

**Bonneville Power Administration**

PO Box 14428

Portland, OR 97293-4428

*Via Electronic Mail*

**RE: Joint Public Power Comments On BPA's Proposed 2009 Spending**

**June 19, 2008**

**Introduction**

These comments are being filed jointly by the following public power organizations: **Public Power Council, Industrial Customers of Northwest Utilities, Northwest Requirements Utilities, Pacific Northwest Generating Company, and the Public Generating Pool**; and are intended to reflect a general consensus towards BPA's proposed 2009 spending levels by the listed organizations.

**Budget Decision-Making**

We appreciate the efforts of staff at BPA to make high level budget information available through this process. We realize that, given the timing this year, it is difficult to change budgets for FY09 in the IPR process. However, there is a larger issue around how BPA will ensure that the IPR process actually can affect and improve future budgets, rather than being merely a set of briefings on budget decisions that have already been made.

A couple of changes would help in evaluating BPA's proposals: first, BPA should provide alternative packages of spending proposals for evaluation. It is difficult to respond to a single proposed budgetary number for a given BPA function – it would be far more useful to see alternative spending proposals, with an indication of the costs and benefits associated with each alternative approach.

Related to this, it would be useful and good budgetary practice to have BPA present a formal business case for new incremental spending proposals where BPA would calculate the benefit and the rate of return associated with the incremental spending, so that the proposal could be better evaluated. Such a business case approach would mirror the new processes used by the Corps of Engineers and Bureau of Reclamation with considerable success in better justifying new spending.

**Lack Of An Overall Budgetary Cap**

One thing that seems obvious from examining the various budgets submitted by BPA and associated organizations is that there is no evidence of an overall spending limit – there is

a general escalation of budgets, which leads to a significant overall cost impact. Future energy prices are inherently unpredictable, and can change very rapidly. BPA should guard against inadvertently raising its cost structure to the point where it may have competitiveness problems if market energy prices decline in the future.

Another 2009-specific issue is that BPA has already set rates based on a forecast of what BPA's costs would be in 2009. In this instance, BPA should be very reluctant to escalate its costs in any given area over what it already established should be sufficient to manage within for this rate period.

BPA also should consider the cost pressures faced by its customers – the new requirements of I-937 and related portfolio standards in other states will impose sizable new costs on retail utilities. It is incumbent on BPA to recognize these other added cost pressures when setting its own costs.

### **Energy Northwest**

BPA proposes to increase its funding level for the increased operating costs of the Columbia Generating Station (CGS) by \$50.9 million in 2009. The funding level for CGS for 2009 in the current rates is \$243 million. In the IPR, BPA proposes to increase this funding level to \$294 million. This represents a 21% increase in costs deemed to be sufficient in the 2007 rate case. We appreciate the work that the BPA Richland staff does with regard to analysis and reporting on CGS costs and the work BPA staff is doing with Energy Northwest to reduce this increase by reducing the contingency reserves and fuel costs and the fact that EN has agreed to remove funding for the Joint Advisory Committee Study of New Resources. However, even after these reductions the operating costs of CGS are the most significant upward cost driver in BPA's program levels for 2009. BPA and CGS should continue to work to identify cost reductions without hindering the safe and reliable operation of this plant.

In the future BPA and EN should continue to develop a closer working relationship when it comes to the inclusion of EN costs in the BPA budgeting and rate making processes. EN plays an important role in the BPA cost structure, and it is important that it provide both a comprehensive overview of key financial issues and the necessary supporting data to BPA and its customers ahead of the BPA rate setting process. Absent more timely and reliable information it is difficult for BPA and its customers to come to informed decisions regarding this key resource. This is especially important as we begin the process of considering relicensing of the plant for the post 2024 period.

In addition, EN should be aware of the importance of its Long Range Plan (LRP) for BPA ratemaking. BPA's rate periods extend beyond the current budget period of EN. Therefore, the LRP becomes very important as BPA uses this data for its rate setting purposes. It would be most effective if the results of the LRP could set a cap on spending in the years beyond the current budget year. Also, it would be very helpful if the timing of the LRP and the BPA Integrated Program Review (IPR) could be better synchronized

so that BPA could have reliable information as BPA and the customers go into the IPR process. In addition, BPA and EN should further explore the costs and benefits of moving CGS financial reporting to BPA's fiscal year. All other entities that BPA provides funding for report their costs on the same fiscal year as BPA. Having two different fiscal years requires BPA to make a crude conversion to their fiscal year and increases the risks of inaccuracies.

For additional guidance, BPA and EN should look to the new relationship between the Army Corps of Engineers, the Bureau of Reclamation and BPA that has developed since direct funding has been put into place. From the customers perspective the relationship between these entities has much improved, along with the quality of information that is being shared with the customers.

## **Corps & Bureau**

While improvement is always possible, it appears that the Integrated Business Management Model developed by the Corps, Bureau and BPA has resulted in a fairly rigorous asset-based planning and management program. The program is designed to address criticism that the Corps and Bureau cost requests under the old process were wish lists rather than funding based on measurable improvements in the asset. For example, the funding of projects at McNary and Grand Coulee seem to provide good value for the funds expended.

The ramp up of capital expenditures in FY2009 is significant (approximately \$50 million). The primary reason given for this is the need to catch up with capital improvements that have lagged over the past several years and the reliance on increasingly costly hydro generation equipment for a limited number of international suppliers. The agencies should be encouraged to broaden their supplier network so they are not captive to a small number of suppliers.

O&M budgets take a substantial jump in FY2009 and then escalate from that base at 3.1 percent per year. We believe that the agencies should be encouraged to take steps to reduce or eliminate inefficient O&M, rather than just escalating O&M costs by a fixed amount.

## **Fish and Wildlife**

### *Integrated Program*

BPA and its customers face a challenging time with respect to fish and wildlife issues in the region. Questions remain as to how the Northwest Power and Conservation Council Program, Memoranda of Agreement with States and Tribes (MOAs), a new biological opinion (BiOp), and other elements of BPA's fish and wildlife budget will be integrated into an effective program. These uncertainties should not be an avenue for additional budget increases beyond those proposed for FY2009. BPA customers would like to see

assurances that as the cost pressures on the fish and wildlife program grow, there are no duplicative efforts or double funding of projects. New elements of the fish and wildlife program need to be complementary to existing fish and wildlife projects and the entire program must prove to be science-based and cost-effective.

There are projects currently funded by rate payer dollars (including projects such as restoring habitat in the Malheur Basin, Mule Deer programs in Washington State, assessing watershed characteristics in the Grays River and freshwater mussel surveys in the Umatilla River) that have little relation to the effects of hydropower construction and operation and should be funded through other sources or eliminated, resulting in a more efficient and cost-effective program. The funding should be seen as comprehensive for both fish and wildlife and the proposed budget should not increase beyond its current limit.

#### *Roll-over Not Good Policy*

The program budgets should be fixed, regardless of whether or not the program has spent all of the allocated dollars in the previous year. Excepting BiOp and MOA commitments, the establishment of funding should not create a locked-in future expectation to the budgeted funds if they are not spent in the current fiscal year. If projects do not meet scientific review or if for any other reason the program cannot spend its budget in a fiscal year, the unspent funds should not be available for funding projects in the future. We understand that some commitments in the MOAs are tied to biological benefits that have been credited in the Biop. Funds for projects that are included in the Biop need to be available until a project is proposed to secure the benefits and that project meets with scientific and Council approval.

#### *Science Review*

BPA's customers recommend that the current requirements for Independent Scientific Review Panel (ISRP) review be continued for all projects funded by BPA. This is not only consistent with the Northwest Power Act but also provides the necessary independent scientific review that BPA customers need for assurance that ratepayer funds are spent effectively and efficiently. Public power ratepayers have a keen interest in BPA's Fish and Wildlife investments achieving expected biological benefits. We have seen a wide variety of proposals for BPA to expend ratepayer funds that could presumably benefit fish and wildlife. However, we have also seen that without objective, independent science review, some of these ideas have been ineffective. We support independent science review because we have observed that fish and wildlife project proposals have been improved in response to scientific review. ISRP review provides BPA's customers with an objective measure of the likelihood of particular projects actually achieving the proposed biological objectives and subsequently, an increased level of assurance that ratepayer funds are providing benefits for fish and wildlife that will help to mitigate for the impacts of the FCRPS. The ISRP improves the chances that good projects will be funded and that projects that are not well thought-out or that have a

poor scientific foundation will not move forward until shortcomings in the proposal are corrected.

#### *Economic Review*

The Council has an important forum for the economic review of fish and wildlife programs, the Independent Economic Analysis Board (IEAB). With the growth of the direct program and the many competing sub-programs under it, it is essential that the program is reviewed to ensure that objectives of the fish and wildlife program are being met in the most cost effective manner. This is the role of the IEAB. We continue to support the IEAB, and request that the IEAB be adequately funded so that it can perform this vital function.

#### *Inflation Factor*

We support a long term capped budget for the fish and wildlife direct program and believe that this important for all parties. For BPA's customers the cap provides some level of cost certainty and for the Fish and Wildlife program funding recipients this provides budgeting certainty.

For the first time in this IPR we have been confronted with a proposal that BPA will set a total budget for the Fish and Wildlife direct program that will increase over time with a 2.5% yearly inflation factor whether or not the underlying growth of program costs are increasing at this rate. In the past, programs have been built from the underlying programs. In this case, BPA proposes to increase the program funding level whether or not it is justified by the total cost of the programs. Customers also expect that many of the projects in the direct program are not subject to inflation. These are ongoing programs under a scope of work and fixed budget each year. Applying an inflation factor to the entire direct program inflates these fixed costs as well. On the other hand, we also recognize that inflation could be higher than 2.5% from year to year. As a result we believe that the addition of the inflation factor provides all the more rationale for the overall budget cap since adequate flexibility is provided under the cap plus inflation for program cost growth. We do request that BPA perform an analysis of whether it is appropriate to apply the inflation adjustment to the entire direct program, or only that portion of the program that is truly subject to inflation.

#### *Uncertainty with Hydro Operations Costs*

The economic impacts of changes in hydropower operations to improve fish survivals are a significant portion (\$332 million) of the total BPA Fish and Wildlife Program in 2009. We appreciate BPA's continuing to keep a full accounting of these costs because this lost generation present poignant tradeoffs and opportunity costs for the region. However, BPA's estimate of projected operations costs is highly uncertain. As an example, in 2007 operational cost that include lost revenues and power purchases were \$403 million and in 2006 these same costs were \$566 million. Actual costs from these years illustrate that lost revenues and power purchases due to fish and wildlife requirements can be

substantially higher than the averages presented by BPA. It is also clear that uncertainty with future operational costs is not uniformly distributed above and below the average. This is easily shown with the actual operational costs in 2001 which were more than \$1.5 billion. Because of the risks that operations costs will be substantially higher it is imperative that BPA establish and abide by a long-term budget for the Integrated Fish and Wildlife Program costs. BPA needs to establish this budget to provide financial certainty to both fish and wildlife program managers and BPA's customers.

### **BPA Internal Operating Costs**

BPA's forecast internal power operations costs for FY2009 are escalating significantly. BPA's proposed FY2009 internal power operations budget is 14% above BPA's level of spending from FY2007-2009. BPA's FY2007 internal power operations costs are already 13% above BPA's FY2004 costs, after BPA laudably cut its internal power operations costs by 18% from FY2001-FY2004. In other words, after a very positive trend several years ago, the new FY2009 internal power operations budget proposal would be an escalation of 30% in five years.

These increases are occurring despite the savings BPA is achieving under the Enterprise Process Improvement Program (EPIP). For example, the General Counsel's office, with 52 attorneys currently, is planning on increasing its spending from \$8 million in FY2007 to \$9.5 million in FY2009, and the Finance function is increasing spending from \$12.6 million to \$15.2 million. BPA also is dramatically increasing spending on a new function – Technology Innovation and Confirmation from \$1.6 million in FY2007 to \$9.9 million in FY2009, without achieving offsetting savings in other areas. It should be noted that BPA's proposed FY2009 internal power operations budget is \$13 million over the number used in the rate case. Particularly given the savings achieved under EPIP, BPA could limit the net escalation in its internal operating costs to the rate of inflation. If the agency wants to add new functions, it should identify offsetting savings in other functions.

### **Energy Efficiency Program**

Recently, the Northwest Power and Conservation Council released the region's 2007 conservation achievements. The region achieved over 200 aMW of conservation, well exceeding the Council's target of 140 aMW for the year. The region's utilities have very strong incentives to continue to pursue conservation efforts, such as conservation requirements imposed by state Renewable Portfolio Standards, increasing consumer demand for energy efficiency, increasing power costs, and preparation for new contracts with tiered rates and sharp price signals. Because the region has demonstrated its ability to achieve conservation under current levels of BPA spending, we question the proposals for increases above the previously set budget for 2009.

Acquisition expenses are proposed to increase significantly from rate case to IPR projections (\$2 to \$7 million). It is important for BPA to describe in detail what the acquisition expenses will be used for and how they will support the Energy Efficiency program in obtaining its conservation targets. The vague nature of many of the line items such as “sector support” and “marketing” leave questions about how these dollars are being used.

Specificity in the nature of some of these costs is needed to provide clarity to the programs ratepayers are funding. For example, the difference between “conservation” and “regional energy efficiency,” as stated on page 38 of *IPR Overview Workshop, May 15, 2008* is not evident. With BPA expecting these costs to increase, customers need greater clarity as to the differences and the reasons BPA believes it is necessary for these budgets to increase.

Finally, it is important for BPA and customers to discuss the role of BPA’s conservation program in the new Regional Dialogue contracts. While we acknowledge that IPR 2009 is not necessarily the forum for discussion of conservation post-2011, customers would be more comfortable discussing the 2009 budget if there was greater understanding of what BPA intends to include in the long-term contracts it expects customers to sign later this summer.

### **Renewable Resources Program**

The region has exceeded its annual renewable energy targets for the last several years. In doing so, the region has shown that it is not only capable of, but also actively interested in, pursuing renewable resource development. Due to state Renewable Portfolio Standards, increasing local community pressure for renewable resources and impending carbon regulation, we can be assured that the region will continue developing renewable resources. We commend BPA for acknowledging the region’s successes in developing renewable resources by reducing its facilitation budget from \$13 million to \$2.5 million. We urge BPA to continue to reflect the region’s progress in renewable resources, and other areas, by adjusting its program budgets accordingly.

We do have one note of concern, however. With significant decisions with ratepayer impact, such as the acquisition of Klondike 3, real customer input is needed. This did not occur with respect to that acquisition. In the future, we would like to participate with BPA before resource acquisition decisions are made.

### **Transmission**

Since BPA’s proposed transmission program does not directly bear on the WP-09 power rate case, we will have comments later in the IPR process with respect to these issues.

## **Conclusion**

Thank you for the opportunity to submit these comments. Again, we appreciate the time and effort of BPA and other utility staff during this process. We look forward to working with you further on these important budget matters.