basin's hydroelectric system almost certainly represents the single most significant human-caused source of

salmon mortality. Intuition as well as the available science argue that juvenile salmon need greater flows and river velocities during the migration period than those that prevail when the system is operated to maximize hydroelectric generation. Although a considerable degree of scientific uncertainty exists, it is imperative that the region act quickly and prudently to improve downstream passage conditions, relying on the best available science.

- ▶ The Army Corps of Engineers should use the money specifically appropriated for that purpose and begin design work on the necessary modifications to allow operation of John Day reservoir at minimum operating pool. Congress should provide the funding and direction necessary to expedite implementation of a John Day drawdown to minimum operating pool while providing mitigation to affected irrigators and others.
- ▶ As part of its effort to remain competitive, BPA should negotiate an agreement transferring its fish and wildlife functions to one or more fish and wildlife agencies. Such an agreement must be conditioned on thorough monitoring and evaluation of results, and tied to specific rebuilding targets, as well as a commitment on the part of the implementing entity to carry out fully the Council's *Strategy*.
- ▶ A common theme heard during the task force's deliberations was the lack of coordination between Federal agencies, State fish and wildlife managers, and Indian tribes. The Chair of the task force recommends one of two approaches to improving regional coordination in salmon-recovery efforts.

During the task force's September 24, 1993, hearing, the creation of a new regional entity responsible for basin planning and implementation was discussed. There may be merit in such an approach as long as the new planning effort: (1) incorporates existing plans and processes; (2) is not used as a pretext for delay in the implementation of the *Strategy*; (3) provides for full public participation; and (4) produces binding agreements that commit the participants to undertake the recommended measures.

Alternatively, NMFS, working with the Council, BPA and other Federal, State, tribal and private interests, could seek to develop a basin-wide conservation plan, using the *Strategy* as a framework. Such a plan should include rebuilding objectives and a timetable for implementation as well as a strong monitoring and adaptive management component. A basin-wide conservation plan, if fully implemented, could provide justification for the Secretary of Commerce to use his authority under §4(b) of the ESA to defer further ESA listings pending evaluation of the effectiveness of actions taken under the plan.

- ▶ The Federal agencies and the States should continue their efforts to reform water law so that conserved water may be dedicated to instream flows. The same logic that counts lost-generation opportunities caused by increased fish flows as lost revenues would consider water purchases for instream flows as an energy resource acquisition cost, not a fish and wildlife program cost. BPA should make this conceptual leap.

Federal policies that discourage water conservation should be reformed. BPA should develop alternatives to its present practice of discounting power for irrigation uses, including new power-pricing methodologies that provide incentives for water conservation.

CONCLUSION

The Bonneville Power Administration is at a crossroads. Decisions being made over the course of the next few years will have profound implications not only for BPA, but for the economy and culture of the Pacific Northwest.

In the final analysis, the Bonneville Power Administration's first responsibility is not to serve its Federal masters, the Governors of the four States in the Pacific Northwest region, or its utility and non-utility customers' individual interests; it is to serve the people of the Pacific Northwest. Whether BPA makes choices in the next two to three years that best serve the long-term interests of the people of the region remains to be seen.

The hearings held by the Bonneville Power Administration Task Force constitute what is arguably the most extensive congressional oversight of the BPA since the passage of the 1980 Northwest Power Act. Continuing informed congressional oversight is essential during this crucial period in BPA's history.

Sincerely,

PETER DEFAZIO, *Chair*

I. INTRODUCTION

The Task Force on Bonneville Power Administration of the Committee on Natural Resources convened on April 28, 1993. Over the following six months, the task force held five hearings on issues that will shape the future course of the Bonneville Power Administration. BPA has far-reaching responsibilities under the Pacific Northwest Electric Power Planning and Conservation Act¹ to meet the Pacific Northwest's electric power needs through sales of Federal power, while encouraging energy conservation and protecting, mitigating and enhancing regional fish and wildlife resources. All these purposes are to be met by BPA based upon recommendations of the Northwest Power Planning Council (Council), which was established under the Northwest Power Act to provide regional planning and participation in the Federal power system.²

The task force hearings were similarly wide-ranging. On April 28, the task force addressed BPA's FY 1994 budget, and its implications for BPA's near-term financial condition.³ The second hearing, held in Portland, Oregon, reviewed BPA's programs for power resources acquisition.⁴ The task force's next field hearing was held in Boise, Idaho, to examine BPA's participation in salmon restoration efforts in the Columbia River basin.⁵ The Task Force then traveled to Eugene, Oregon, to discuss BPA's plans to remain competitive in future power markets.⁶ The final hearing addressed BPA's legislative proposals to allow the agency to buy out its Federal debt and to convert itself into a government corporation.⁷

Upon review of the transcripts of these hearings, and other materials submitted to the task force, the Chair of the Committee on Natural Resources

¹ P.L. 96-501, 94 Stat. 2697, codified at 16 U.S.C. §§ 839-839h (hereinafter Northwest Power Act).

² Northwest Power Act § 4, 16 U.S.C. § 839b.

³ "BPA Proposed Fiscal Year 1994 Budget," Oversight Hearing before the Task Force on Bonneville Power Administration, Committee on Natural Resources, 103d Congress, 1st Session, Serial No. 103-20 Part I (April 28, 1993) (hereinafter Hearing Part I).

⁴ "BPA Electric Power Resources Acquisition," Oversight Hearing before the Task Force on Bonneville Power Administration, Committee on Natural Resources, 103d Congress, 1st Session, Serial No. 103-20 Part II (July 12, 1993) (hereinafter Hearing Part II).

⁵ "BPA Columbia River Salmon Restoration," Oversight Hearing before the Task Force on Bonneville Power Administration, Committee on Natural Resources, 103d Congress, 1st Session, Serial No. 103-20 Part III (September 24, 1993) (hereinafter Hearing Part III).

⁶ "BPA Competitiveness," Oversight Hearing before the Task Force on Bonneville Power Administration, Committee on Natural Resources, 103d Congress, 1st Session, Serial No. 103-20 Part IV (September 25, 1993) (hereinafter Hearing Part IV).

⁷ "BPA Proposals," Oversight Hearing before the Task Force on Bonneville Power Administration, Committee on Natural Resources, 103d Congress, 1st Session, Serial No. 103-20 Part V (October 28, 1993) (hereinafter Hearing Part V).

and the Chair of the task force concluded that a report bringing together the many disparate issues influencing the future of BPA, and providing guidance in directing the agency into the twenty-first century, could be a benefit to BPA and the Pacific Northwest.

II. BPA'S COMPETITIVENESS PROJECT

BPA is considering far-reaching changes in its marketing strategies and structure in response to real and perceived threats to the agency's competitive position. BPA is concerned that electric industry deregulation and the narrowing gap between its wholesale electric power rates and the cost of power from natural gas combined-cycle combustion turbines could cause a critical mass of BPA's customers either to seek other energy suppliers or develop their own resources. Such an abandonment of the Federal power resource would erode BPA's revenue base and undermine its ability to carry out its statutory mandates. It would also place the burden of Treasury debt repayment, fish and wildlife costs, and other BPA obligations on a smaller pool of utility customers.

Specifically, BPA's concerns are prompted by: the expansion of the Federal Energy Regulatory Commission's power to order wholesale wheeling; the growing interest on the part of some States in allowing and regulating retail wheeling; the increasing importance of independent power producers; and the decrease in the marginal cost of gas-fired generation. It is fair to say that the Nation's energy markets are undergoing significant change. It is also fair to say that the utility industry and BPA are uncertain about what the future holds.

In November 1993, BPA released a Draft Strategic Marketing Plan, which provided the most detailed description to that date of changes BPA is considering as part of its Competitiveness Project.⁸ Subsequently, the Council's staff completed an analysis of the Draft Strategic Marketing Plan. In February 1994, a Final Draft Strategic Marketing Plan was released.⁹

Some of the changes BPA is proposing include designing and implementing a tiered wholesale electric power rate, "unbundling" its melded services, and generally becoming less bureaucratic and more responsive to its customers' needs. BPA plans to implement many of these changes between 1994 and 1996.

A. TIERED WHOLESALE POWER RATES

BPA is engaged in discussions with its customers and other shareholders aimed at designing a tiered wholesale electric power rate. In its simplest form, a two-tiered rate would offer customers a first tier allocation consisting in whole or part of less expensive power generated by Federal base system resources, and a second tier priced to reflect the marginal cost of more expensive, new generating resources. By sending marginal cost price signals at the wholesale level, a tiered rate should encourage more efficient energy development and use.

⁸ Bonneville Power Administration, Strategic Marketing Plan, Draft, November 1993.

⁹ Bonneville Power Administration, Final Draft Strategic Marketing Plan, February 1994.

BPA considers a tiered rate to be a central element in its effort to "reinvent" its conservation program. The Final Draft Marketing Plan states that "[t]o the greatest extent possible, the conservation program will become a self supporting product line."¹⁰ BPA believes that a tiered rate will prompt BPA's utility customers to make their own investments in conservation, relieving BPA of much of its liability for the direct acquisition of conservation resources. BPA's description of conservation as a product line, as well as discussions with BPA staff, suggests that BPA believes it can sell conservation services to its utility customers, or loan BPA customers the funds needed to purchase energy-efficiency measures as an alternative to new utility-sponsored generation.

A properly designed tiered rate would force BPA customers to face the realities of the marketplace, i.e., the marginal cost of new resources, as they deal with load growth. However, the Council staff makes the point that in the absence of BPA-sponsored programs or incentives, a tiered rate would be unlikely to offer a sufficient incentive to cause utilities to invest in conservation as opposed to new generation.¹¹ BPA's analysis tends to support this view. In a February 1994 draft BPA document, BPA concludes that only about 40 aMW of a revised target of 608 aMW of conservation will result directly from implementing a tiered rate.¹²

B. UNBUNDLING BPA SERVICES

BPA now offers melded service packages to its various customer groups. Generally, these packages combine a number of discrete services into a single package at a single price. For example, BPA's firm power package for small customers includes transmission and shaping services, as well as transformation from network voltages to the customer's lower distribution voltage. The direct service industries—industrial customers that purchase power service directly from BPA without a utility intermediary—receive transmission services as well as a credit on their bills for the estimated value of certain portions of their contracted power that are deemed to be interruptible under some conditions.

BPA is proposing to identify and market a range of individual services for its partial-requirements customers and others who may prefer to provide for some but not all of their own needs. For example, a customer with its own generating resources may wish to purchase shaping services or power reserves from BPA. Others may wish to wheel power over BPA-owned transmission lines. BPA believes that offering an array of unbundled services will allow it to better tailor its services to its customers' needs. It also believes that it may be able to offer higher-value services that could enable customers to use or develop their own resources more efficiently.

The challenge for BPA will be to price these unbundled products in a manner that avoids cross-subsidization between customer groups and services

¹⁰ Bonneville Power Administration, Final Draft Strategic Marketing Plan, February 1994, p. 47.

¹¹ "Bonneville Marketing Plan Issue Briefing," Northwest Power Planning Council staff paper, p. 10.

¹² Document titled "Bonneville Power Administration, Conservation Reinvention, February 1994 (Draft)."

and continues to promote regional least-cost energy resource development. Unbundled services, if appropriately priced, could help deter BPA customers from uneconomical development of new generation resources.

In the worst case, however, unbundled services could facilitate uncoordinated and environmentally unsound resource development, imposing environmental and economic costs on the region as a whole at the same time that a tiered rate encourages utilities to look to suppliers other than BPA for their needs. It is not inconceivable that the combination of the two could serve to undermine the region's goals of coordinated and least-cost resource development.

BPA asserts its intention to design and price unbundled services in a manner that will promote the goals of the Northwest Power Act. It is interesting to note, however, that on the one hand BPA argues that open transmission access is one of the most significant forces driving its competitiveness concerns, while on the other hand BPA contends that its ability to set the price of transmission and related services—i.e., its control over the transmission grid—will enable it to promote regional planning and resource development.

C. BPA'S FUTURE PRICE COMPETITIVENESS

BPA's Competitiveness Project is driven in large part by the agency's concern that its wholesale electric power rates could soon be higher than the cost of competing energy resources. BPA's average priority firm (PF) rate is currently 26.8 mills for preference customers and 27.4 mills for residential exchange customers. BPA's PF-rate has declined in real terms since 1984. Even taking BPA's 1993 rate increase into account, BPA's current PF-rate is nearly 8 percent lower than the 1984 rate in real terms.¹³

Improvements in natural gas turbine technology and other changes in the market have substantially narrowed the gap between BPA's rates and the cost of gas-fired generation. The Tenaska Project, a gas-fired combustion turbine which is being acquired by BPA, is expected to provide power costing about 38 mills in 1993 levelized dollars, about 41 percent higher than the current PF-rate. Recent bids to construct cogeneration plants seem to offer very attractive terms, though uncertainty about future gas price increases or possible energy or carbon taxes remains.

For example, Clark public utility commissioners recently voted to begin final negotiations with a North Carolina-based company for construction of a 240 MW cogeneration plant whose estimated long-term costs, in 1994 levelized dollars, are about 30.1 mills/kwh.¹⁴ However, it should be noted that near-term costs for most generating projects are higher than the levelized costs and must be recovered through rates.

The Draft Marketing Plan includes projections of BPA's PF-rate and compares them to the projected costs of power from a gas-fired combined cycle combustion turbine. The Draft Marketing Plan's analysis shows the gap between the two rates remaining more or less constant in the medium forecasts, with the PF-rate remaining 5-10 mills lower in real terms than the

¹³ BPA Wholesale Power and Transmission Rate Projections and Historic Wholesale Power Rates, November 1993.

¹⁴ *Clearing Up*, May 2, 1994, p. 8.

cost of gas-fired power. However, when comparing the high PF-rate projection with the low gas-cost projection, BPA's rates can be shown to be marginally uncompetitive in 10-15 years.¹⁵

The November 1993 Draft Strategic Marketing Plan concludes that without dramatic changes, BPA's position as low-cost energy provider for the region is in "serious jeopardy."¹⁶ However, BPA included in its high PF-rate projection a number of costs that are not currently borne by the agency. For example, \$200 million a year was added to represent uncertainties such as possible BPA debt repayment reform. Significant generation losses from the hydroelectric system are assumed to account for contingencies such as increased fish flows.¹⁷ The Draft Marketing Plan also gives a projection of the PF-rate that includes a 5 mill "independence premium," in an attempt to quantify what BPA perceives as a widespread desire on the part of its utility customers to develop their own generating resources.

On the other hand, there is no corresponding projection that attempts to quantify the risk that a BPA utility customer assumes when it invests in its own generation or signs a long-term contract for thermally generated power. Nor is any value assigned to the fact that BPA currently has virtually no exposure to the financial risks associated with possible limits or taxes on carbon dioxide emissions. The analysis also fails to include the costs of wheeling, shaping, and reserves in the projected costs of power from a gas-fired combustion turbine. BPA estimates that wheeling costs alone could add as much as 10 percent to the cost of gas-fired generation.¹⁸

D. THE BPA "HASSLE FACTOR"

During its hearings, the task force heard a considerable amount of testimony about what has become known as the "hassle factor" inherent in dealing with BPA. Customers almost uniformly complain that BPA is excessively bureaucratic, and that its decisionmaking processes are hopelessly complex. In response to its customers' concerns and the concerns of the Chair of the task force, BPA has taken steps to begin to address this problem, including a simplification of its negotiating process and a proposal to restructure the organization.

An example of the BPA hassle factor can be found in Chairman DeFazio's congressional district. The Emerald People's Utility District (EPUD) had to spend nearly 4 years negotiating a third-party financing agreement for its conservation power plant proposal. More than 50 BPA employees were involved in the multi-stage process. The hurdles to completion of a billing credits agreement for EPUD's Short Mt. methane generation project were equally daunting.

¹⁵ Bonneville Power Administration, Final Draft Strategic Marketing Plan, February 1994, p. 38.

¹⁶ Bonneville Power Administration, Strategic Marketing Plan, Draft, November 1993, "BPA Competitiveness," p. 1.

¹⁷ Bonneville Power Administration, Final Draft Strategic Marketing Plan, February 1994, p. 38.

¹⁸ Ibid.

BPA's focus in the Competitiveness Project seems to have drifted away from this central and pressing problem. That point is illustrated in BPA's Final Draft Marketing Plan. The "Strategic Marketing Thrusts" section of the marketing plan seeks "[t]he creation of customer satisfaction through process enhancements, rate stabilization and product choice."¹⁹

However, the discussion in that section highlights not the need to address the hassle factor, but the need to "minimiz[e] . . . rate increases in the next six years." Only one sentence is given over to describing BPA's intention to "streamline its decisionmaking process and establish clear accountability."

BPA's importance to the Pacific Northwest's economy is ample reason for the agency to seek to minimize electric rate increases. But BPA's focus seems to have shifted too much toward rate issues—many of which are highly speculative—and away from the more immediate and pressing customer-satisfaction concerns.

E. POTENTIAL LOSS OF MARKET SHARE

The Final Draft Marketing Plan concludes that BPA is likely to lose 1,400 aMW of load within ten years unless the Marketing Plan's recommendations are implemented.²⁰ The possibilities that the DSIs and other customers might purchase power from new suppliers, that some large industrial customers will develop their own generation, and that sales in the California market will decline, all contribute to the load-loss scenario described in the Draft Marketing Plan. The Draft Marketing Plan suggests that even greater load-losses are possible, including the potential loss of 1,450 aMW from DSI closures and significantly greater losses due to other causes.

F. OTHER COMPETITIVENESS ISSUES

In addition to the issues evaluated in the agency's Draft Marketing Plan, the majority staff has identified three other issues that BPA should address in evaluating the agency's current and future competitiveness in the power marketplace.

1. Relationship to the Direct Service Industries

In addition to more traditional contracts with local utilities and government entities, BPA sells a significant amount of power to the DSIs. The price that the DSIs pay for BPA power is linked to the worldwide price of aluminum. BPA adopted this rate to increase the economic viability of the aluminum industry by lowering the DSIs' electricity rate when aluminum prices were low and increasing their rate when aluminum prices were high. BPA intends to keep the current variable rate in effect until June 1996.

Aluminum prices have plummeted in recent years and have been near historical lows for almost two years. Consequently, the current DSI rate is about 21 mills, considerably lower than the 26.8 mills PF-rate paid by preference customers.²¹ The Northwest Conservation Act Coalition (NCAC) estimates that at current world aluminum prices, the variable rate currently

¹⁹ Final Draft Strategic Marketing Plan, p. 45.

²⁰ Ibid., p. 42.

²¹ Ms. Leslie Ratcheye, BPA Washington DC Office, telephone conversation with task force staff, January 1994.

costs regional ratepayers about \$11 million per month.²² If world aluminum prices do not increase significantly, the DSI rate could cost regional ratepayers more than \$300 million by June 1996.²³

It must be noted that there have been extended periods since the variable rate was adopted in 1986 when high aluminum prices raised the DSI rate higher than the PF-rate. Regional ratepayers and non-DSI utility customers benefitted from these additional revenues. However, according to the majority staff's estimate, the crossover point where revenues losses from the rate exceeded revenue gains was reached in 1993.

Another special feature of the DSIs' contracts is the curtailment provision. In the utility industry the willingness of a customer to agree to curtail the amount of power it receives is a service that has considerable economic value. In consideration of the DSIs' agreement to curtail their use of power under certain circumstances, BPA has quantified the value of reserves (VOR) provided by the DSIs. The rate they pay for power has been adjusted to factor in the value of this service. Consequently, if the value assigned to these reserves is lowered, then the rate that the DSIs pay for power will increase.

BPA has not recalculated the VOR since 1987 and has agreed to freeze the 1987 VOR value until 1996. NCAC and others contend that the 1987 calculation is inaccurate and out-of-date since it is based in part on the cost of replacement power from a theoretical natural gas combustion turbine purchased at a prevailing interest rate of 14 percent and includes an overestimation of the amount of reserves actually provided by the DSIs. NCAC estimates that the subsidy for overpayment of the VOR is about \$40 million per year.²⁴

The question for the Northwest region is whether the regional economic benefits from the aluminum industry justify a continuation of the variable rate over the long term. The DSIs are a major economic force. According to the DSIs, they pay \$550 million in wages each year. The DSIs also provide important benefits to the Northwest's power system, including the provision of interruptible reserves and a significant demand for night-time load. At the same time, the low price the DSIs pay for power and the overvaluation of the reserves they provide impose an economic cost on the region by increasing the electricity rates paid by all other BPA customers. For example, if aluminum prices are stable, the revenue loss to BPA in FY 1994 due to the variable rate will be approximately \$132 million, which translates into a cost to non-DSI BPA ratepayers of about 5 percent of the price they pay for BPA

²² Hearing Part IV, p. 192 (testimony of Mr. K.C. Golden, executive director, Northwest Conservation Act Coalition).

²³ See BPA chart "Variable Industrial Rate—Cumulative Simple VI vs. IP" prepared at the request of the task force staff, who asked BPA staff to calculate the difference between charging the DSIs the VI rate and the IP rate paid by other industrial customers. BPA does not agree with these assumptions.

²⁴ Hearing Part IV, p. 123 (testimony of Mr. K.C. Golden).

electricity.²⁵ However, as noted earlier, the variable rate has proven to be a benefit over part of its history.

2. *Integrated Resource Planning*

In the Northwest Power Act, Congress recognized "the unique opportunity provided by the Federal Columbia River power system" as a means to encourage efficient energy use and the development of renewable resources in the Pacific Northwest.²⁶ These goals have been advanced by BPA's participation in regional energy planning and acquisition.

The deregulation of the Nation's energy markets could, however, undermine the Northwest Power Act's goal of regional least-cost energy planning and development, particularly if BPA retreats from its role as a regional resource provider. This loss of efficiency could be overcome by bringing more efficient decisions into localized power acquisition. Least-cost planning, or integrated resource planning, by BPA's public utility customers would provide a mechanism to achieve such localized least-cost planning, preserving the regional commitment to least-cost solutions.

The region's investor-owned utilities are required to prepare integrated resource plans. The Energy Policy Act of 1992 placed an IRP requirement on the public utility customers of the Western Area Power Administration (WAPA).²⁷ Due to the historically integrated nature of the Northwest's energy system and the planning requirements of the Northwest Power Act, BPA's public utility customers have not previously been required to engage in least-cost planning, though many already do so.

3. *Market Loss Potential and Extra-regional Power Sales*

The Regional Preference Act provides that BPA may sell outside the region only power that is surplus to the needs of the Pacific Northwest. Any contract to sell surplus power outside the region must include a call-back provision that allows the Administrator to suspend the sale of such power on 60-days notice when necessary to serve the energy requirements of any Pacific Northwest customer. For the purposes of the Act, the Pacific Northwest is generally defined as "the region consisting of the States of Oregon and Washington, the State of Montana west of the Continental Divide, and those portions of the States of Nevada, Utah and Wyoming within the Columbia drainage basin and of the State of Idaho as the Secretary may determine to be within the marketing area of the Federal Columbia River power system."²⁸

²⁵ Task force staff calculation:

$$\frac{(\$11\text{million}/\text{month}) \times (12\text{months})}{(\$25\text{million} \ast \ast)} = 5.28\%$$

* Council estimate of subsidy

** Hardy estimate of 1% rate of savings for each \$25 million saved

²⁶ 16 U.S.C. § 839.

²⁷ 42 U.S.C. §§ 7275-7276(c)

²⁸ 16 U.S.C. § 837(b).

If the load-loss scenario described in the Draft Marketing Plan becomes a reality, it may be advantageous for BPA and the region to reexamine the requirements that apply to the sale of surplus power outside the region. If BPA's fears of a 1,400 aMW load-loss become a reality, and extra-regional markets for that power exist, BPA could realize significant additional revenues if it were able to sell the power under more favorable contract terms. Put another way, if BPA were able to market surplus power under more favorable terms, it should be able to sell the power for at least as much as it stands to lose due to the projected load-losses.²⁹

G. FINDINGS AND RECOMMENDATIONS

- ▶ The Northwest Power Act sought to encourage conservation and efficient energy use and promote the development of renewable energy resources, thus assuring the Northwest an adequate, efficient and economical supply of power. The goals of the Northwest Power Act remain sound. In the final analysis, these goals are the yardstick by which BPA's new Marketing and Business Plans should be measured. A more competitive BPA could better achieve the Northwest Power Act's goals. However, the region's long-term interest in promoting efficient energy use, developing renewable energy resources, and rebuilding the Columbia River basin's incomparable salmon stocks should not be sacrificed solely in order to minimize electric rates in the short term.

- ▶ BPA's conclusion that its rates are imminently uncompetitive is not supported by the analysis in the Draft Marketing Plan or by testimony presented during the task force's hearings. That is not to say, however, that BPA's interest in maintaining its competitive position is not prudent and appropriate. BPA should make every effort to become a more efficient provider of conservation and energy resources, while continuing to satisfy its statutory mandates.

However, the BPA Draft Marketing Plan's analysis seems to have been structured to arrive at a predetermined conclusion, i.e., that BPA's rates would soon be uncompetitive when compared to the costs of gas-fired generation. The Council's analysis of the Draft Marketing Plan disagrees: "The examination of competitive cost issues in the marketing plan does not strongly support the conclusion that there is a current or likely problem with the competitiveness of BPA's rates for most of its customers."³⁰

BPA's excessive public concern over its prospects may have the unintended consequence of encouraging individual utilities to make questionable resource decisions based on their mistaken perception of BPA's unreliability as a low-cost energy supplier. Alternatively, customers may be encouraged to threaten such actions in order to extract rate concessions, to the detriment of other stakeholders. In either event, greater institutional self-confidence at BPA would benefit the region.

- ▶ A significant factor driving many of BPA's utility customers to consider alternative energy sources is the BPA hassle factor. BPA's

²⁹ This assumes that an extra-regional market will exist for BPA power priced within the projected range of the PF-rate even in the face of substantial Northwest load losses.

³⁰ Northwest Power Planning Council, Bonneville Marketing Plan Issue Briefing.

customers are immediately and legitimately dissatisfied with BPA's bureaucratic processes and cumbersome decisionmaking. However, BPA's focus seems to have shifted largely to the issue of price, and away from the customers' concerns about unwieldy BPA processes. BPA should refocus its efforts on responding to its customers' legitimate concerns about BPA's bureaucratic tendencies.

- ▶ A tiered rate should be one element in BPA's conservation acquisition strategy. However, BPA has apparently concluded that continued *regional* investment in energy efficiency is inconsistent with a strategy emphasizing improved price signals and new conservation-based products and services. That conclusion should be rejected. Market signals and direct investment should be mutually reinforcing parts of a regionally integrated energy conservation program.
- ▶ There are many potential responses to a wholesale tiered rate's marginal price signal. One of them is direct utility investment in energy-efficiency measures, which the Northwest Power Act seeks to promote. Other responses could include fuel switching, the curtailment of residential energy consumption in response to a retail tiered rate (sometimes referred to as "freezing in the dark"), or investments in new generation. Though some of these responses may be preferable to overbuilding new thermal generation capacity, they do not conform to the Northwest Power Act's purposes, which are to promote efficient energy use *and* provide an adequate and economical supply of power.
- ▶ BPA should implement tiered wholesale electric power rates and offer certain unbundled services to better serve customer needs. But BPA should not abandon direct investment in energy-efficiency measures, retreat from its fish and wildlife responsibilities, or decrease its commitment to improving its delivery of services in favor of untried "market mechanisms" until those mechanisms have been proven to be widely effective. The Northwest Power Act's mandate that the Administrator "acquire" conservation resources remains in effect.
- ▶ BPA must maintain a stable, long-term commitment to conservation if the region expects to reach the energy-efficiency goals set out in the Council's Conservation and Electric Power Plan. In 1993, BPA achieved record conservation savings of 52 aMW at an average weighted cost of 23 mills. Rather than abandon acquisition processes that are clearly working, BPA should build on its successes.

Although BPA's conservation performance improved markedly during 1993, the task force heard a considerable amount of testimony indicating that significant amounts of cost-effective conservation are not being acquired due to BPA budget constraints.³¹ Slashing conservation budgets will only exacerbate the problem.

However, greater decentralization of conservation acquisition would benefit BPA and the region, as long as it is combined with some level of regional support for local energy efficiency measures. As part of its continuing commitment to energy-efficiency, BPA should place particular emphasis on mechanisms that enable utility customers to develop their own conservation and renewable resources, consistent with the priorities

³¹ Hearing Part II, p. 124 (testimony of Ms. Sue Hickey).

of the Northwest Power Act, and in a manner that obviates the need for new BPA Treasury-borrowing authority. Such mechanisms could include long-term third-party financing agreements, billing credits, and the use of energy service companies.

- ▶ BPA needs to work with the Council on a comprehensive analysis of the economic costs and benefits to the Northwest region of the current variable rate/value of reserve structure. Based upon this analysis, a new rate structure should be designed for the DSIs that equitably balances the interests of the DSIs and all other regional ratepayers. The assumptions underlying the calculated value of reserves are clearly out-of-date and need to be revised. Furthermore, BPA must prepare for the very real possibility that some of the individual DSIs may not survive the competitive challenges facing the industry in the near term.

During new DSI power sales contract negotiations, BPA should examine the possibilities of increased interruptibility, shorter contract periods, and any other provisions that may be deemed to be necessary to protect BPA's ratepayers and non-DSI customers from the potential disruptions that sudden DSI load-loss may cause.

- ▶ Those who benefit from the power provided by the Columbia River hydroelectric system bear a responsibility to further the efficiency goals of the Act. Therefore, BPA's public utility customers should be required to prepare integrated resource plans as a pre-condition to independent resource acquisition. The requirement could either be laid upon BPA's customers by legislative mandate or as an obligation in their power sales contracts. Technical assistance should be provided to smaller utilities that lack the resources to undertake an IRP exercise.

The majority staff notes that the Council, in a letter to task force Chairman DeFazio, stated:

"[M]embers of the Public Power Council are willing to accept a contractual obligation, if properly structured, to prepare and comply with an integrated resource plan as a condition for independent resource acquisition. The power sales contracts are currently being rewritten, affording a timely opportunity to develop and incorporate an IRP provision."³²

BPA should commence discussions with its public utility customers, the Northwest Power Planning Council and other interested parties toward the development of regionally acceptable IRP guidelines. IRPs should promote the goals of the regional power plan. They should be developed in an open and public process. Mandatory penalties (such as a power surcharge) or the use of incentives (such as discounted costs of services) should be employed to enforce compliance with regionally developed IRP guidelines. It may be necessary to give the Council authority to make consistency determinations once the IRP requirements are incorporated into the power-sales contracts.

If progress is not made toward the development of acceptable contract provisions, a legislative mandate should be placed on BPA's

³² Letter from Mr. William K. Drummond to Chairman DeFazio, February 24, 1994.

publicly owned utility customers, similar to the one placed on the Western Area Power Administration public utility customers in the Energy Policy Act of 1992.

- ▶ The discussion above of regional preference issues should not be construed as an endorsement of eliminating regional preference. To the contrary, regional preference provides significant benefits to BPA customers and their ratepayers. But a financially insolvent BPA cannot serve the region, fulfill its mandates under the Northwest Power Act, or satisfy its financial obligations to the U.S. Treasury. If regional preference entities effectively abandon BPA by signing long-term power-purchase contracts with other suppliers, BPA's remaining customers will have a stake in allowing BPA to maximize revenues from extra-regional surplus-power sales.

III. RESTRUCTURING BPA

Over the past year, two major proposals have emerged that could significantly alter BPA's relationship to the Federal Government: refinancing BPA's appropriated Treasury debt by allowing BPA to pay off the Federal investment in one lump sum using privately borrowed funds; and recreating BPA as a government corporation. Each of these proposals is intended to assist BPA in better meeting regional needs, with less interference by the Federal Government. However, each of these proposals as currently designed raises questions regarding BPA's accountability.

A. REFINANCING THE BPA DEBT

The budget proposals of three consecutive Presidents have contained debt-repayment reform proposals aimed at changing BPA's repayment obligation to the U.S. Treasury. Though different in scope and impact, each has proposed substantial increases in project interest rates and conversion to a fixed schedule of annual repayment. The last Bush Administration proposal would have cost Pacific Northwest ratepayers about \$2.6 billion.

The recurring threat of debt-repayment reform represents one of the most significant uncertainties facing BPA and its customers. Resolving this issue in a manner fair both to the ratepayers in the Northwest and the U.S. Treasury will better enable BPA to serve the region and continue to satisfy its obligations to the Treasury.

The "Bonneville Power Administration Repayment Bonds Act" was included in the Clinton Administration "Reinventing Government" legislation (H.R. 3400).³³ As introduced, this legislation authorized BPA to borrow funds on the private market in order to make a single payment to the U.S. Treasury that would discharge all of BPA's obligations for appropriated Treasury debt.

On October 28, 1993, the task force conducted a hearing on this legislative proposal. The language submitted by the Administration had a number of technical problems. The Congressional Budget Office (CBO) scored the BPA refinancing legislation as a budget "cost" due to the increased cost of borrowing from private markets as opposed to current Treasury-borrowing practices. Because of the budget cost found by CBO, the committee could only approve the BPA refinancing proposal if equivalent budget "savings" were found to offset these costs. In addition, a number of provisions included in the bill may have had potentially far-reaching, if unintended, effects. These concerns made it impracticable for the committee to act on the legislation.

Unfortunately, the Chair of the task force was left with no choice but to request that the Committee on Natural Resources refrain from acting on the Administration proposal before the end of the committee's brief referral of

³³ H.R. 3400, Part 1, Subtitle C, Title IV.

H.R. 3400. The committee complied with this request and replaced the BPA refinancing provision with study language intended to serve as a placeholder for future efforts by the committee on the issue. The Chair of the task force and other members of the region's congressional delegation are continuing discussions with the Administration and parties in the region over a possible Treasury debt buy-out proposal.

B. GOVERNMENT CORPORATION

On December 17, 1993, BPA released a draft bill proposing to convert BPA to a government corporation. Both the Northwest Power Planning Council and the Department of Energy conducted public hearings to obtain comments on the draft bill. Many concerns were raised regarding the possible unintended consequences of such a change.

1. *Accountability*

Converting BPA into a government corporation could reduce the accountability of the agency to the citizens of the Northwest, its utility customers, the Northwest Power Planning Council, the executive branch, and the Congress. For example, the Council staff issue paper on the December 17 draft bill states that the bill would remove BPA's budget entirely from the annual congressional appropriations process. Although there are significant drawbacks to being part of the appropriations/budget process, it remains a primary avenue of access for regional interests seeking review or modification of BPA policies.

In addition, BPA already has more autonomy than the other Federal Power Marketing Administrations (PMAs) because it is self-financing and has the authority to borrow funds directly from the Federal Treasury. Unlike the other PMAs, the agency can spend funds and incur most obligations without an annual appropriation, although certain planned expenditures—such as for major transmission lines and fish and wildlife facilities with a useful life greater than 15 years and a cost greater than \$1 million—must be approved in an appropriations bill.

2. *Environmental Responsibility*

Another concern is the lack of a precedent for giving a government corporation environmental responsibilities, such as BPA's responsibility to help restore fish and wildlife resources in the Columbia River basin. Careful deliberation should be devoted to the issue of whether a corporate structure is best suited to carry out the environmental mandates of the Northwest Power Act.

In this regard, it should be noted that when Congress recently converted the Department of Energy uranium enrichment complex into a government corporation in the Energy Policy Act of 1992 it did *not* assign the new government corporation responsibility for cleanup of past contamination of the enrichment complex. Congress withheld this environmental responsibility due to concerns that the cleanup duties would not be consistent with the profit-maximizing mission of a corporation. Instead, cleanup responsibility remained with the Federal Government, and a fee on nuclear electricity was imposed to finance these costs.

The draft incorporation legislation would also allow BPA to represent itself in legal proceedings. The result could be that in some proceedings, including those in which other agencies of the Federal Government are

parties, BPA would not necessarily be required to take positions consistent with broader Federal policy.

3. *Administrative Savings*

BPA estimates that legislation making BPA a government corporation would allow BPA to reduce its permanent and contracted work force by a total of 1,000 full time equivalent (FTE) positions and save the agency \$100,580,000 a year. BPA estimates that it could achieve savings of \$66,310,000 and reduce its work force by 650 FTE positions in the absence of government corporation legislation.³⁴ The fiscal savings possible through legislation include greater flexibility in personnel and procurement practices, and a decrease in budgeting and reporting requirements BPA feels are a hindrance to its mission.

4. *Other Considerations*

The December 17 draft bill states that one of the purposes of the new corporation is "to operate as a commercial enterprise." The unanswered question is whether BPA could use its new corporate authorities along with its existing broad powers as a governmental entity to hinder competition. In addition, many of BPA's responsibilities, including its fish and wildlife obligations, could be considered to be of secondary importance to a "commercial enterprise."

The draft legislation also creates a new exception to the Freedom of Information Act that would allow BPA to refuse to disclose any information it defines as "government commercial information." BPA has been criticized in the past for unnecessarily withholding information from the Council, Congress, and the public. In the task force's July 12, 1993, hearing, the Chair criticized BPA for failing to share with the Council information relating to natural-gas costs for the Tenaska natural gas combustion turbine. He also criticized the Council for approving the project without having reviewed the data being held in confidentiality by BPA.³⁵ As drafted, the Freedom of Information Act exception is overly broad, perhaps even unnecessary.

Finally, in many instances throughout the draft, unspecified laws are made inapplicable to the corporation. This makes it very difficult for members of the public to understand the likely impacts of the legislation.

C. FINDINGS AND RECOMMENDATIONS

- ▶ The goal of debt-restructuring legislation—to stabilize BPA rates and resolve the "repayment reform" controversy—is sound. The repayment issue should be resolved in a manner that will (1) provide long-term repayment certainty for BPA and its customers; (2) minimize near-term BPA rate impacts; and (3) not cause any increase in the Federal deficit as determined by the Congressional Budget Office.
- ▶ Despite failings by BPA, such as exceeding the annual borrowing limit recommended by the Appropriations Committees in the report accompanying the Fiscal Year 1993 Appropriations Act, the independence

³⁴ "Savings from BPA Incorporation vs. Existing Situation and Administrative Action," Bonneville Power Administration memo, January 6, 1994.

³⁵ Hearing Part II, p. 111.

the agency has under current law should be retained. BPA requires flexibility to meet its legal obligations. However, a conclusive case has not yet been made that even more independence is necessary or appropriate.

- ▶ A properly structured government corporation proposal could be a benefit for BPA and the region. However, the Administration should proceed very cautiously in developing a proposal to convert BPA to a government corporation. No clear consensus supporting such a proposal emerged from hearings held by the Department of Energy and the Council earlier this year. There are legitimate concerns that the "side effects" from the enactment of a government corporation bill could conceivably cause harm far in excess of any benefits that might result from the legislation.
- ▶ The December 17 draft corporation bill would give BPA new authorities that exceed those the agency identified as necessary to make itself more efficient and competitive. BPA must take care to draft any new version of the corporation bill narrowly, to achieve the goals of the legislation as represented by BPA and only those goals. Where the needs of a BPA corporation require an exemption from a Federal statute, the statute should be specifically identified.
- ▶ Discussion regarding the potential savings from the corporation should be kept in perspective in relation to savings that can be achieved without legislation. BPA has identified \$66 million in annual savings that it has the authority to achieve *now* under current law. BPA and the Administration should aggressively pursue these savings as well as other savings identified in this report. According to BPA, \$34 million in additional annual savings would result from corporate status. Of course, a corporation could also give BPA greater flexibility in meeting the demands of changing energy markets and customer concerns. It is difficult to place a value on the benefits such flexibility could provide.

IV. CUTTING COSTS—CUTTING RATES

BPA is currently experiencing severe financial pressures due to a wide variety of factors, including a series of extremely dry years, increased electric demand, low aluminum prices,³⁶ failure to increase rates in the past, and modifications of power operations to reduce harm to endangered salmon. As a consequence, BPA raised its rates about 14 percent in October 1993.

As noted above, even this recent rate increase has not raised BPA's rates to their 1984 level in real terms. However, the rate increase has led BPA and many others concerned with regional power matters to embark on an effort to cut BPA costs and make BPA more "competitive." According to BPA Administrator Randy Hardy, every \$25 million that BPA saves roughly translates into reducing electricity rates by 1 percentage point.³⁷

The majority staff has identified about \$150 million in potential annual budget savings that do *not* compromise BPA's commitment to sound environmental stewardship. In a number of instances, these budget savings could also advance important Northwest Power Act goals such as encouraging more efficient use of regional water and power resources. BPA is properly considering many additional savings and efficiencies as part of its Competitiveness Project.

A. WASHINGTON PUBLIC POWER SUPPLY SYSTEM

Proponents of cutting BPA costs often fail to focus on the fact that approximately 25 percent of BPA's budget is devoted to paying for debt service, operations, and "mothballing" of the three Washington Public Power System nuclear plants. The WPPSS fiasco occurred because BPA in effect agreed to pay for all of the costs of three nuclear plants built by WPPSS. Only one of these three plants has been completed (WNP-2) and it has a very poor operating record, though the plant's management has been able to substantially improve the plant's capacity during the last year. The other two (WNP-1 and WNP-3) were never completed, but BPA continues to pay for the debt incurred on their construction and for the cost of mothballing them in case their power is ever needed. Between 1979 and 1983 BPA's priority firm electric power rate increased by about 600 percent in nominal terms, largely due to the costs of WPPSS.³⁸

According to data provided by BPA and the Congressional Research Service (CRS), the costs of running the WPPSS WNP-2 reactor are far higher than the nuclear industry average for similar plants. WPPSS costs are further increased by wasteful spending on mothballing the incomplete WNP-1

³⁶ As discussed on p. 7 above, the DSI power rate is linked to the price of aluminum.

³⁷ Hearing Part I, p. 18 (testimony of Mr. Randall W. Hardy).

³⁸ *Wholesale Power and Transmission Rate Projections and Historic Wholesale Power Rates 1939-1992*, Bonneville Power Administration, November 1993.

and WNP-3 reactors. Despite the apparent inefficiencies in WNP-2 operations, BPA has *never* formally disapproved *any* WNP-2 expenses.³⁹

CRS estimates that the average industry capital expenditure for reactors comparable to WNP-2 is about \$23 million per year.⁴⁰ In 1993, WNP-2 capital expenditures were almost \$80 million.⁴¹ For FY 1994-1996 capital additions are budgeted at approximately \$50 million per year, and for FY 1997-2003 capital additions are estimated to be \$35-\$40 million.⁴² Some of the 1993 costs were one-time only costs.⁴³ Nonetheless, if WNP-2 capital expenditures were reduced to the industry average, annual savings of between \$10 million and \$25 million per year would result in FY 1995 and FY 1996.

WPPSS currently has approximately 1,550 full-time staff for the WNP-2 reactor.⁴⁴ CRS estimates that the average staffing for comparable reactors is 1,250 positions.⁴⁵ The average annual cost per staffer at WNP-2 is \$64,573.⁴⁶ Consequently, if WNP-2 staffing is brought down to the industry average, eliminating 300 extra positions, savings of about \$20 million per year would result.

In April 1993, BPA initiated efforts to terminate WNP-1 and WNP-3; however, the WPPSS Board has yet to vote for termination. Thus, the continuing cost of mothballing the WNP-1 and WNP-3 reactors remains at about \$10.5 million per year, half of which is paid from BPA revenues, the other half from the WNP-1 construction fund.⁴⁷ In addition to annual savings, termination of WNP-1 and WNP-3 would also yield one-time savings from the sale of as much as \$100 million of reactor fuel that would no longer be needed.⁴⁸

Because so much of the BPA budget is devoted to WPPSS, the majority staff has devoted considerable attention to identifying savings in this area. Of

³⁹ Hearing Part I, p. 93 (supplement to the statement of Mr. Randall W. Hardy).

⁴⁰ Congressional Research Service, "Nuclear Power Plant Costs and Staffing," Memorandum to Committee on Natural Resources by Mark Holt, Specialist in Energy Policy, Environment and Natural Resources Policy Division, January 5, 1994 (hereinafter CRS January 5 Memo).

⁴¹ Hearing Part I, p. 96 (supplement to statement of Mr. Randall W. Hardy).

⁴² CRS January 5 Memo.

⁴³ According to BPA staff, \$24 million of the \$80 million was an investment in increased plant capacity, which BPA considers a resource acquisition cost, and \$17 million is attributable to the settlement of a lawsuit between the WPPSS and General Electric.

⁴⁴ Congressional Research Service, "Additional WNP-2 Cost and Staffing Information," Memorandum to Committee on Natural Resources by Mark Holt, Specialist in Energy Policy, Environment and Natural Resources Division, January 24, 1994.

⁴⁵ *Ibid.*

⁴⁶ *Ibid.*

⁴⁷ Hearing Part I, p. 92 (supplement to statement of Mr. Randall W. Hardy).

⁴⁸ *Ibid.*

course, the fundamental mistake that BPA made many years ago to back these plants financially cannot be reversed, and the region will continue to live with the consequences for many decades. Nevertheless, considerable opportunities for savings do exist within WPPSS.

B. IRRIGATION POWER RATES

1. *Bureau of Reclamation*

One of the largest consumers of federally generated hydropower in the Northwest is the Federal Bureau of Reclamation (BuRec), which uses the electricity to pump water through its irrigation distribution systems. BuRec estimates that it uses about 480 MW of hydropower for pumping.⁴⁹ The price that BuRec pays for power is passed on to its irrigation customers through operation and maintenance payments or a separate energy charge.

The rate that BuRec pays for this power—and passes through to its customers—is generally set by the Secretary of the Interior under Reclamation law. The price BuRec pays varies depending upon the project; however, in all cases it is less than half the 26.8 mill priority firm rate paid by most BPA customers.⁵⁰ In fact, over two-thirds of the power consumed by BuRec is used in the Columbia Basin Project and is sold for 0.95 mills, less than one twenty-eighth of the 26.8 mill priority firm rate.⁵¹ Charging BuRec the same rate for power that other BPA customers pay would raise approximately \$32 million a year.

Before the 600 percent BPA rate increase that resulted in the early 1980s from the WPPSS fiasco, the disparity between the electricity price paid by BuRec and the price paid by other BPA customers was not a major concern. But by 1994 this disparity has grown to the point where other regional power consumers find themselves paying the lion's share of the costs for BuRec power.

In addition, the extremely low price for irrigation pumping electricity also encourages the increased use of water resources that might otherwise be used for power generation or other purposes. BPA has not quantified the amount of power generation lost due to BuRec's irrigation pumping discount. However, even if the low rate BuRec pays for power causes only a moderate increase in water use and consequent loss of power generation, considerable revenue is lost to the region. Finally, more efficient water use would also assist efforts to restore salmon runs.

2. *Private Irrigation Discount*

In addition to the extremely low price BuRec pays for power used for pumping purposes, BPA provides discounts to individual irrigators who use electricity for water pumping in their own irrigation distribution systems. BPA will forego a total \$27.018 million in FY 1994 and FY 1995 due to the

⁴⁹ Mr. Al Bolin, Bureau of Reclamation, Boise Office, telephone conversation with task force staff, February 1994.

⁵⁰ Bureau of Reclamation, Boise Office, written response to task force inquiry, February 11, 1994.

⁵¹ Bureau of Reclamation, written response to task force inquiry, February 9, 1994.

irrigation discount.⁵² In order to understand the magnitude of the water depletion attributable to irrigation withdrawals in the Columbia River basin, and the theoretical resulting lost power-generation opportunities, the task force asked BPA to provide an estimate of the amount of foregone revenue attributable to water withdrawals using discounted BPA-supplied power. BPA's estimate of lost power sale revenues attributable to irrigation withdrawals was \$150-\$300 million per year.⁵³

Proponents of the irrigation discount argue that it helps increase energy consumption in the summer when other BPA loads are low and BPA needs to increase flows for fish purposes. This argument, however, ignores the fact that the value of this power to the region can be maximized through exchange agreements with Southwest utilities, in which BPA agrees to supply power to meet their peak summer loads in exchange for the Southwest utilities providing power to the Northwest to meet peak winter loads. Thus, by increasing electricity consumption for irrigation pumping, the discount in some cases prevents more valuable power exchanges.

In addition, like the low rates that the Bureau of Reclamation pays for power, the irrigation discount may have the effect of increasing water use, or at the very least, offering no incentive for more efficient water use. Again, increased water use has a variety of negative impacts on the region, including diminishing hydroelectric production and increasing the cost and complexity of restoring salmon runs.

It should be noted that BPA's Draft Marketing Plan assumes the elimination of the irrigation discount.

C. SUPER GOOD CENTS

BPA's "Super Good Cents" program provides a \$2,500 payment toward the construction of energy-efficient all-electric homes. This payment is provided throughout the BPA service territory, including areas that are currently served by natural gas. According to BPA, between FY 1985 and FY 1992 it spent about \$8.4 million on Super Good Cents subsidies for new construction in areas where gas is currently available.⁵⁴ BPA estimates that it will spend \$3-\$5 million per year on these payments from FY 1994 to FY 1998.⁵⁵

This has the effect of encouraging builders, who are economically compelled to minimize up-front construction costs, to install electric space and water heating systems in new homes, even when it would be more prudent to install gas systems. As a result, Super Good Cents discourages the use of natural gas for space and water heating in new homes constructed in the Northwest. This in turn stimulates new demand for electricity, which requires BPA to acquire costly new resources contrary to the energy conservation mandate of the Northwest Power Act.

⁵² Hearing Part I, p. 88 (supplement to the statement of Mr. Randall W. Hardy).

⁵³ Hearing Part III, pp. 57-58 (prepared statement of Mr. Randall W. Hardy).

⁵⁴ Hearing Part I, p. 99 (supplement to the statement of Mr. Randall W. Hardy).

⁵⁵ *Ibid.*

Ironically, BPA intends to meet part of the increased demand for electricity in the Northwest by purchasing the output of the proposed Tenaska natural gas turbines. It must be noted that direct gas use in the home produces about two times more energy than burning the same gas in a turbine to produce electricity that is subsequently used for space- or water-heating purposes.

In defense of its practice of providing electric heating subsidies in areas served by natural gas, BPA claims that 2.0 MW of efficiencies would be lost in multifamily construction if the payments were canceled.⁵⁶ BPA neglects to mention, however, the cost savings that would result from the reduced demand for electricity if gas is utilized for heating purposes. It is also interesting that BPA does not claim that any electrical efficiencies would be lost from terminating Super Good Cents payments for single-family construction in areas currently served by natural gas.

BPA asserts that market forces are sufficient to encourage appropriate fuel switching to natural gas, without considering the market barriers that exist to prevent customers from using gas. For example, according to the NCAC, a number of BPA's customer utilities require their customers that receive weatherization financing to agree not to convert to gas. This prompts NCAC to ask the following question, "If it is worth paying a customer \$2,000 to reduce their heating load on the electric system by 30 percent, through weatherization, why discourage that customer from reducing their heating load by 100 percent for the same price?"⁵⁷

D. FINDINGS AND RECOMMENDATIONS

As part of its "reinvention" effort, BPA has identified \$66 million in annual administrative savings that it has the authority to accomplish under current law, without becoming a government corporation. These savings include personnel cuts, procurement changes and other reforms. However, current efforts to cut BPA costs could ultimately compromise important regional goals established by the Northwest Power Act, such as energy efficiency and the protection of fish and wildlife resources.

What follows are budget savings that BPA could achieve that would produce approximately \$150.5 million of savings per year starting in 1995. BPA's proposed savings combined with the potential savings of up to \$150.5 million identified by the majority staff can significantly reduce BPA's costs and rates. BPA should move to implement as many of these savings as possible.

Strongly Recommended Savings:

► *WPPSS: Total Annual Savings—\$55.5 million*

About \$55 million in annual savings could be gained through improving the efficiency of WPPSS. If WNP-2 costs cannot be reduced—and safety improved—then BPA and the region should consider the option of permanently shutting down the reactor. At any rate, BPA must use the tools at its disposal to reduce wasteful spending at WPPSS.

⁵⁶ Ibid.

⁵⁷ Hearing Part II, p. 170 (attachment to prepared statement of Mr. K.C. Golden, Northwest Conservation Act Coalition).

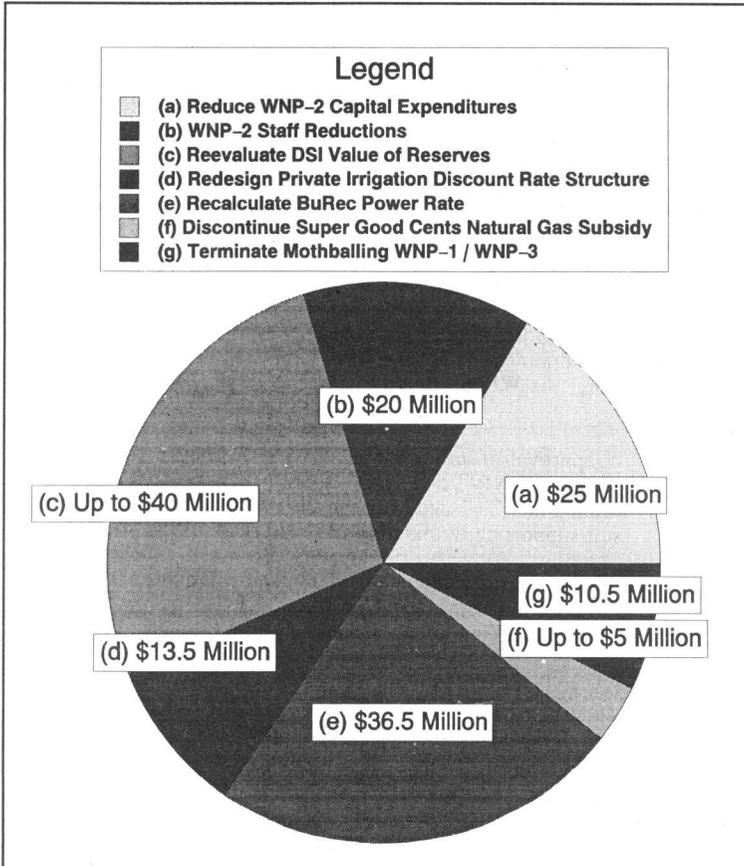


Figure 1. Strongly Recommended and Other Potential Savings Totaling \$150.5 Million

BPA should insist upon the following savings in WPPSS expenses:

- *WNP-2 Capital Expenditures: Annual Savings—\$25 million*

It should be noted that the new manager of WPPSS, William Council, plans to reduce WNP-2 capital expenditures to below the industry average. BPA should hold him to his stated goal.

- *WNP-2 Staff: Annual Savings—\$20 million*

BPA, and the region, can no longer afford to permit WPPSS to run a jobs program. Again, it should be noted that Mr. Council is attempting to reduce the size of the WNP-2 staff.

- *Terminate Mothballing: Annual Savings—\$10.5 million*

Continuation of mothballing is unjustifiable. The practice should have been terminated years ago when it became apparent that completing WNP-1 and WNP-3 would be far more expensive than a wide range of other energy resources available in the Northwest. The recent closure of the Trojan reactor reinforces the conclusion that additional nuclear generation is not economically viable in the Pacific Northwest.

Recently, WPPSS has announced that it is exploring the option of completing WNP-1, using a mixture of uranium and weapons grade plutonium to fuel both WNP-1 and WNP-2. The decision to end BPA funding of mothballing should not be delayed on account of this far-fetched proposal, which may just be a tactic to delay the mothballing decision.

If the WPPSS Board does not vote for termination by May 1994 as requested by Administrator Hardy, BPA should take a series of unilateral actions to force the WPPSS Board to agree to termination, including the following:

- disapproval of any proposed WPPSS budget that continues to preserve WNP-1 and WNP-3; and
- joining the Clark and Mason utilities as a party plaintiff in their suit supporting termination of WNP-1 and WNP-3.

BPA should also consider other steps, including filing a separate lawsuit barring WPPSS from using any Construction Fund money to pay for preservation and seeking State legislation to terminate WNP-1 and WNP-3.

If BPA and WPPSS do not act as expeditiously as possible to terminate mothballing then it may be necessary for Congress to address the issue through legislation that would remove WNP-1 and WNP-3 from the Federal base system.

- ▶ *Super Good Cents Payments: Annual Savings—Up to \$5 million*

BPA should stop making Super Good Cents payments in areas served by natural gas. At bottom, BPA's reluctance to discontinue Super Good Cents payments in areas served by natural gas results from pressure by some of its utility customers to *increase* electricity demand and utility revenues. BPA can no longer afford to support this type of subsidy at the expense of regional ratepayers.

Other Potential Savings:

Along with the strongly recommended savings, the majority staff has identified certain costs to BPA associated with the lower wholesale rates offered to BPA's irrigation utility customers and the Bureau of Reclamation. Whether these subsidies should be discontinued or modified in order to provide incentives for greater water conservation is an open question, but one that should be addressed. For the purposes of comparison, this report includes the estimated savings from a complete elimination of the known irrigation subsidies.

Another open question is the appropriate value of the DSI reserves. Though the reserves are clearly overvalued at present, the majority staff does not take a position as to their appropriate value. Again, for the purposes of

comparison, this report uses figures provided during the task force's hearings to estimate the savings that could be attained by recalculating the value of the DSI reserves.

► *BuRec Power Rate: Annual Savings—\$36.5 million*

The Secretary of the Interior should reevaluate the policies that have led to BuRec's paying less than 1 mill per kwh when most customers are paying over 26.8 mills. Minimally, the agency should seek to set rates that encourage energy and water conservation in the region. If necessary, the agency should consider seeking congressional authorization to do so.

► *Private Irrigation Discount: Annual Savings—\$13.5 million*

The discount for private irrigation pumping, which tends to encourage increased electricity and water use, also runs contrary to the Northwest Power Act's mandate to encourage efficient use of energy. At a time when BPA is considering establishing a tiered rate that will charge customers a higher rate as their consumption increases, the results will be undercut by the irrigation discount, which actually encourages increased consumption. It also makes little sense to perpetuate a rate structure that offers no incentive for water conservation when the region is trying to provide more water for fish flows. As noted, BPA plans to eliminate the irrigation discount as it is now structured. BPA should design a rate structure in its place that discourages excessive energy and water consumption and encourages new conservation efforts.

More efficient water use would also translate into additional revenues for BPA from the sale of power generated by increased flows.

► *Value of DSI Reserves: Annual Savings—Up to \$40 million*

As mentioned on page 8, the value of the interruptible portions of the DSI loads is clearly out of date and should be reevaluated. The potential savings to BPA and its ratepayers range as high as \$40 million.

V. SALMON RECOVERY

The Northwest Power Act requires that the Columbia basin's fish and wildlife resources receive equitable treatment with respect to power production.⁵⁸ As with planning a strategy for meeting regional power demand into the next century, planning a strategy for restoring and maintaining Columbia basin salmon stocks into the next century must begin with regionwide participation and coordination under the Northwest Power Act. Although a regional fish and wildlife plan has been developed, efforts to implement that plan have been only partially successful.

The task force's examination of this issue focused on the *Strategy for Salmon* developed by the Northwest Power Planning Council⁵⁹ and efforts by BPA and others to carry out the *Strategy*. The plan's goal is "the doubling of the total number of adult salmon and steelhead in the Columbia basin as fast as possible without further loss of biological diversity among or within anadromous and resident fish populations."⁶⁰ The Endangered Species Act requires that these efforts be supplemented by the National Marine Fisheries Service's adoption of a recovery plan for those salmon stocks listed as endangered or threatened under Federal law.⁶¹

A. STATUS OF THE SALMON

Estimates of Columbia basin salmon runs predating European settlement range from 7.5–16 million.⁶² Those stocks have now been reduced to fewer than 2.5 million, more than 70 percent of which come from hatcheries.⁶³

⁵⁸ Section 4(h)(11)(A)(i) of the Pacific Northwest Electric Power Planning and Conservation Act requires that the BPA Administrator exercise his responsibilities in a manner that "provides equitable treatment for . . . fish and wildlife . . ." Northwest Power Planning Act § 2, 16 U.S.C. § 839.

⁵⁹ Northwest Power Planning Council, *Strategy for Salmon*, Vols. I & II, Doc. Nos. 92-21 and 92-21A (October 1992).

⁶⁰ *Ibid.*, section 2.1A, Vol. II, p. 18.

⁶¹ NMFS' Endangered Species Act responsibilities have given it a role in salmon restoration at three different stages: (1) listing individual salmon stocks as threatened or endangered species; (2) issuing "biological opinions" that determine whether proposed federal agency actions will "jeopardize" the survival of listed species; and (3) developing recovery plans for listed species. ESA §§ 4, 7, 16 U.S.C. §§ 1533, 1536.

⁶² Congressional Research Service, "Salmon in the Pacific Northwest: Endangered Species Act Issues," Issue Brief by Eugene H. Buck, Amy Abel, and Betsy Cody, Environment and Natural Resources Policy Division, p. 1, April 5, 1993.

⁶³ *Ibid.*

The major factors that have contributed to this depletion have been described as the "four Hs":

- poor hatchery management;
- fisheries harvest;
- hydropower dam construction and operation; and
- habitat degradation due to many activities in the watershed, including pollution, which reduce salmon health and survival, and water diversions for irrigated agriculture.

Despite regional efforts to restore and maintain wild salmon stocks, NMFS listed the Snake River sockeye as "endangered" under the Federal Endangered Species Act in November 1991, followed by separate "threatened" listings for two Snake River chinook stocks in April 1992. During 1993, regional conservationists filed two additional petitions with NMFS, requesting ESA listing of three additional salmon stocks: (1) the mid-Columbia chinook populations; (2) the entire southern range of coho;⁶⁴ and (3) steelhead populations throughout the basin.

Further endangered species listings may well occur. In early 1992, the American Fisheries Society reported 214 separate native salmon stocks at risk in California, Washington, Oregon, and Idaho.⁶⁵ Since NMFS applies different standards from those used by the Fisheries Society to determine whether various salmon runs should be treated as separate species under the Endangered Species Act, the number of endangered species listings will be far lower than 214. Once a species is listed, however, NMFS may address the independent needs of the various populations of the species in developing a species recovery plan.

Two potentially inconsistent goals have guided efforts to restore salmon populations: maintaining and increasing treaty and commercial salmon stocks for harvest and protecting and restoring naturally spawning salmon stocks. These goals are not inherently contradictory, but can become inconsistent when hatchery management and harvest practices targeted at the commercial stocks also damage wild runs. However, wild fish advocates argue that the hatchery stocks are doomed as well unless wild stocks are maintained to support genetic diversity in the hatcheries.

B. SALMON RECOVERY MANDATES

Regional efforts to restore salmon populations and maintain wild salmon stocks have centered around the measures recommended in the *Strategy for Salmon*. In the Columbia River mainstem, the principal responsibility for executing the plan rests with the BPA, but the other river management agencies, the U.S. Army Corps of Engineers (Corps) and Bureau of Reclamation, also play a role. The actions of these three river managers under the Council's plan are constrained by their separate duty to comply

⁶⁴ Coho salmon are largely extinct in the Columbia basin; but if the remaining stocks are listed, recovery efforts could affect the Columbia River and certainly would affect ocean fishery management.

⁶⁵ Willa Nelson, Jack E. Williams, and James A. Lichatowich, "Pacific Salmon at the Crossroads: Stocks at Risk from California, Oregon, Idaho, and Washington," *Trout*, Winter 1992, p. 21.

with the ESA as interpreted by NMFS. Other Federal agencies, such as the Forest Service and Bureau of Land Management, are also directed to take the Council's program into consideration when planning their management actions.

1. Council Plan—the Strategy for Salmon

Under the Northwest Power Act, the Council must develop a program:

. . . to protect, mitigate and enhance fish and wildlife affected by the development, operation, and management of [federal power] facilities while assuring the Pacific Northwest an adequate, efficient, economical, and reliable power supply.⁶⁶

The Council has approached this challenging task in stages. The third phase of the Council's fish and wildlife program merged its earlier efforts into the comprehensive *Strategy for Salmon*. A fourth-phase plan addresses conservation of resident fish and wildlife.

The *Strategy for Salmon* adopted two separate goals—to double the total salmon runs and to conserve existing diversity. Both of these goals are essential to the purposes of the Northwest Power Act *and* to the full implementation of the Council's mandate. Although the mandates of the Endangered Species Act draw public focus to the plight of the weakest stocks, restoring harvestable stocks is also essential to the Northwest Power Act and to meeting treaty commitments to the basin's Indian tribes.

The *Strategy* seeks improvements in salmon survival at every stage in the salmon's life cycle. The plan calls for the development of rebuilding targets for each run of naturally spawning salmon.⁶⁷ It provides interim rebuilding targets for Snake River spring, summer, and fall chinook.⁶⁸

Like most projects affecting salmon in the Northwest, the *Strategy for Salmon* has not gained universal endorsement. Certain commercial interests whose use of the Columbia River would be affected filed a lawsuit challenging the plan in Federal District Court; environmental advocates have joined the suit. The *Strategy* has been correctly criticized for its weakness in the areas of ocean survival and harvest.⁶⁹

The *Strategy for Salmon* requires scores of individual actions by all the agencies acting in the Columbia basin to achieve the goal of doubling salmon populations without losing biological diversity. Two of the most controversial aspects of the *Strategy* have been measures affecting management of water and power; namely, increases in river velocity and salmon transportation. Two principal mechanisms are designated to increase river velocities for improved salmon passage: increased water flow and drawing down the level of reservoirs along the migration corridor.

⁶⁶ Northwest Power Act § 4(h)(5), 16 U.S.C. § 839b(h)(5).

⁶⁷ *Ibid.*, section 2.3, Vol. II, p. 21.

⁶⁸ *Ibid.*, section 2.2, Vol. II, p. 20.

⁶⁹ For example, see Hearing Part III, p. 44 (testimony of Mr. Randall W. Hardy).

The *Strategy* makes a distinction between actions to improve mainstem survival that can be taken immediately and actions that will require more time to evaluate and implement. The plan states specifically that the immediate measures will not be sufficient to rebuild some weak stocks.⁷⁰

The *Strategy for Salmon* specifies immediate actions to achieve a "flow equivalent" target of at least 85,000 cfs at Lower Granite from April 16 through June 15 for Snake River spring migrants.⁷¹ This level of water flow was met in 1993 operations, in part because BPA, the Corps, and NMFS had to meet targets set by NMFS under the ESA, discussed below. The *Strategy* also requires further flow augmentation to reduce water temperature for fall Snake River migrants and enhance flows in the Columbia as well. By contrast, the Columbia Basin Fish and Wildlife Authority has requested minimum flows between 100,000 and 140,000 cfs in all years in the Snake and between 220,000 and 300,000 cfs in the Columbia.⁷²

As stated, the Council's plan recognizes that its immediate measures are not likely to be sufficient to rebuild salmon populations. As an additional means for improving water velocities, the *Strategy for Salmon* requires studies of the potential to lower the level of certain reservoirs to make the shape of the reservoirs more like the historic river during juvenile migration periods. There are two major parts of these drawdown recommendations. The first involves drawing down the level of the John Day reservoir on the lower Columbia River to minimum operating pool—the minimum level at which the John Day Dam was designed to operate.⁷³ The second would depend upon new studies of lowering four lower Snake River reservoirs, possibly *below* minimum operating pool, which would require dam modifications.⁷⁴

These drawdown proposals have been quite controversial among many entities that rely upon commercial use of the reservoirs. At the task force hearing, utility representatives argued that there was insufficient evidence that drawdowns or increased river speeds would help the salmon.⁷⁵ An organization representing various commercial users of the river presented the irrigation utilities' argument that drawdowns would be the "least viable, least

⁷⁰ *Strategy for Salmon*, section 3, Vol. II., p. 23.

⁷¹ *Ibid.*, section 3.2, Vol. II, p. 25. The "flow equivalent" is a measure of water particle travel time, which may be met in part by lowering reservoirs levels instead of increasing water amounts passed down the river.

⁷² Columbia Basin Fish and Wildlife Authority, "Proposed Flows for Columbia Basin Anadromous Fish," p. 9, March 1990. The Columbia Basin Fish and Wildlife Authority is composed of all the major fisheries agencies and Indian tribes in the Columbia basin. Although its original flow proposal was fairly brief, substantial technical justification was published in February 1991.

⁷³ *Strategy for Salmon*, section 3.6A, Vol. II, pp. 32-33.

⁷⁴ *Ibid.*, section 3.5, Vol. II, pp. 30-32.

⁷⁵ Hearing Part III, p. 378 (prepared statement of Mr. Don Godard), pp. 461-462 (prepared statement of Mr. Al Wright), p. 475 (testimony of Mr. Al Wright), pp. 483-484 (testimony of Mr. Don Godard).

cost-effective" mechanism for restoring salmon runs.⁷⁶ An Idaho grain elevator operator argued that drawdowns would be costly and unnecessary.⁷⁷ By now, the studies and implementation of the drawdown plans have been delayed many years past the deadlines set in the *Strategy*.

The *Strategy for Salmon* acknowledges the degree of scientific uncertainty surrounding reservoir drawdowns, and establishes a process to monitor and evaluate the effectiveness of the measures taken in a manner that adds to scientific understanding and, ultimately, salmon recovery. Specifically, the *Strategy for Salmon* calls for reservoir drawdowns for the lower Snake River, unless such drawdowns are shown to be structurally or economically infeasible or biologically imprudent.⁷⁸

The *Strategy* also requires that measures necessary to operate the John Day reservoir at minimum operating pool from May 1 to August 31 be evaluated and implemented while providing mitigation for the impacts of operating the reservoir below the minimum irrigation pool.⁷⁹ The Council estimates that a John Day drawdown would reduce water particle travel time between McNary and Bonneville Dams by one to two days, which represents a decrease of about 10 percent. To achieve the same reduction in travel time from increased flows would require about 3.1 million acre-feet of water from upstream storage.⁸⁰ A John Day drawdown would benefit not only listed Snake River salmon stocks, but also mid-Columbia summer chinook now petitioned for listing.

In 1993, Congress appropriated \$2 million for Advanced Planning and Design of modifications to public and private facilities that would be affected by a drawdown. The Corps has barely begun design work. The Corps estimates that at its present rate of progress, it will be 1999 before a John Day drawdown can be implemented.⁸¹

Another controversial feature of the *Strategy for Salmon* is the provision for juvenile salmon "transportation," which involves collecting salmon smolts at each of the Lower Snake River dams and barging them downstream to the Columbia River estuary. The effectiveness of this practice has been the subject of substantial dispute. Competing scientific studies suggest on the one hand that most of the smolts survive the trip and on the other hand that, although the voyage in artificial containers does not kill many hatchery fish, it has a much greater impact on wild salmon. In addition, survival to the estuary may not be the full measure of success for transportation; some argue

⁷⁶ Ibid., p. 342 (materials accompanying prepared statement of Mr. Bruce Lovelin), p. 330 (prepared statement of Mr. Bruce Lovelin), p. 473 (testimony of Mr. Bruce Lovelin).

⁷⁷ Ibid., pp. 509-510 (testimony of Mr. Joe Stegner).

⁷⁸ *Strategy for Salmon*, section 3.5, Vol. II, p. 30.

⁷⁹ Ibid., section 3.6A, Vol. II, pp. 32-33.

⁸⁰ Ibid., p. 428 (materials accompanying prepared statement of Mr. Jim Baker).

⁸¹ Hearing Part III, p. 293 (testimony of Maj. Gen. Ernest J. Harrell).

that the smolts have high mortality after release from the barges and may not receive the imprinting necessary for adult return to their native streams.⁸²

Despite the regional consensus represented by development of the Council's plan, the Northwest Power Act does not require that Federal agencies adhere to the Council's fish and wildlife program. Instead, it requires that Federal agencies operating power facilities on the Columbia River "tak[e] into account at each relevant stage of decisionmaking processes to the fullest extent practicable, the program adopted by the Council" In addition, BPA is to use its financial resources and authorities "in a manner consistent with the plan." There has been much dispute over whether the agencies have met these standards.⁸³

If the Council finds BPA's actions inadequate, it may make a formal Council determination of inconsistency with the plan. A Council finding of inconsistency would trigger a series of actions under the Northwest Power Act.⁸⁴ Again, this statutory process ends with a judgment made by the BPA Administrator, rather than the Council, regarding consistency with the Council's plan and Federal law. The threat of an inconsistency finding in mid-1993 led to productive negotiations between BPA and the Council over the content of BPA's fish and wildlife program.

2. NMFS Endangered Species Act Mandates

NMFS's efforts on behalf of salmon are focused on those naturally spawning salmon stocks listed or proposed for listing as threatened or endangered. Since the 1991 and 1992 listings of Snake River stocks, the agency has reviewed annual plans of operations for the river and begun to develop a recovery plan for those stocks.

As part of its statutory obligation to review whether agency activities will jeopardize listed species, NMFS has been heavily involved in the development of annual plans of operations for the reservoirs developed by BPA, the Corps, and BuRec. The 1992 and 1993 operating plans and biological opinions were challenged in court by several fishing and environmental groups. The State of Idaho filed a separate suit over the 1993 biological opinion. The State of Oregon joined Idaho in its challenge.

Environmentalists' attempts to obtain a court order to stop barging of salmon smolts in 1993 were unsuccessful. A recent decision on the States' suit in federal court, however, overturned the 1993 biological opinion, which formed the basis for a biological opinion on 1994-1998 operations as well.

⁸² *Ibid.*, pp. 398-939, 403 (materials accompanying prepared statement of Mr. Jim Baker).

⁸³ Contrast *Ibid.*, pp. 45-47 (prepared statement of Mr. Randall W. Hardy) and p. 159 (prepared statement of Maj. Gen. Ernest J. Harrell) with *Ibid.*, pp. 365-367 (prepared statement of Mr. Ed Chaney), pp. 384-385, 393 (prepared statement of Mr. Jim Baker), pp. 597-598 (additional material submitted by Mr. Lionel Q. Boyer), and pp. 658-659 (additional material submitted by Columbia River Inter-Tribal Fish Commission (CRITFC)). CRITFC represents four tribes living in the Columbia River basin: the Umatilla, Warm Springs, Yakama, and Nez Perce Tribes. *Ibid.*, p. 288.

⁸⁴ Northwest Power Planning Act § 4(j), 16 U.S.C. § 839b(j).

The judge found that NMFS's 1993 finding of "no jeopardy" to the endangered and threatened stocks was based on an analytical process that

... is too heavily geared towards the status quo that has allowed all forms of river activity to proceed in a deficit situation—that is, relatively small steps, minor improvements and adjustments—when the situation literally cries out for a major overhaul. Instead of looking for what *can* be done to protect the species from jeopardy, NMFS and the action agencies have narrowly focused their attention on what the establishment is capable of handling with minimal disruption.⁸⁵

The court remanded the biological opinion to NMFS for revision; further proceedings to bring the biological opinion on river operations into compliance with the ESA will continue over the next weeks and months.

The 1993 biological opinion was arrived at in negotiation with the Corps and led to the adoption of the following targets for both spring and summer flows, in addition to other management practices:⁸⁶

	<u>Flow</u>	<u>Time Period</u>
Lower Snake River	85,000 cfs	April 10 – June 20
(at Lower Granite Dam)	50,000 cfs	June 21 – July 31
Columbia River	200,000 cfs	April 20 – June 30
(at McNary Dam)	160,000 cfs	July 1 – July 31

The decision to require the summer flow meant that less of the 10.4 million acre-foot "water budget" stored for fish could be used in the spring, but substantial spring rainfall in the Snake River basin helped the agencies to meet these targets. One part of the biological opinion that caused some concern among fish advocates was designating these flows as "targets" rather than required minimums. But in fact, the flow targets were generally met.

NMFS recently issued a biological opinion finding that river operations over the next five years, 1994–1998, will not jeopardize the listed species of Snake River salmon.⁸⁷ This opinion evaluates an operations plan again developed by BPA, the Corps, and BuRec in consultation with NMFS. The flow targets remain the same, but varying amounts of additional water will be devoted to the flow augmentation "water budget" depending on water conditions each year. In addition, BPA will undertake to acquire more water for flow augmentation over the next five years. ESA consultation may be re-initiated if the agencies are unable to meet the flow requirements or the water

⁸⁵ *Idaho Department of Fish and Game vs. National Marine Fisheries Service*, Civ. No. 92-973-MA, slip op. at 36 (D. Ore. March 28, 1994).

⁸⁶ Corps of Engineers, "Record of Decision, Columbia and Snake River Flow Improvement Measures for Salmon, Supplemental Environmental Impact Statement, Plan of Reservoir Regulation and Project Operations," pp. 16-17, June 18, 1993.

⁸⁷ National Marine Fisheries Service, biological opinion, March 16, 1994.

budgets prove inadequate due to drought.⁸⁸ The biological opinion also directs the Corps to design a biological test of a Lower Granite reservoir drawdown by January 1, 1995. Since this 1994–1998 biological opinion was based on the same analysis as the 1993 opinion, it will presumably be modified as well in light of the recent court order.

Each of NMFS's biological opinions regarding river operations has led to controversy, in part because the ESA consultation process has been conducted among the agencies in private with minimal public involvement. For example, the first public notice of the alternative under consideration for operations over the next five years was the issuance of a draft biological opinion allowing just seven days for technical review and comment. And under the ESA regulations, this notice and opportunity for comment was provided only to State and tribal governments. But, as noted by the court in the recent decision overturning NMFS's 1993 biological opinion, "the underlying root of the litigation problem is the feeling of these parties that the Federal Government is simply not listening to them."⁸⁹

NMFS does claim to "encourage and consider any information volunteered by the public in its decision process."⁹⁰ In response to Chairman DeFazio's inquiry regarding this lack of public participation, NMFS acknowledged that there is no statutory or regulatory provision forbidding public involvement.⁹¹ Rather, the ESA is silent on this issue while it requires public notice and comment for certain other activities related to endangered species.

NMFS suggests public participation in the process of developing a biological opinion would be "unwieldy."⁹² NMFS also argues that such participation is less essential, since the biological opinion is not the product of policy debate, but rather scientific inquiry; the decision on final action by the consulting agency after issuance of the biological opinion is the appropriate point for public comment on policy.⁹³ This analysis disregards the practical process that takes place in developing a biological opinion and the potential benefits of public input. In a situation where NMFS is working actively with the river operating agencies to develop an alternative plan of operations that will not jeopardize the species, public comment—even constrained by short statutory time frames—might well suggest creative and valuable alternatives, or bring to the attention of agency scientists information regarding the potential impacts of a given alternative. The seven-day comment period provided for technical review by State and tribal governments might have been more useful if proposed alternatives had been suggested and public comments obtained in advance.

⁸⁸ Ibid.

⁸⁹ *Idaho Department of Fish and Game vs. National Marine Fisheries Service*, slip op. at 34-35.

⁹⁰ Hearing Part III, p. 282 (prepared statement of Mr. J. Gary Smith).

⁹¹ Ibid., pp. 302-306 (insert to testimony of Mr. J. Gary Smith).

⁹² Ibid., p. 304.

⁹³ Ibid., pp. 302-303.

In fact, NMFS has tried seeking public comment more extensively in the development of a recovery plan for the listed species. A team of outside analysts convened by NMFS to develop a recommendation for a recovery plan for the three listed Snake River stocks has received public comment on its draft recommendations. Final recommendations for a recovery plan will be issued later this year; NMFS will then review the recommendations and adopt a final recovery plan.

Unfortunately, the ESA does not require that measures be taken to achieve species recovery in fact after a "recovery plan" is adopted. This gap in the statutory scheme means that once the recovery plan is developed there is no guarantee that it will be followed. Agencies need not implement its recommendations. They may take any actions that a NMFS biological opinion determines will not place the species in "jeopardy." Agency actions would be limited only occasionally by NMFS opinions that actions will actually place the species in jeopardy of final extinction. Without any mandate for actual recovery, the ESA raises the prospect of salmon stocks constantly sustained on the brink of extinction.

C. AGENCY COMPLIANCE WITH THE MANDATES

Under the Northwest Power Act, BPA is the primary entity responsible for implementing the fish and wildlife program developed by the Council. The cost of the program is repaid by power sales. BPA Administrator Hardy testified that "virtually all" of 117 separate salmon-related actions identified in the *Strategy for Salmon* have been funded by the agency.⁹⁴ However, timetables for many of these actions, including major activities like reservoir drawdown studies, have slipped substantially.

1. Bonneville Power Administration

According to BPA figures, the cost of the fish and wildlife program has risen from \$150 million in 1991 to \$300 million in 1993.⁹⁵ These figures include \$149 million in 1993 for foregone power production, which rose in cost over the last few years as water flows for fish increased and as regional drought raised the amount of BPA's power purchases and also the cost of each kilowatt-hour purchased.⁹⁶ Thus, much of BPA's cost resulting from reduced flows due to drought has been attributed to salmon recovery. This accounting is inconsistent with BPA's budget treatment of other constraints on flows available for hydropower production; for example, as mentioned, irrigation withdrawals reduce water flows that might produce \$150-\$300 million worth of annual power production, yet irrigation withdrawals are not treated as an annual expense by BPA.

BPA's administration of the fish and wildlife program has been criticized by both power users and environmental advocates. BPA's customers, conducting a "function-by-function review" of BPA's programs, presented draft recommendations to streamline and possibly restructure the

⁹⁴ Ibid., p. 45 (prepared statement of Mr. Randall W. Hardy).

⁹⁵ Ibid., pp. 19, 28-29 (testimony and prepared statement of Mr. Randall W. Hardy). BPA estimates that the 1994-1998 biological opinion will boost annual fish and wildlife costs to \$350 million.

⁹⁶ Ibid., pp. 19, 28-30, 40-41 (testimony and prepared statement of Mr. Randall W. Hardy).

administration of the fish and wildlife program.⁹⁷ Environmental advocates have argued that BPA commits excessive program resources to activities that are better implemented by fish and wildlife specialist agencies and that BPA has failed to implement all of the actions required by the *Strategy for Salmon* on the schedule set by the Council.⁹⁸

The Columbia River Inter-Tribal Fish Commission and some private entities have recommended that BPA's fish and wildlife programs be transferred en bloc to the Fish and Wildlife Service, NMFS, or some combined group of fishery management agencies. In Administrator Hardy's written and oral testimony at the Bonneville Power Administration Task Force's September 24 hearing, he indicated a willingness to consider a lump sum transfer of fish and wildlife funds to one or more fish and wildlife agencies.⁹⁹

A lump sum transfer could allow BPA to substantially reduce its fish and wildlife staffing level, which now stands at 77 FTE positions. Many of BPA's critics complain that the BPA's fish and wildlife program is at best redundant and, in some cases, operates at cross purposes with other Federal, State, and tribal fish and wildlife agencies.

BPA has adopted an analogous approach to funding its responsibility to implement the Council's resident fish and wildlife program. BPA has signed resident fish and wildlife trust agreements satisfying its responsibilities to the States of Idaho and Montana. Those agreements provide long-term mitigation for projects in those States while indemnifying BPA against further claims. The agency has signed an interim funding agreement with the State of Washington, worth \$43 million and has provided the State of Oregon with \$150,000 to fund its efforts to negotiate a resident fish and wildlife trust agreement.¹⁰⁰

Apart from financing issues, BPA's implementation of flow augmentation for fish came under particular criticism in 1992, when the agency used water provided by Idaho water users only to move fish to barge collection sites at Lower Granite reservoir. From Lower Granite on, water intended to enhance flows for the length of the river downstream was offset by reduced flows from the Upper Columbia, whose water was held for power production instead.

BPA Administrator Hardy explained that the agency felt the flows were unnecessary in the Columbia because most of the endangered salmon smolts from the Snake River were presumed to be in barges by the Columbia reach of the river.¹⁰¹ However, water is necessary in the Lower Columbia River to transport fish coming from the Columbia River watershed as well as any other smolts that have avoided the collection facilities in the Snake. In

⁹⁷ "A Functional Review of Fish and Wildlife in the BPA," Draft Review Team Report, October 13, 1993.

⁹⁸ Hearing Part III, pp. 368 and 372 (prepared statement of Mr. Ed Chaney), pp. 384-85 (prepared statement of Mr. Jim Baker).

⁹⁹ *Ibid.*, pp. 68-69 (prepared statement of Mr. Randall W. Hardy).

¹⁰⁰ Hearing Part III, p. 140 (testimony of Mr. Randall W. Hardy).

¹⁰¹ *Ibid.*, p. 152 (testimony of Mr. Randall W. Hardy).

addition, this reasoning leads to the contradictory result noted by Chairman DeFazio,

We have got to barge salmon because there are not enough flows and then we do not have flows because we have got barges. It is hard for people to understand, mere mortals like me and I think some of the farmers; it is a little counter-intuitive.¹⁰²

2. Corps of Engineers

The Corps of Engineers, not BPA, took the lead in developing the 1994-1998 river operation plan currently under consultation with NMFS. The Corps is also the lead agency for two long-term studies, the System Operation Review (SOR), and the System Configuration Study.

The System Configuration Study will evaluate various changes in the Columbia River system that might require new construction by the Corps. These include the *Strategy for Salmon's* recommended drawdowns of the John Day reservoir below minimum irrigation pool and drawdowns of the lower Snake River reservoirs below minimum operating pool. The Corps' timetable for this analysis requires ten years before drawdown tests on the lower Snake are complete, salmon survival is analyzed, and a decision is made. A "Phase I" report on the study is scheduled for completion in spring of 1994, with drawdown testing in 1996.¹⁰³ The System Configuration Study also includes the possible construction of new salmon collection facilities to aid in barging smolts. As discussed above, the Corps has accelerated studies on the John Day drawdown, anticipating that the modifications might be completed as early as 1999.

The SOR, which incorporates some of the study questions recommended in the *Strategy for Salmon*,¹⁰⁴ is a separate study of hydropower operations in the Columbia River hydropower system taking into account the needs of the salmon. The SOR will produce an environmental impact statement (EIS) with options for new procedures to set hydropower operations, as well as new terms for the Pacific Northwest Coordination Agreement (PNCA), which expires in 1998.¹⁰⁵ The PNCA is a contract that determines how hydropower operations will be coordinated among Federal and non-Federal entities to guarantee, among other things, that the power production terms of the Columbia River Treaty with Canada are met.

3. Bureau of Reclamation

Despite the Council's recommendation that the Federal agencies explore alternatives for increasing water quantities available for salmon in the Columbia basin,¹⁰⁶ non-power-producing reservoirs of the Bureau of

¹⁰² Ibid., p. 153.

¹⁰³ Ibid., p. 293 (supplemental information included in testimony of Maj. Gen. Ernest J. Harrell).

¹⁰⁴ *Strategy for Salmon*, section 3.6D, Vol. II, p. 34.

¹⁰⁵ Hearing Part III, pp. 159-160 (prepared statement of Maj. Gen. Ernest J. Harrell).

¹⁰⁶ *Strategy for Salmon*, section 3.6C, Volume II, pp. 33-34.

Reclamation have been excluded from the SOR studies. BuRec Assistant Regional Director Kenneth Pedde asserted that incorporating these BuRec reservoirs into the study could delay the outcome of the SOR by 3-4 years, although the possible availability of BuRec water has been modeled using a hypothetical 15th reservoir in the studies.¹⁰⁷ The Corps also has mentioned that salmon needs would be protected as non-power uses which take priority under the terms of the PNCA.

BuRec's major role in the Columbia River system is to store and divert water for irrigation, but its Grand Coulee and Hungry Horse Dams also produce hydropower sold through BPA. BuRec has played a substantial role in obtaining additional water for salmon flows. The agency is working on model water conservation programs in the Grande Ronde River basin and the Yakima River basin. Unfortunately, water conservation efforts are to some extent undercut by BPA's prices for irrigation pumping power. In addition, as discussed in section D below, illegal water use and limitations of State water law have limited BuRec's effectiveness.

D. WATER LAW LIMITATIONS

Acquiring additional water to assist in moving juvenile salmon downstream is a major theme of the *Strategy for Salmon*, as well as NMFS's biological opinions under the ESA. BuRec has been able to assist in this effort because not all BuRec water has been contracted for, and significant water conservation savings can be obtained from BuRec customers in the Northwest. One area in which BuRec has directly moved to carry out the *Strategy's* recommendations is in developing new conservation demonstration projects providing Federal money toward improved water conservation in the region.

However, BuRec's efforts to obtain water in the Snake River basin for out-of-state use have been stymied somewhat by restrictions in Idaho water law.¹⁰⁸ In addition, illegal "water spreading"—applications of irrigation water outside project boundaries or on land deemed unsuitable for irrigation—has prevented some conserved water from returning to the river system.

Idaho State law makes it very difficult to provide permanent protection for water used for fish. The Idaho Natural Resources Board may obtain permanent water rights for instream flows, or an existing water user may transfer its water to instream use, but several further standards constrain water that will flow out of the State. These standards make it virtually impossible to protect such water; a 1991 BuRec attempt to change the nature of use of its existing storage water rights to instream flow rights for salmon recovery encountered more than 650 letters of protest to the State water board.

Annual water rentals through Idaho water banks can provide water for salmon from year-to-year. Again, State law makes it difficult to obtain such rentals, and water bank rules discourage users from transferring water to

¹⁰⁷ Hearing Part III, pp. 590-591 (testimony of Mr. Kenneth R. Pedde).

¹⁰⁸ Water conservation measures in the 1980s reduced irrigation diversions by 800,000 acre-feet, but none of that water was transferred to flows for fish. Hearing Part III, p. 578 (prepared statement of Ms. Garrison).

instream use.¹⁰⁹ The State legislature passed a special three-year exemption for BuRec to provide out-of-state flows from rented water through January 1, 1995.¹¹⁰ This law requires only that the flows be part of an overall augmentation plan, and that other parties make a proportional contribution to salmon restoration. The BPA decision to offset Snake River flows by reducing flows from the Upper Columbia in 1992 led to allegations that BuRec's flows violated the provisions of the three-year exemption law.

On top of the State disincentives to transfer water to instream flows, Federal involvement in irrigation often undercuts BuRec's efforts to obtain water for salmon flows. BPA's reduced rate for irrigation pumping (discussed above on page 21) lowers the cost of irrigating and thus provides a disincentive to water conservation. In addition, BuRec has known for years that irrigation districts have illegally applied water to lands lying outside the approved scope of the Reclamation projects, yet has only recently convened a task force to address this practice. And BuRec has in the past been quite lax in enforcing the water conservation requirements of the Reclamation Reform Act of 1982, although new water conservation regulations are currently being drafted. As the region continues to look for ways to provide fish flows in the rivers, reform of these Federal policies could supply some of the needed water.

E. AGENCY SATISFACTION OF INDIAN TRUST RESPONSIBILITY

The Indian tribes of the Pacific Northwest region are among those most concerned with salmon recovery activities due to their historic dependence on salmon fisheries and their treaty rights to continued access to those fisheries. Since the Federal Government has a general trust responsibility to the tribes in addition to these specific treaty obligations, the Federal agencies must take tribal concerns into account in decisionmaking regarding the salmon. Unfortunately, the tribes have found the agencies' decision processes unresponsive and have remained some of the most vocal critics of BPA and other Federal entities in the Northwest. A petition by the Shoshone-Bannock Tribes led to the listing of the threatened and endangered stocks in the Snake River.

The tribes' criticism of salmon recovery efforts begins with the *Strategy for Salmon*. The Yakama Tribe has sued the Council over the adequacy of the plan, arguing that it meets the requirements of politics but not those of science.¹¹¹ Both the Columbia River Inter-Tribal Fish Commission and the Shoshone-Bannock Tribes told the task force that tribal concerns were inadequately addressed because of lack of tribal membership on or an inter-governmental relationship with the Council.¹¹² (Even NMFS supported adding tribal representation to the Council, which would require amending the Northwest Power Act.¹¹³)

¹⁰⁹ Ibid., p. 579 (prepared statement of Ms. Garrison).

¹¹⁰ Idaho Code § 42-1763A.

¹¹¹ Hearing Part III, p. 288 (testimony of Mr. Anthony Van Pelt).

¹¹² Ibid., pp. 602 (additional material submitted by Mr. Lionel Q. Boyer), 657, and 660 (additional material submitted by CRITFC).

¹¹³ Hearing Part III, p. 283 (prepared statement of J. Gary Smith).

In addition, the tribes have been highly critical of Federal agency efforts to restore salmon stocks, particularly the efforts of BPA. They feel they have been left out of important decisionmaking processes, even where the *Strategy for Salmon* mandates their involvement.¹¹⁴ They expressed doubt that the agencies managing Columbia basin resources were even aware of the existence of their trust responsibility to the tribes.¹¹⁵

The lack of attention to tribal concerns is unfortunate also because Indian water rights could contribute to the solution to the problem of protecting water flows for fish. The Nez Perce Tribe has intervened in an Idaho State court adjudication of water rights on the Snake River, claiming a right to the water necessary to sustain salmon to meet their treaty fishing rights, with a mid-1800s priority date set by the treaties. If upheld by the court, this claim could provide the legal basis for maintaining adequate flows for Snake River stock.

F. FISH AND WILDLIFE PROGRAMS IN THE COMPETITIVENESS PROJECT

BPA has proposed tying fish and wildlife program spending to the agency's fiscal success.¹¹⁶ One stated purpose is to give fish-protection advocates some stake in BPA's financial well-being. BPA also hopes to gain greater planning certainty by setting a "floor" for fish and wildlife expenditures that would only be exceeded during periods in which BPA is financially successful.

Since BPA's actual outlays for fish and wildlife expenses and capital outlays amounted to \$82.5 million in 1993,¹¹⁷ the potential for real savings through "incentivization" of the fish and wildlife program is probably small. In addition, BPA's statutory fish and wildlife responsibilities do not somehow evaporate during bad water years or other financially difficult periods.

G. FINDINGS AND RECOMMENDATIONS

- ▶ The Northwest must unite behind a single vision for salmon recovery if the purposes of the Northwest Power Act are to be achieved. To the extent a regional consensus on salmon recovery exists, it is represented by the Council's *Strategy for Salmon*. The *Strategy* is a comprehensive plan for rebuilding healthy and genetically diverse anadromous fish populations throughout the basin. It is aimed not only at recovering listed stocks and making future listings unnecessary, but also at producing harvestable numbers of fish for both Indian and non-Indian harvesters. The *Strategy for Salmon* was developed within the region with strong public participation.

¹¹⁴ *Ibid.*, p. 289 (testimony of Mr. Anthony Van Pelt), pp. 597-598 (additional material submitted by Mr. Lionel Q. Boyer).

¹¹⁵ *Ibid.*, p. 604 (additional material submitted by Mr. Lionel Q. Boyer), p. 662 (additional material submitted by CRITFC).

¹¹⁶ Hearing Part III, pp. 20-21 (testimony of Mr. Randall W. Hardy). Also see Final Draft Strategic Marketing Plan, February 1994 at p. 48.

¹¹⁷ About one-half of BPA's estimated \$300 million fish and wildlife budget consists of "losses" attributed to foregone power sales and resulting power purchases; see Hearing Part III, p. 29 (testimony of Mr. Randall W. Hardy).

- ▶ There has been considerable interest in the actions proposed to recover Snake River salmon stocks listed under the Endangered Species Act. However, the focus on listed stocks could detract from the fundamental purposes of the Northwest Power Act and the *Strategy for Salmon*, which seek basin-wide recovery of all affected fish and wildlife populations. Whatever the outcome of NMFS's ongoing efforts to protect and recover threatened and endangered species under the Endangered Species Act, those efforts should not compromise the implementation of an overall regional plan under the authority of the Council.

Notwithstanding the measures proposed in any future ESA recovery plan or biological opinion governing operation of the Columbia River system, BPA and other Federal agencies continue to bear a responsibility to implement the *Strategy*. The *Strategy for Salmon* should not be delayed while ESA recovery plans are developed or NMFS's biological opinions are litigated. NMFS should work closely with the Council to ensure that its proposed actions are consistent with the *Strategy for Salmon*.

On the other hand, the four States in the region should avoid undermining the regional consensus as they pursue their own parochial interests. The Council has been and should continue to be the forum for resolving regional conflicts.

- ▶ The *Strategy for Salmon* has suffered from uneven implementation and uncertain funding, with some significant actions falling well behind schedule. One theme sounded by many witnesses was the need for accountability for fish and wildlife mitigation measures.¹¹⁸

The rebuilding targets called for in the *Strategy for Salmon* are the standard that must be used to evaluate salmon recovery efforts. It will be difficult, if not impossible, to judge the effectiveness of individual actions taken under the *Strategy* until these objectives are determined. State and tribal fish managers, working with the Council, should quickly complete the development of rebuilding targets for individual naturally spawning salmon runs within the Columbia basin.

- ▶ The causes of salmon decline are numerous, although the development of the Columbia basin's hydroelectric system almost certainly represents the single most significant human-caused source of salmon mortality. Intuition as well as the available science argue that juvenile salmon need greater flows and river velocities during the migration period than those that prevail when the system is operated to maximize hydroelectric generation.

Though a considerable degree of scientific uncertainty exists, it is imperative that the region act quickly and prudently to improve downstream passage conditions relying on the best available science. To that end, the *Strategy for Salmon* calls for both immediate and longer-term measures to decrease downstream travel times through a combination of increased storage for flows and reservoir drawdowns. Without pre-judging the outcome of the Lower Granite Dam test now being designed and fully understanding the difficulty of designing and

¹¹⁸ For example, see Hearing Part III, p. 44 (testimony of Mr. Randall W. Hardy) or p. 457 (testimony of Mr. Al Wright).

conducting a meaningful experiment under minimally controllable circumstances, the Corps should move aggressively to design and conduct a meaningful biological test. The decline of Snake River salmon stocks represents a biological emergency that demands prompt action. Sufficient staff and funding should be allocated to ensure that this effort proceeds in a timely manner.

- ▶ The Corps is proceeding at what can only be described as a glacial pace in its efforts to evaluate and design measures to mitigate operation of John Day reservoir at minimum operating pool. The Corps should begin design work on the necessary modifications immediately, using the money specifically appropriated for that purpose. Congress should provide the funding and direction necessary to expedite implementation of a John Day drawdown to minimum operating pool while providing full mitigation to affected irrigators.
- ▶ As part of its effort to remain competitive, BPA should negotiate an agreement transferring its fish and wildlife functions to one or more fish and wildlife agencies. Such an agreement must be conditioned on thorough monitoring and evaluation of results, tied to specific rebuilding targets, as well as a commitment on the part of the implementing entity to fully carry out the Council's *Strategy for Salmon*. BPA, in turn, would reasonably expect that such an agreement would hold the implementing agency or agencies accountable for results, perhaps through the use of independent audits, and provide a significant degree of planning certainty over a specific period of time.

Administrator Hardy, in his testimony before the task force, indicated a willingness, if not an eagerness, to begin discussions toward a lump sum transfer of many of its fish and wildlife responsibilities. However, no such discussions have commenced between BPA, any other Federal entities, and the Council.

- ▶ Another common theme heard during the task force's deliberations was the lack of coordination between Federal agencies, State fish and wildlife managers, and tribes. Since the demise of the Northwest River Basins Commission in 1981, there has been no single entity responsible for developing a comprehensive basin plan and coordinating the implementation of that plan.

During the task force's September 24, 1993 hearing, the creation of a new regional entity responsible for basin planning and implementation was discussed. There may be merit in such an approach as long as the new planning effort: (1) incorporates existing plans and processes; (2) is not used as a pretext for delay in the implementation of the *Strategy for Salmon*; (3) provides for full public participation; and (4) produces binding agreements that commit the participants to undertake the recommended measures.

Alternatively, NMFS, working with the Council, BPA, and other Federal, State, tribal, and private interests, could seek to develop a basin-wide conservation plan, using the *Strategy for Salmon* as a framework. Such a plan should include rebuilding objectives and a timetable for implementation, as well as a strong monitoring and adaptive management component. A basin-wide conservation plan, if fully implemented, could provide justification for the Secretary of Commerce to use his authority under §4(b) of the ESA to defer further ESA listings pending evaluation of the effectiveness of actions taken under the plan.

- ▶ The Federal agencies and the States should continue their efforts to reform water law so that conserved water may be dedicated to instream flows. The same logic that counts lost-generation opportunities caused by increased fish flows as lost revenues would consider water purchases for instream flows as an energy resource acquisition cost, not a fish and wildlife program cost. BPA should consider making this conceptual leap.

Federal policies that discourage water conservation should be reformed. BPA should develop alternatives to its present practice of discounting power for irrigation uses, including new power-pricing methodologies that provide incentives for water conservation.
- ▶ BPA and the State of Oregon should begin negotiations on a long-term resident fish and wildlife trust agreement. In the interest of equity, BPA should consider an interim funding agreement with the State of Oregon, similar to its agreement with the State of Washington.
- ▶ Federal efforts to restore salmon stocks have not always given sufficient deference to the Federal trust responsibility to Indian tribes in the region or to Indian treaty rights. The Federal agencies should redouble their efforts to involve the Indian tribes at all levels of decisionmaking on management of the Federal water system. Impacts on traditional hunting and fishing rights should be an essential part of the analysis of all Federal activities. In addition, Federal agencies, the Council, and the States should recognize the tribes' status as separate governments within the Northwest region.
- ▶ In the interest of open government, as well as greater public understanding of the tradeoffs inherent in balancing scientific uncertainty against social and economic interests, the National Marine Fisheries Service and other Federal agencies should explore options aimed at opening Endangered Species Act consultations to public scrutiny, if not public participation.
- ▶ Though there may be some merit in allowing BPA a greater degree of flexibility in determining its fish and wildlife program spending levels (or "incentivizing" its fish and wildlife program, as proposed in the Final Draft Marketing Plan), it must be recognized that in the final analysis BPA is not a utility; it is a public agency with a mandate from the public.

The Northwest Power Act's conservation and fish and wildlife mandates are at the very core of BPA's mission. They distinguish BPA as a steward of the Columbia River's fish and energy resources and as a power supplier committed to providing affordable energy to the people of the region at the lowest long-term cost. Fulfilling that mission more effectively and efficiently should be the primary aim of BPA's Competitiveness Project.

VI. CONCLUSION

The Bonneville Power Administration is at a crossroads. The agency is considering, and in many cases moving to implement, major changes in its structure and the manner in which it seeks to fulfill its mandates. Decisions being made over the course of the next few years will have profound implications not only for BPA, but also for the economy and culture of the Pacific Northwest.

In the final analysis, the Bonneville Power Administration's first responsibility is not to serve its Federal masters, the Governors of the four States in the Pacific Northwest region, or its utility and non-utility customers' individual interests; it is to serve the people of the Pacific Northwest. Whether BPA makes choices in the next two to three years that best serve the long-term interests of the people of the region remains to be seen.

The hearings held by the Bonneville Power Administration Task Force constitute what is arguably the most extensive congressional oversight of the BPA since the passage of the Northwest Power Act in 1980. Continuing informed congressional oversight is essential during this crucial period in BPA's history.

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