

2007 Wholesale Power Rate Case Initial Proposal

REBUTTAL TESTIMONY
IMPLEMENTATION OF SECTION 7(b)(2)

March 2006

WP-07-E-BPA-37



This page intentionally left blank.

INDEX

REBUTTAL TESTIMONY OF

BYRON G. KEEP, WILLIAM J. DOUBLEDAY, PAUL A. BRODIE,
AND MICHAEL MACE

Witnesses for Bonneville Power Administration

SUBJECT: IMPLEMENTATION OF SECTION 7(b)(2)

	Page
Section 1. Introduction and Purpose of Testimony.....	1
Section 2. Implementation of Section 7(b)(2).....	1

This page intentionally left blank.

1 REBUTTAL TESTIMONY OF
2 BYRON G. KEEP, WILLIAM J. DOUBLEDAY, PAUL A. BRODIE,
3 AND MICHAEL MACE

4 Witnesses for Bonneville Power Administration

5
6 **SUBJECT: IMPLEMENTATION OF SECTION 7(b)(2)**

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

8 *Q. Would you please state your names?*

9 A. My name is Byron G. Keep. My qualifications are contained in WP-07-Q-BPA-22.

10 A. My name is William J. Doubleday. My qualifications are contained in
11 WP-07-Q-BPA-11.

12 A. My name is Paul A. Brodie. My qualifications are contained in WP-07-Q-BPA-07.

13 A. My name is Michael Mace. My qualifications are contained in WP-07-Q-BPA-33.

14 *Q. Have you previously submitted testimony in this proceeding?*

15 A. Yes, we submitted direct testimony on BPA's implementation of section 7(b)(2) of the
16 Northwest Power Act identified as Keep, *et al.*, WP-07-E-BPA-27. Our direct testimony,
17 as well as this rebuttal testimony, is submitted on behalf of BPA.

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

19 A. The purpose of this testimony is to rebut certain arguments and assertions regarding the
20 section 7(b)(2) rate step contained in the direct testimony of Gary Saleba, Linc
21 Wolverton, and Kevin O'Meara filed on behalf of the Preference Customer Group
22 (PCG), WP-07-E-JP1-01.

23 **Section 2. Implementation of Section 7(b)(2)**

24 *Q. The PCG makes a number of arguments regarding the operation and purpose of section*
25 *7(b)(2) of the Northwest Power Act. (Saleba, et al., WP-07-E-JP1-01 at 2-4.) Do you*
26 *agree with these arguments?*

WP-07-E-BPA-37

Page 1

Witnesses: Byron G. Keep, William J. Doubleday, Paul A. Brodie, and Michael Mace

1 A. Legal issues regarding the operation and purpose of section 7(b)(2) will be addressed by
2 BPA counsel in BPA’s Draft Record of Decision. This testimony is not provided as
3 legal argument, but rather reflects our understanding of the section 7(b)(2) rate step
4 based on our extensive experience conducting the rate step in previous BPA rate
5 proceedings.

6 Q. *The PCG argues that section 7(b)(2) sets an upper limit, or “rate ceiling,” on how much*
7 *BPA can charge preference customers after July 1, 1985, under rates charged for their*
8 *general requirements. (Id. at 2.) Do you agree?*

9 A. No. The section 7(b)(2) rate step uses amounts projected under hypothetical assumptions
10 to calculate a credit to 7(b)(2) customers as part of BPA’s rate design. It does not set the
11 final rates to be charged to such customers. The 7(b)(2) rate step is not the most
12 important element of BPA’s ratemaking. The most important element of BPA’s
13 ratemaking is to establish rates that will recover BPA’s total costs. It is our
14 understanding that FERC’s approval of BPA’s rates depends upon BPA demonstrating
15 that its rates will recover its total system costs.

16 For over 20 years, BPA has noted that the section 7(b)(2) rate step is not the final
17 step in BPA ratemaking. Before BPA’s 1985 rate case, BPA established a *Legal*
18 *Interpretation of Section 7(b)(2) of the Pacific Northwest Electric Power Planning and*
19 *Conservation Act* (Legal Interpretation). We are not interpreting the Legal Interpretation
20 in this testimony, but simply note that it states that “implementation of section 7(b)(2),
21 and any subsequent reallocation pursuant to section 7(b)(3), will not conflict with the
22 requirements of section 7(a).” (*Id.* at 10.) Similarly, the Legal Interpretation states that
23 BPA must establish rates in accordance with section 7(a) in order to receive confirmation
24 and approval from FERC. (*Id.* at 9.) BPA will address issues regarding the interpretation
25 of the Legal Interpretation in the Draft ROD.

1 BPA also developed a *Section 7(b)(2) Implementation Methodology* in 1984
2 (Implementation Methodology). The Implementation Methodology also states that
3 section 7(b)(2) is not necessarily the last rate step because BPA must establish rates to
4 recover its costs. (*Id.* at 45.)

5 Furthermore, BPA's preference customers have admitted that the section 7(b)(2)
6 rate step does not establish an absolute "rate ceiling." In the Western Public Agencies
7 Group's ("WPAG") reply brief in challenges to BPA's 2002 power rates in *Golden*
8 *Northwest Aluminum v. Bonneville Power Administration*, Nos. 03-73426, *et al.*, WPAG
9 stated:

10 There is only one conceivable way that a conflict could arise between the
11 revenue sufficiency requirement of section 7(a) and the rate test and cost
12 reallocation directives of sections 7(b)(2) and (3). Such a conflict *could*
13 arise if the costs that must be excluded from the preference customer rate,
14 and allocated to the rates for "all other power sold by the Administrator"
15 pursuant to sections 7(b)(2) and (3) would raise such rates to a level that
16 the non-preference customers could not or would not purchase enough
17 power to recover all of the reallocated costs. In such a limited case, the
18 ability of BPA to collect from non-preference customers the full costs
19 reallocated to their rates under sections 7(b)(2) and (3) could jeopardize
20 BPA's ability to collect sufficient revenues to cover its total costs. *Such a*
21 *situation would violate the revenue sufficiency test set out in section 7(a),*
22 *and would require BPA to take action to reconcile these two directives.*

23
24 (WPAG Reply Brief at 5.) (second emphasis added). The situation WPAG describes
25 exists in the current rate case. There are no DSI loads, no investor-owned utility (IOU)
26 requirements loads, and the 7(b)(3) reallocation amount has made the PF Exchange rate

1 so high that there are no REP loads. BPA therefore must recover any remaining 7(b)(3)
2 reallocation amount from BPA's preference customers.

3 In addition, whenever the 7(b)(2) rate step has triggered in BPA's rate
4 development, BPA has always reestablished the IP-PF link after BPA conducted the
5 7(b)(2) rate step. This also shows that the 7(b)(2) rate step is not the final step in
6 developing BPA's rates.

7 *Q. The PCG claims that section 7(b)(2) excludes Residential Exchange Program (REP)*
8 *costs from BPA's rates for power sales to preference customers to the extent such costs*
9 *exceed specified benefits enjoyed by preference customers under the Northwest Power*
10 *Act. (Saleba, et al., WP-07-E-JP1-01 at 3.) Is this an accurate description?*

11 *A.* No. The 7(b)(2) rate step is not accurately described as a means of excluding REP costs
12 from BPA's PF Preference rate. REP costs can remain allocated to preference customers
13 even if the section 7(b)(2) rate step triggers. Thus, given a 7(b)(2) trigger, the resultant
14 7(b)(3) reallocation amount is not equal to projected REP costs. Removal of projected
15 REP costs is only one of the five assumptions BPA makes in conducting the 7(b)(2) rate
16 step. The 7(b)(2) trigger and the resultant 7(b)(3) reallocation amount are a function of
17 all five different, required assumptions, only one of which involves the REP. The 7(b)(2)
18 rate step can trigger in the absence of REP costs, as it did in BPA's WP-07 Initial
19 Proposal, and not trigger with substantial REP costs, as it has done in the past.

20 When BPA calculates the 7(b)(2) trigger, BPA cannot quantify the synergy
21 between the five assumptions that results in the trigger amount. It is not possible or
22 meaningful (because all five hypothetical assumptions must be made) to segregate the
23 individual component contributions of any single section 7(b)(2) assumption to the
24 trigger amount. Thus, to the extent possible, BPA removes the 7(b)(3) reallocation
25 amount from the costs allocated to the PF Preference rate, not simply REP costs or costs
26 of any other particular rate step assumption.

1 Similarly, when BPA reallocates the 7(b)(3) reallocation amount to non-
2 preference rates, BPA does not reallocate REP costs. The 7(b)(3) reallocation amount,
3 however, affects the net REP costs allocated to the PF Preference rate.

4 *Q. The PCG argues that if Program Case costs exceed 7(b)(2) Case costs, it means the total*
5 *amount charged under the tentative Program Case rate exceeds the cost BPA is*
6 *permitted to charge preference customers under section 7(b)(2). (Saleba, et al., WP-07-*
7 *E-JP1-01 at 3.) Is this an accurate statement?*

8 *A.* No. The PCG has oversimplified the section 7(b)(2) rate step and the section 7(b)(3)
9 reallocation after the rate step triggers. The actual trigger is the difference between the
10 average adjusted Program Case PF rates for the rate period plus the ensuing four years
11 (excluding applicable 7(g) costs) and the discounted average 7(b)(2) Case PF rates for
12 the rate period plus the ensuing four years. After the trigger is determined, in the form
13 of a mills/kWh rate, that trigger is multiplied by the PF Preference load in each year of
14 the rate period to calculate the amount of section 7(b)(3) reallocation for the rate period.

15 The trigger-derived 7(b)(3) reallocation amount is allocated, to the extent
16 possible, to non-preference customers' rates. This, however, is not the end of BPA's
17 ratemaking. For example, if BPA has costs remaining after running the 7(b)(2) rate step
18 that are not otherwise allocated, such as REP settlement costs, BPA must still allocate
19 such costs to ensure cost recovery. Therefore, simply because the 7(b)(2) rate step
20 triggers, it does not follow that the Program Case rate exceeds the costs BPA is permitted
21 to charge preference customers.

22 *Q. The PCG argues that BPA has not complied with its 7(b)(2) Legal Interpretation and*
23 *7(b)(2) Implementation Methodology because BPA's Program Case projects REP*
24 *participation and does not include costs associated with REP Settlement Agreements with*
25 *the IOUs. (Saleba, et al., WP-07-E-JP1-01 at 6-8.) Do you agree?*

26 *A.* No. The section 7(b)(2) rate step is conducted by comparing the costs of the Program

1 Case, which traditionally has included resource costs and loads of the REP, with the
2 7(b)(2) Case, which excludes the costs and loads of the REP and the other four
3 assumptions of section 7(b)(2). There is no indication BPA's Legal Interpretation or
4 Implementation Methodology considered the possibility of settlements of REP disputes,
5 which create REP settlement costs, but not REP resource costs or loads. BPA had to
6 implement the section 7(b)(2) rate step reflecting these unanticipated circumstances.

7 BPA recognized that the REP settlement benefits are simply monetary settlement
8 payments. They are not the same as the REP itself, which is comprised of (1) a power
9 sale from an exchanging utility to BPA at the utility's average system cost in the amount
10 of its residential and small farm loads, and (2) a power sale from BPA to the exchanging
11 utility's residential and small farm loads at the PF Exchange rate in the amount of such
12 loads. The REP therefore contains both resources and loads. Because there is the
13 possibility (regardless of BPA's REP forecast) that a utility could participate in the REP
14 during the rate period, BPA must establish a PF Exchange rate. If BPA did not establish
15 a PF Exchange rate, BPA could not implement the REP. During more than 20 years of
16 implementing the 7(b)(2) rate step, BPA has always established the PF Exchange rate
17 based, in part, on the forecasted resources and loads of the REP. REP resources and
18 loads have always been part of the Program Case and, when the 7(b)(2) rate step has
19 triggered, the 7(b)(3) reallocation amount has largely been reallocated to the PF
20 Exchange rate.

21 The existence of resources and loads directly affects the 7(b)(2) rate step.
22 However, including only REP settlement costs in the Program Case would create an
23 anomalous result. By removing the REP resources and loads from the Program Case,
24 which historically has included REP resources and loads, the Program Case would
25 contain only settlement costs. This would increase the costs in the Program Case while
26 reducing the loads in the Program Case, thereby creating an artificially and

1 extraordinarily high-cost Program Case rate that would be compared to the 7(b)(2) Case
2 rate, which is unaffected because no REP costs are included in the 7(b)(2) Case. This
3 would cause an artificially and extraordinarily high trigger and ensuing artificially and
4 extraordinarily high 7(b)(3) reallocation amount.

5 The REP is a basic assumption in the 7(b)(2) rate step. In simple terms, the
6 Program Case includes the REP and the 7(b)(2) Case excludes the REP and the other four
7 assumptions in section 7(b)(2). As noted previously, it was not anticipated that BPA
8 would enter into settlement agreements to resolve disputes arising under the REP.
9 Therefore, no guidance is provided on how to treat REP settlements in performing the
10 rate step, except that the REP itself is a central assumption in the rate step. BPA's WP-
11 02 rate case addressed this issue by starting with a Program Case reflecting the traditional
12 REP, running the Rate Design Step, calculating the rate step trigger, reallocating the
13 7(b)(3) reallocation amount to non-preference rates, then crediting BPA's rates for REP
14 costs avoided by the possible REP settlements, and equitably allocating REP settlement
15 costs to BPA's rates. This method allowed BPA to recover its costs and to equitably
16 allocate the REP settlement costs, which are costs not otherwise allocated. BPA is
17 conducting the 7(b)(2) rate step and 7(b)(3) reallocation in a similar manner in this
18 proceeding. Because BPA's Implementation Methodology does not address the
19 treatment of REP settlements in implementing the 7(b)(2) rate step, BPA's proposal is
20 consistent with the manner in which BPA has previously implemented the Methodology,
21 and with BPA's WP-02 rate proceeding. BPA will address the consistency of BPA's
22 proposal with BPA's Legal Interpretation in the Draft ROD. BPA also will address
23 whether there should be any revisions to the Legal Interpretation and Implementation
24 Methodology in BPA's Draft ROD.

25 *Q. Does BPA's approach produce a reasonable result?*

26 A. Yes. In BPA's WP-02 rate case, the IOUs raised numerous arguments challenging

1 BPA's implementation of the 7(b)(2) rate step and the implementation of the REP under
2 the 1984 ASC Methodology. The REP Settlement Agreements resolved these disputes.
3 In the absence of the REP Settlement Agreements, if BPA had adopted the IOUs'
4 positions on section 7(b)(2), the rate step would not have triggered. If this had occurred,
5 the PF Exchange rate would have equaled the PF Preference rate at 27.48 mills per kWh.
6 In this circumstance the IOUs would have received over \$329 million in REP benefits
7 each year. (Also, if the IOUs had prevailed on their challenges to BPA's
8 implementation of the REP, this alone would have produced \$323 million in REP
9 benefits each year.) Similarly, if there were no REP settlement and no trigger in the
10 instant case due to BPA adopting the IOUs' previous positions on 7(b)(2) issues, the PF
11 Preference rate (and PF Exchange rate) would be 34.8 mills per kWh.

12 In contrast, the PCG advocates fixing the PF Preference rate after the preliminary
13 7(b)(2) rate step. By doing so, it posits an average PF Preference rate of 27.2 mills per
14 kWh for FYs 2007-09. (Saleba, *et al.*, WP-07-E-JP1-01 at 10.) (This rate is flawed
15 because it does not reflect BPA's recovery of REP settlement costs.)

16 BPA's WP-07 initial rate proposal contains a PF Preference rate of 31.11 mills
17 per kWh. This is a reasonable result. The PF Preference rate is not the low rate
18 advocated by the PCG, nor the high rate that would occur in the absence of a trigger.
19 Instead, as one would expect for a rate that reflected a settlement of REP disputes, the PF
20 Preference rate proposed by BPA is between these two extremes.

21 *Q. The PCG argues that no REP will take place during the rate period because the IOUs*
22 *currently have REP Settlement Agreements with BPA and not Residential Purchase and*
23 *Sale Agreements (RPSA), which implement the REP. (Saleba, et al., WP-07-E-JP-01 at*
24 *7.) Do you agree?*

25 *A. The PCG's assumption is not necessarily correct. Although BPA's IOU customers*
26 *currently have REP Settlement Agreements with BPA, BPA's preference customers*

1 have challenged the validity of those Agreements in court. The parties are currently
2 waiting for the court to issue an opinion. If the preference customers prevail in their
3 challenge, the REP Settlement Agreements may be eliminated and the IOUs could
4 participate in the REP through RPSAs, even during the WP-07 rate period.

5 In addition, the IOUs are not the only utilities that can participate in the REP.
6 Public agencies also may participate. Although BPA's current forecasted ASCs in this
7 proceeding are too high for utilities to receive REP benefits, BPA must recognize that
8 changing conditions can increase utilities' ASCs during the rate period and make utilities
9 eligible to receive REP benefits.

10 *Q. The PCG claims that the REP Settlement Agreements provide monetary payments to*
11 *replace the method of calculating benefits as provided in section 5(c) of the Northwest*
12 *Power Act. (Saleba, et al., WP-07-E-JP1-01 at 7-8.) Is this correct?*

13 *A. No. The REP Settlement Agreements, as amended, only provide monetary payments to*
14 *settle disputes regarding the IOUs' claims concerning BPA's implementation of the*
15 *REP. The REP Settlement Agreements are not a substitute program for the REP.*

16 *Q. The PCG argues that BPA's allocation of section 7(g) REP settlement costs (after BPA*
17 *allocated the 7(b)(3) reallocation amount to non-preference rates) is contrary to BPA's*
18 *Legal Interpretation and Implementation Methodology. (Saleba, et al., WP-07-E-JP1-01*
19 *at 8.) Do you agree?*

20 *A. No. BPA's Legal Interpretation and Implementation Methodology are silent on how to*
21 *treat settlements of REP disputes. BPA, however, addressed this issue in BPA's WP-02*
22 *rate case. After calculating the 7(b)(2) rate step in the Rate Design Step, BPA had*
23 *additional, unallocated costs and benefits associated with its settlement of REP disputes*
24 *with the IOUs. BPA equitably allocates any costs and benefits that are otherwise*
25 *unallocated, which include the unallocated costs and benefits of REP settlements, to all*
26 *power rates. Therefore, in order to recover BPA's total costs, BPA equitably assigned*

1 the unallocated REP settlement costs and benefits to both preference and non-preference
2 rates (the Subscription Step).

3 The Implementation Methodology, which BPA has used for over 20 years, states
4 that the 7(b)(2) rate step is “conducted outside the mainstream of BPA’s rate
5 development process.” (Implementation Methodology at 45.) It has “no impact on rates”
6 until it is included in BPA’s rate design. (*Id.*) If an adjustment is made, it “must be done
7 within the overall framework of the rate development process and of BPA’s ratemaking
8 objectives and statutory requirements.” (*Id.*) The section 7(b)(2) rate step is a step in
9 BPA’s rate design process, which must be included in a manner that is “consistent with
10 other statutory provisions and BPA’s ratemaking objectives.” (*Id.*) By first
11 implementing sections 7(b)(2) and 7(b)(3), and then allocating otherwise unallocated
12 REP settlement costs equitably to both preference and non-preference rates, BPA
13 properly implemented the 7(b)(2) rate step.

14 *Q. The PCG argues that the Subscription Step ensures that section 7(b)(2) will not provide*
15 *preference customers with any protection from the “REP benefits” BPA incurs under the*
16 *REP Settlement Agreements. (Saleba, et al., WP-07-E-JP1-01 at 8.) Do you agree?*

17 *A.* No. First, REP settlement benefits are not REP benefits. REP benefits are the benefits
18 provided to exchanging utilities’ residential and small farm consumers under
19 implementation of the REP. REP settlement benefits, in contrast, are monetary amounts
20 paid to settling utilities to resolve disputes regarding the manner in which BPA
21 implements the REP. In addition, traditional REP costs and REP settlement benefit costs
22 are allocated differently. REP costs enter the ratemaking process as the costs associated
23 with REP resources and are allocated to preference and REP loads, if needed, and then to
24 other loads. REP settlement benefit costs, in contrast, are equitably allocated to power
25 rates.

1 Second, preference customers have received rate protection from the section
2 7(b)(2) rate step in BPA's Initial Proposal. BPA started the current ratemaking process
3 with the assumption that there were as many as twelve potential exchanging utilities. The
4 initial 7(b)(2) rate step had a Program Case with over 5900 aMW of PF Exchange load
5 and \$2.1 billion in gross REP costs. The resultant section 7(b)(2) rate step trigger was
6 8.1 mills per kWh. Through an iterative rate modeling process, the section 7(b)(3)
7 reallocation amount raised the PF Exchange rate, which in turn eliminated some potential
8 exchangers from receiving REP benefits, which then lowered the Program Case costs,
9 which then changed the section 7(b)(2) rate step trigger, which then changed the section
10 7(b)(3) reallocation amount, and so on. The iterations ended when all potential
11 exchanging utilities were eliminated and the gross cost of the REP became zero. In short,
12 BPA reallocated the 7(b)(3) reallocation amount to non-preference customers until there
13 were no more non-preference loads, and only then was BPA required to allocate a portion
14 of the 7(b)(3) reallocation amount to the PF Preference rate. BPA's preference customers
15 received protection from all of the trigger amount except that portion necessarily
16 allocated to the PF Preference rate to ensure that BPA could recover its costs. BPA,
17 however, still had to recover its total costs, including REP settlement costs, which were
18 equitably allocated to power rates.

19 Third, the REP Settlement Agreements resolved the IOUs' disputes with BPA
20 regarding implementation of the REP. These disputes exposed BPA and its preference
21 customers to over \$300 million per year in REP costs during the settlement period. The
22 REP Settlement Agreements resolved these claims for \$140 million per year during the
23 first 5 years of the settlements, or less than 50 cents on the dollar. BPA's preference
24 customers have received extensive cost protection from BPA's limited exposure to high
25 REP costs through the REP Settlement Agreements.
26

1 Q. The PCG has recalculated the section 7(b)(2) rate step in a manner it claims is consistent
2 with BPA's Legal Interpretation and Implementation Methodology. (Saleba, et al., WP-
3 07-E-JP1-01 at 9-10.) Do you agree?

4 A. No. To understand this response, it is helpful to review BPA's implementation of the
5 7(b)(2) rate step. BPA forecasted IOU and public utilities' REP resources and loads in
6 the Program Case. When the 7(b)(2) rate step triggered, the 7(b)(3) reallocation amount
7 was largely allocated to the PF Exchange rate. This was done in an iterative manner
8 whereby the addition of the 7(b)(3) reallocation amount increased the PF Exchange rate
9 and eliminated utilities from receiving REP benefits. In BPA's analysis, the PF
10 Exchange rate was thereby set at a level that was higher than any potential exchanger's
11 ASC. Therefore, no REP loads or gross costs of REP resources were included in the
12 Program Case.

13 The PCG analysis purports to include the cost associated with the IOU REP
14 Settlement Agreements in the Program Case rather than the traditional IOU REP. The
15 costs of the IOU REP Settlement Agreements are calculated by multiplying the
16 difference between the lowest cost PF rate and a market forecast rate by 2200 aMWs and
17 are approximately \$300 million. Because the difference between the lowest cost PF rate
18 and the market forecast rate is forecasted to be greater than zero for the rate period, the
19 PCG (under its approach) should have included the \$300 million of IOU REP Settlement
20 Agreements in the Program Case. Instead, the PCG arbitrarily assumed that the \$300
21 million would simply disappear (“[i]n our analysis, we have directly removed the REP
22 Settlement Agreement costs”, Saleba, et al., WP-07-E-JP1-01 at 11.)

23 Further, if the PCG had actually retained the calculated costs of the IOU REP
24 Settlement Agreements in the Program Case, approximately \$300 million per year, and
25 had not arbitrarily removed those costs from the calculation of their Program Case PF
26 rates, the 7(b)(2) rate step trigger would have been much higher. This would have caused

1 an extraordinarily high 7(b)(3) reallocation amount, which in the absence of non-
2 preference loads would have been reallocated to the PF Preference rate in order for BPA
3 to recover its total system costs. In fact, because the PCG's Program Case rates, after the
4 arbitrary removal of \$300 million per year, were similar to the Program Case rates BPA
5 produced after BPA's iterative process removed all potential exchanging utilities, the
6 PCG's Program Case rates would have been similar, if not equal, to BPA's Subscription
7 Step rates if PCG had not removed the \$300 million.

8 *Q. The PCG argues that BPA's allocation of the trigger amount to the PF Exchange rate,*
9 *which iterates to eliminate all utilities from the REP, demonstrates that, without any non-*
10 *preference loads to absorb the cost of the REP, BPA cannot provide any REP benefits to*
11 *utilities and remain consistent with sections 7(b)(2) and 7(b)(3). (Saleba, et al., WP-07-*
12 *E-JP-01 at 11.) Do you agree?*

13 *A.* No. First, the PCG refers to non-preference loads "absorbing the costs of the REP." As
14 noted previously, however, the 7(b)(3) reallocation amount is not equivalent to REP
15 costs.

16 Second, the fact that BPA might forecast no REP benefits in BPA's rate case does
17 not preclude BPA from providing REP benefits to utilities during the rate period. BPA
18 forecasts REP benefits in the rate case only for ratemaking purposes. During
19 implementation of the REP during the rate period, the rate case basis for BPA's REP
20 forecast may change significantly. BPA could pay REP benefits to utilities that were
21 forecasted not to receive benefits if, for example, BPA revised the ASC Methodology in a
22 manner that increased utilities' ASCs; or if a court remanded BPA's rates and subsequent
23 rate development lowered the PF Exchange rate; or under other circumstances.

24 Third, even assuming for the sake of argument that there were no REP benefits,
25 this would not preclude the proper payment of REP *settlement* benefits during the rate
26 period. REP settlement benefits are based on REP Settlement Agreements executed in

1 2000 for a 10-year FY 2002-11 term. BPA's estimate of the proper amount of payments
2 to settle REP disputes at that time justifies the continued payment of settlement benefits
3 during the contract period.

4 *Q. The PCG argues that BPA conducts the Subscription Step to avoid the consequences of*
5 *its calculation of the 7(b)(2) rate step. (Saleba, et al., WP-07-E-JP-01 at 12.) Do you*
6 *agree?*

7 *A.* No. As explained previously, BPA performs a Subscription Step in order to properly
8 develop its rates. BPA's calculation of the 7(b)(2) rate step in the Rate Design Step is
9 based on a forecasted REP. It would be inappropriate to use this calculation alone to
10 develop BPA's rates because it would not account for BPA's REP settlement costs.
11 BPA must establish rates in order to recover its total system costs. The Subscription
12 Step allows BPA to equitably allocate REP settlement costs, which are costs not
13 otherwise specifically allocated, to BPA's rates to ensure cost recovery.

14 Furthermore, had the PCG not arbitrarily removed \$300 million of REP
15 settlement costs, the PCG's resulting PF rates would be very similar, if not equal, to the
16 PF Preference rates that BPA calculated in the Subscription Step.

17 *Q. Does this conclude your testimony?*

18 *A.* Yes.

19
20
21
22
23
24
25
26