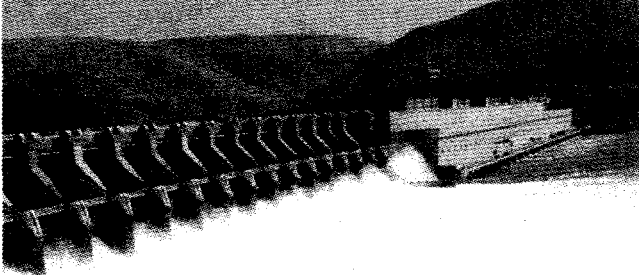


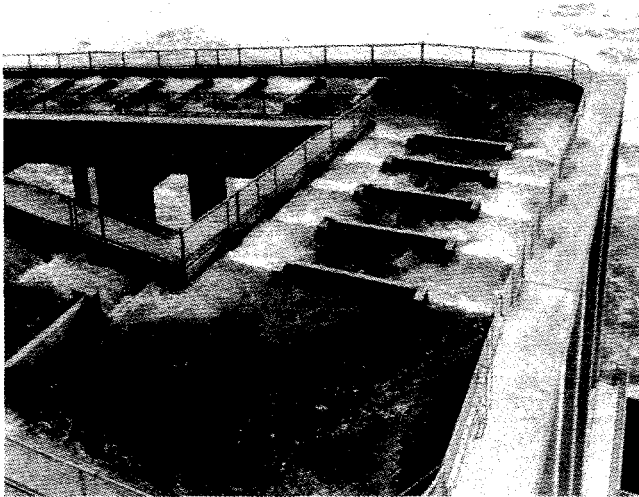
BONNEVILLE POWER ADMINISTRATION

DOE/BP-3125



POWER SUBSCRIPTION STRATEGY

DECEMBER 21, 1998



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Introduction – Sharing the Benefits

This document lays out the Bonneville Power Administration's "Power Subscription Strategy," a process that will enable the people of the Pacific Northwest to share the benefits of the Federal Columbia River Power System after 2001 while retaining those benefits within the region for future generations. The strategy also addresses how those who receive the benefits of the region's low-cost federal power should share a corresponding measure of the risks.

This strategy seeks to implement the subscription concept created by the Comprehensive Review¹ in 1996 through contracts for the sale of power and the distribution of federal power benefits in the deregulated wholesale electricity market. The success of the subscription process is fundamental to BPA's overall business purpose to provide public benefits to the Northwest through commercially successful businesses.

On Sept. 18, 1998, BPA released the "Power Subscription Strategy Proposal" for public review. We were gratified to receive almost 200 responses comprising nearly 600 pages of comments. We want to thank all commenters collectively and individually for taking the time to share their views and concerns on this important and complex issue. While BPA is responsible for the strategy's authorship, the fact is that many in the region including BPA customers, interest groups, other federal agencies, states, Native American tribes and concerned individuals have all contributed to its composition.

BPA's clean hydropower is increasingly valuable and promises to be even more so in the future as the agency follows a stringent cost-cutting program aimed at keeping its cost-based power rates significantly below market. BPA has provided five years of stable rates starting in 1996 and aims to provide another five years of rate stability and predictability starting with new power sales contracts that would go into effect in October 2001.

We believe that this subscription strategy reflects the Northwest's varied and complex interests and that it achieves an equitable distribution of the benefits of the Federal Columbia River Power System throughout the region, consistent with public preference. It presents our customers with access to cost-based power and flexibility through a variety of choices. It acknowledges our responsibilities to fish and wildlife in the region, and it offers a means for keeping energy conservation and renewable energy development alive and well. The strategy commits us to fulfilling our obligations to the nation's taxpayers by meeting our U.S. Treasury payments on time and in full.

The subscription strategy is premised on BPA's partnership with the people of the Northwest. BPA is dedicated to reflecting their values, to providing them benefits and to expanding and spreading the value of the Columbia River throughout the region. In this respect, the strategy has four principal goals:

- Spread the benefits of the Federal Columbia River Power System as broadly as possible, with special attention given to the residential and rural customers of the region;
- Avoid rate increases through a creative and businesslike response to markets and additional aggressive cost reductions;
- Allow BPA to fulfill its fish and wildlife obligations while assuring a high probability of U.S. Treasury payment; and

¹ A year-long review, carried out in 1996, by the four Northwest governors of how the region's electricity system should be structured.

- Provide market incentives for the development of conservation and renewables as part of a broader BPA leadership role in the regional effort to capture the value of these and other emerging technologies.

To help meet these goals, BPA will serve all public agency net firm load requirements placed on it. BPA's strategy is to provide approximately 1,800 average megawatts to residential and small farm consumers of investor-owned utilities (IOUs) – at least 1,000 average megawatts in power sales and an equivalent of up to 800 average megawatts in power or financial benefits. We expect to be able to serve all direct service industry loads that customers ask the agency to meet. We will carry out cost-effective power purchases only to the extent necessary and consistent with our overall rate and financial goals. We believe this approach will provide for the broadest possible distribution of federal power throughout the region.

Over the past year, BPA has worked intensively with interest groups, other agencies, Northwest tribes and customers to achieve a common understanding of how BPA will address the uncertainty of future fish and wildlife costs in its post-2001 power rates and contracts. This discussion has resulted in a set of eight principles for fish and wildlife funding, "Fish and Wildlife Funding Principles for Bonneville Power Administration Rates and Contracts" included in the appendix.

BPA is fully committed to meeting these principles in the subscription process and rate case. Analysis conducted before the draft subscription proposal indicated that the rate and contract provisions in the proposal would, in fact, carry out the fish and wildlife funding principles. The changes in the final subscription strategy enhance BPA's ability to meet the principles. However, this conclusion is subject to further testing in the rate case. If, upon further analysis in the rate case, the strategy contained here proves not to meet the fish and wildlife funding principles, then adjustments will be made to conform to the principles.

BPA intends to take a renewed leadership role in energy efficiency, renewable resources and new distributed energy technologies. BPA believes that the region stands to realize substantial value through lower long-term energy costs, lower emissions, lower investment in transmission and distribution infrastructure, better customer service and higher reliability by taking advantage of these technologies. This becomes especially important when the region is not in a power surplus condition and new resources are being developed. BPA plans to seek ways in which it can act as a regional catalyst for capturing this value primarily through market mechanisms and without placing significant upward pressure on BPA rates. The conservation and renewable discount proposal is one means of accomplishing this goal. Other steps BPA is taking in this direction include:

- Continuing to develop additional renewable resources within the expenditure cap recommended by the BPA Cost Review;²
- An aggressive effort to create and market "environmentally preferred" power products from BPA's system and the new renewable resources;
- Working with the Bonneville Environmental Foundation;³
- Continuing the market transformation effort BPA is currently funding;

² A 1997 review of BPA's future cost projections focusing in particular on the FY 2002–2006 period conducted jointly by the Northwest Power Planning Council and BPA using experts from private industry.

³ The foundation funds new renewable energy resources and fish and wildlife projects in the Northwest through premiums put on sales of BPA's environmentally superior power.

- Continuing BPA support of low income weatherization; and
- Completing the significant “legacy”⁴ conservation programs.

BPA intends to consult extensively with regional interests to find other opportunities to create environmental and customer value through these programs and technologies.

BPA will propose a conservation and renewable rate discount of \$30 million for customers who voluntarily choose to implement a wide range of energy conservation and renewables measures. In addition, if BPA’s actual financial performance turns out to be substantially better than the rate case plan, BPA may offer an additional discount as part of a mechanism for distributing dividends among key stakeholders. The first \$15 million in dividends would go to customers who carry out incremental conservation and renewables activities.

The subscription strategy is BPA’s attempt, through new power sales contracts with regional customers, to best meet all segments of our existing customers’ needs — public power, residential and small farm loads of investor-owned utilities (IOUs) and direct service industries (DSIs) — while also achieving important regional environmental objectives. It comprehends not only public power preference but also regional preference. This strategy enables us to serve residential and small farm consumers directly by providing power for sale to the IOUs and other purchasers qualified under BPA statutes to serve those consumers so that the benefits of the Federal Columbia River Power System flow throughout the region whether those consumers are currently served by public or private power. This strategy reflects BPA’s very roots.

This subscription strategy recognizes that our customers have unique needs, needs we’ve worked hard to address. For those in rural areas, we are committed to continuing the low-density discount. In addition, BPA is willing to negotiate nonrequirements surplus firm power contracts with rural customers to help mitigate for rate design changes if those changes prove to have inordinate effects on them.

We have responded to the call of our larger public agency generating customers for a new power product called Slice of the System. The details of the Slice product are being developed in an open process that will be completed before the beginning of the power rate case.

We’ve also acknowledged a customer concern about who would pay for general transfer agreements (GTAs) to deliver federal power to customers not directly linked to the federal transmission system. BPA believes it can carry these costs in power rates to ensure that customers who are not directly connected to the network transmission system will still get the benefits of low-cost federal power.

While BPA proposed differentiated rates in the subscription proposal, we are not as concerned with implementing that particular rate design as with achieving the cost recovery objectives that arise with serving new loads after the subscription power sales have been made. The final subscription strategy does not include differentiated PF(1) and PF(2) rates. For the FY2002-2006 rate period, sales that are made during the subscription window and those that are made after the window all will pay the PF rate. New sales made after the subscription window, however, would be subject to a targeted adjustment charge that would recover the cost of system augmentation BPA must undertake, if any, to serve the load. The targeted adjustment charge would be determined for each individual purchaser placing new load on BPA and would apply until those new loads can be reflected in BPA’s next general rate adjustment.

⁴ These are conservation programs begun in past years that will continue until existing contracts expire.

To sum up, we will sell our products in a way that reaffirms our commitment to fulfill our responsibility for fish and wildlife and at the same time present a package that preserves the region's historic low-cost federal power. The strategy acknowledges BPA's special relationship to Northwest tribes, and it provides a foundation for leadership in regional energy conservation and renewables. We believe this subscription strategy offers something for everybody, from the rural customer to our largest industrial customer, from the public power customer to residential consumers in IOU service areas. BPA believes the strategy is responsive to and balances the concerns and interests of its customers and constituents.

If you would like to talk to someone about this strategy, contact a BPA account executive or call BPA at 1-800-622-4519. Send written inquiries to: Bonneville Power Administration, P.O. Box 12999, Portland, OR 97212. Opportunities for further comment on rate-related issues also will be available in the power rate case that will begin in April 1999.

I. Subscribing to Federal Power

BPA proposes to open the subscription window in February 1999 and remain open for contract negotiations until 120 days after the Record of Decision in the 1999 power rate case is issued. Rates for post-2001 service will be set in this power rate case, which is scheduled to begin in April 1999. BPA and its customers can bilaterally negotiate and execute power sales contracts at any time during this period. Subscription contracts signed prior to the end of the rate case will be subject to the final rate(s) established in the rate case. Subscription power sales contracts will be generally effective on Oct. 1, 2001.

The strategy encompasses products, product pricing and contract elements. The product pricing elements will be carried into the rate case through the development of BPA's initial proposal for the rate case. Final decisions on those matters will be made in the 7(i) process.

All customers currently serving regional firm load or who become qualified BPA customers serving retail load are eligible to purchase firm power within the constraints of existing statutes.

BPA will meet all regional net firm load requirements of public agency customers. BPA's strategy is to provide the equivalent of approximately 1,800 average megawatts (aMW) in power sales to investor owned utilities for their residential and small farm consumers. Of this amount, at least 1,000 aMW would be in the form of power sales and about 800 aMW would be in the form of power or financial benefits. BPA expects to be able to meet all direct service industry load that DSI customers ask the agency to meet.

BPA proposes to develop rates for 2002-2006 that are significantly below market and approximately equal for all customer groups. The goal is to have no increase in the current Priority Firm rate. We believe this approach will provide for the broadest possible distribution of federal power throughout the region.

A. Serving Public Agency Loads

Public agency customers will be able to sign subscription power sales contracts for all of their regional load not currently being served either by customers' generating resources or long-term power purchase contracts that continue beyond 2001. Public agency customers will be able to continue Residential Exchange transactions under section 5(c) of the Northwest Power Act at the Priority Firm Exchange (PF Exchange) rate, subject to BPA purchasing power from other sources in lieu of purchasing power from the utility. In determining the amount of the subscription power sale, BPA will examine the factors described in section I.E.

1. Public Agency Annexed Loads

Public agency annexed loads are those loads that are added through mergers, consolidations and annexation among or between utilities. If annexations occur and power sales contracts for that annexed load are signed before the subscription window closes, that load will be served at the PF rate.

The following reflects BPA's concern about expanding BPA's load serving obligations and increasing costs for other customers. Annexed loads for which contracts are signed after the subscription window closes will be served according to the notice and rate treatment (for example, the targeted adjustment charge during the notice period) described in section III.A. If the load was previously served at PF, it would continue to be served at this rate during the notice period. If an annexed load were previously an IOU residential and small farm load that was receiving BPA power or other benefits, the annexed load will continue during the notice period to receive its prorated share of the power delivery or financial benefits as if it had remained an IOU residential and small farm load. All new large single loads will be served at the new resource (NR) rate. In determining the amount of the subscription power sale, BPA will examine the factors described in section I.E.

2. Public Agency Load Growth

BPA will offer load growth coverage under the full service and actual partial service products to all public agency customers under the same terms and conditions, with pricing to be determined in the rate case. Load growth coverage is not provided under the firm power block product. BPA plans to determine the cost of providing this service and equitably recovering these costs under the full service and actual partial service products. Load growth costs will be rolled into what previously was called the load shaping charge. To more accurately reflect what the product now covers, BPA is changing the name of this charge to load variance. All new large single loads will be served at the new resource (NR) rate.

3. Serving the Load of a New Public Agency

A new public agency that forms and qualifies for service under BPA statutes and signs a power sales contract within the subscription window will be offered power at the PF rate for its entire general requirements load obligation, except for any new large single loads, which would be served at the NR rate. New publics that sign contracts after the subscription window closes will be served according to the notice and rate treatment (e.g., the targeted adjustment charge during the notice period) described in section III.A. If the load was previously served at PF, it would continue to be served at this rate during the notice period. If the load was previously an IOU residential and small farm load that was receiving BPA power or financial benefits, the load will continue during the notice period to receive its prorated share of the power delivery or financial benefits as if it had remained an IOU residential and small farm load. In determining the amount of the subscription power sale, BPA will examine the factors described in section I.E.

4. New Preference Tribal Utility

Northwest tribes have expressed significant interest in becoming eligible to purchase federal power during the subscription process. Tribes have an independent means to form their own utilities and may qualify under BPA statutes to purchase power from BPA. They may qualify to purchase on a preference customer basis, depending on the type of utility formed.

New preference tribal utilities that form an electric cooperative utility, sign a power sales contract and qualify for service will be treated the same as other new public utilities, as described in section I.A.3. above and will be served at the PF rate. The loads of new preference tribal utilities that sign contracts after subscription ends will continue to be treated the same as other new publics who sign contracts at that time. BPA expects

new tribal entities to work collaboratively with the entities currently serving reservation lands. In determining the amount of the subscription power sale, BPA will examine the factors described in section I.E.

5. Customer Resource Replacement

Regional consumer loads currently served by a customer's 5(b)(1)(A) resources or 5(b)(1)(B) generating resources, including long-term contracts for nonfederal power purchases, will be served at the PF surcharge rate, which will reflect the cost of new resources.

6. Surplus Firm Power Contracts

Some small rural full service customers with heavy irrigation load could be inordinately affected by rate design changes in our final wholesale power rate schedule and may have no ability to respond to these changes. If this proves to be the case and based on the availability of surplus power, BPA would be willing to negotiate nonrequirements surplus firm power contracts with such customers.

B. Serving Residential and Small Farm Consumers of Investor Owned Utilities

Under the Residential Exchange Program established in section 5(c) of the Northwest Power Act, a Pacific Northwest utility (either a public utility or an investor-owned utility) may offer to sell power to BPA at the utility's average system cost (ASC). BPA purchases such power and, in exchange, sells the same amount of power to the utility at BPA's PF Exchange Rate. The amount of the power exchanged equals the utility's residential and small farm load. In past practice, no actual power sales have taken place, and BPA provided monetary benefits to the utility based on the difference between the utility's ASC and the applicable PF Exchange Rate multiplied by the utility's residential load. These monetary benefits must be passed through directly to the utility's residential consumers. The amount of Residential Exchange benefits depends in large part on the level of the PF Exchange rate. Generally speaking, the higher the PF Exchange rate, the lower the exchange benefits. If the PF Exchange rate is above market, utilities are unlikely to purchase the power offered by BPA under in-lieu transactions, and residential consumers would receive no benefits from the Residential Exchange Program.

In BPA's upcoming rate case, the current ASC methodology will be used for any Residential Exchange forecasts. Because the Residential Purchase and Sale Agreements (RPSA) that implement the Residential Exchange Program have been terminated or will terminate in 2001, new RPSAs must be negotiated for utilities choosing to participate in the Residential Exchange Program after 2001. BPA will determine the payment of negative deemer balances at the time BPA negotiates new RPSAs. BPA will determine the effect of negative deemer balances, if any, on individual IOU subscription amounts after reviewing the comments of interested parties, including the state public utility commissions, regarding such amounts.

BPA's strategy is that IOUs may agree to a settlement of the Residential Exchange Program in which they would be able to purchase a specified amount of power under subscription for their residential and small farm consumers at a rate approximately equivalent to the PF Preference rate. BPA expects that the statutory mechanism for providing such sales will be a contract under either section 5(b) or section 5(c) of the Northwest Power Act. BPA will determine in subsequent discussions which mechanism will be employed. Therefore, residential and small farm loads of the IOUs may receive benefits from the federal system through one of two ways. An IOU may participate in the established Residential Exchange Program as described above or it may participate in a settlement of the program through subscription. If an IOU chooses to request Residential Exchange benefits under section 5(c), then the subscription settlement amount for all the IOUs would be reduced by the amount that would have gone to the exchanging utility.

In subscription, BPA proposes a settlement in which residential and small farm loads of the IOUs will be assured access to the equivalent of 1,800 aMW of federal power for the 2002-2006 period. Of this amount, at least 1,000 aMW will be met with actual BPA power deliveries. The remainder may be provided through either a financial arrangement or additional power deliveries, depending on which approach is most cost-effective for BPA.

BPA and each IOU will set the physical and financial components of the subscription amount, by year, in the negotiated subscription settlement contracts. Any cash payment will reflect the difference between the market price of power forecast in the rate case and the rate used to make such subscription sales. The actual power deliveries for these loads will be in equal hourly amounts over the period. These deliveries can be made to IOUs or any entity eligible under BPA statutes to buy power to serve these residential and small farm loads.

BPA will offer a five-year and a 10-year settlement contract for subscription sales to the IOUs. Under the five-year contract, BPA will offer and guarantee 1,800 aMW of power and/or financial benefits for the 2002-2006 period. The IOUs' settlement of rights to request Residential Exchange benefits under section 5(c) of the Northwest Power Act will be in effect until the end of the five-year term of the contract. Under the 10-year contract, BPA will offer and guarantee 1,800 aMW of power or financial benefits for the 2002-2006 period and 2,200 aMW for the 2007-2011 period. BPA intends for this 2,200 aMW to be all power deliveries. If BPA is unable to deliver all power for the 2007-2011 period, a mechanism similar to that described above will be used for determining the financial component payment. The IOUs' settlement of rights to request Residential Exchange benefits under section 5(c) will be in effect until the end of the 10-year term of the contract. In the event of reduction of federal system capability and/or the recall of power to serve its public preference customers during the terms of the five-year and 10-year contracts, BPA will either provide monetary compensation or purchase power to guarantee power deliveries.

BPA will request comments from interested parties regarding the amounts of subscription power and benefits that should be provided to individual IOUs. The state PUCs have indicated that they will collaborate on a recommendation on this topic, which BPA would welcome. BPA must ultimately decide the appropriate amounts, after consideration of comments. BPA will then determine the appropriate amounts. The consumer bills of participating IOUs should designate "Benefits of the Federal Columbia River Power System" to describe the amount of benefits each consumer receives.

Subscription power (both the physical and financial components) will be transferable to an eligible entity qualified to take federal power that serves the residential and small farm load under the same general terms and conditions as the subscription purchase by the original IOU. BPA intends that a provision for assignment in the subscription contracts will provide the IOUs with sufficient flexibility to accomplish this goal.

BPA believes that it has an obligation to ensure that the benefits of federal power are provided to the intended recipients. For this reason, the subscription contracts with IOUs will include a provision permitting BPA to review the manner in which the benefits of the federal system, through subscription settlement of the Residential Exchange, are being provided to the intended beneficiaries.

BPA intends to ensure that the benefits of low-cost federal power are widely enjoyed by residential and small farm customers throughout the Pacific Northwest. The region needs to clarify how the benefits of low-cost in-region nonfederal resources are preserved to benefit regional consumers. An important consideration in BPA's proposal to sell power for service to residential and small farm customers of IOUs is that these sales not dis-

place low-cost nonfederal resources currently serving regional loads and which could then be used to serve loads outside the region.

C. *Serving the Direct Service Industries*

BPA's goal is to serve all direct service industrial loads that individual companies ask BPA to meet, and BPA expects to be able to do so. BPA is working with its industrial customers on a variety of power service measures in the event that power costs or customer energy demands significantly exceed our expectations. These measures include: working with some DSIs to bring low-cost power to BPA; adjusting the shape of deliveries of power; risk-sharing pricing arrangements; adjusting the volume of sales to industrial customers; and interruption provisions. BPA is confident that, if needed, a mix of these and other available measures will allow us to achieve the objective of broadly distributing the benefits of federal power in the region.

Subject to 7(i) process review and consistent with rate directives, the base Industrial Firm (IP) rate is expected to be approximately equivalent to the PF rate. The DSI secondary subscription product is no longer a part of BPA's subscription strategy.

D. *Serving Other Loads*

Other regional loads not addressed above may be served with federal power sales according to existing law. BPA also intends that any power remaining after all requests from regional loads are met will be sold extraregionally consistent with public preference and Northwest preference in existing law.

E. *Considerations in Providing Requirements Service*

Section 9(c) of the 1980 Northwest Power Act directs BPA, in making power sales, to consider whether power from a customer's firm resources that have been serving regional load is or will be sold outside the region. In determining the amount of requirements service BPA is obligated to provide, BPA will consider how customer firm resources that have been serving load are being disposed of. Such determinations are not part of this policy but would be addressed in future decisions. Further, BPA will review and apply standards defining which entities qualify for the purchase of net firm load requirements service.

II. Power Products and Services

This section addresses BPA's risk management strategy, the list of power products BPA will offer and the approach to pricing these services. The core product descriptions will form the primary basis of the initial power rate case proposal.

A. *Risk Management Strategy*

BPA faces a number of uncertainties in the 2002-2006 period that could significantly affect how it operates and successfully meets all of its public responsibilities. The most significant uncertainties are:

- **Hydro conditions** – The amount of power BPA has to sell directly depends on the available water supply and generation.
- **Market prices** – It is difficult to predict with certainty whether market prices will trend downward, remain about the same or go up. Market prices define the revenues BPA receives from surplus power sales and its costs for short-term power purchases.
- **Operating costs** – There are significant uncertainties in many of BPA's operating costs.

- **Fish and wildlife costs** – For planning purposes, BPA will use the full range of potential fish and wildlife costs and financial impacts currently under discussion for the 2002-2006 rate period. The range is currently estimated at \$438 million to \$721 million annually.

A key principle of BPA risk management is to manage risks through a comprehensive plan that incorporates a set of risk management tools. The ability to manage risk using these tools is measured by the U.S. Treasury payment probability. Statutes defining priority of payments dictate that BPA's annual Treasury payments be made after other payment obligations are satisfied. Therefore, the probability that BPA can pay Treasury is the key indicator of the agency's cost recovery potential. BPA modeling captures all of the major sources of uncertainty that PBL may face in meeting its obligations. To ensure recovery of its power costs, BPA will use a combination of the following tools to manage power risks. The specific mix and design of these tools will be determined, as appropriate, in the rate case and the subscription process:

- Implement the principles for fish and wildlife funding, including risk management principles, in rates and contracts. The fish and wildlife funding principles are included in the appendix.
- Implement any possible additional cost-reduction efforts to reduce internally manageable costs, exclusive of fish and wildlife costs, before exercising any contingent cost recovery mechanism.
- Encourage staggered contract terms – some shorter than five years and some longer than five years.
- Offer cost-based indexed pricing as an option for some products.
- Use reserve balances carried into the 2002-2006 rate period as a risk mitigation tool.
- Use 4(h)(10)(C) credits allowed by the Northwest Power Act against BPA's Treasury payment. (The credit is for about 27 percent of certain fish and wildlife expenditures BPA makes each year that are not related to the hydropower system. The statutory basis for 4(h)(10)(C) is that ratepayers should not be responsible for fish mitigation costs that are not attributable to electricity production.)
- Access the Fish Cost Contingency Fund (currently \$325 million) under certain narrowly defined circumstances. This fund represents past money BPA has paid for fish and wildlife costs associated with the nonpower uses of the region's federal dams but for which the agency has not taken 4(h)(10)(C) credits.
- Subject to the rate case, BPA proposes using an adjustment to posted prices, known as a cost recovery adjustment clause (CRAC), in its firm requirements rate schedules. All net firm power load requirements customers would be subject to a CRAC. BPA believes that a CRAC of about \$100 million per year would be adequate to maintain the desired Treasury Payment Probability, but the final determination of the amount will be made in the rate case.

Under one approach BPA is considering, CRAC would trigger based on BPA's projected financial reserves at the end of the second quarter of each fiscal year. If Power Business Line financial reserves appeared likely to fall below a certain threshold, BPA would conduct a public review process. After public review of the financial reserve projections, BPA would make any necessary revisions and, if the revised projections were below the threshold, the cost recovery adjustment would trigger. Posted prices would increase effec-

tive the first day of the next operating year. The adjustment would terminate after one year if projected financial reserves rose above the threshold. BPA is also considering other approaches.

- In the 1999 power rate case, BPA will propose criteria and mechanisms for distributing “dividends” among key stakeholders during the 2002-2006 rate period if actual financial performance turns out to be substantially better than the rate case plan. BPA will propose that the threshold for triggering a dividend distribution be based on accumulated net revenues. The threshold would be set at a level substantially above the rate case plan. The mechanism would not trigger if post-2006 expenses are expected to rise substantially or if the uncertainties related to fish costs have not been resolved. The “dividends” would be distributed among customers, U.S. Treasury, conservation and renewable initiatives, and other public purposes. The first \$15 million in dividends would go to customers who carry out incremental conservation and renewables activities. (See section III.F.)
- As with pre-subscription contracts, both parties in subscription power sales contracts will preserve their rights regarding transmission surcharges. BPA will set power rates adequate to meet the Treasury Payment Probability target without reliance on a cost recovery mechanism on the transmission system.

B. Product Categories

There will be three product categories: core subscription, customized subscription and nonsubscription. BPA will include in the posted rates for core subscription products only those risks that apply to all customers purchasing core subscription products. Some risks, such as the risk of fluctuations in small generating resources, are assumed to be so minimal that they will be rolled into the posted rates. Some customers require additional flexibility beyond that embedded in the core products. Customizing core products will provide this additional flexibility. The primary reason for a distinction between the core and customized subscription products below is to ensure that only those customers who stand to benefit from additional risks assumed by BPA on their behalf are required to pay the related costs. The lists of nonsubscription products are offered as examples of the types of service BPA can provide. These products may be bilaterally negotiated and the price will be set under BPA's Firm Power Products and Services rate schedule.

1. Core Subscription Products

These products are available to customers who request requirements service to serve load and accept constraints on their ability to shape their purchases from BPA for any reason other than following variations in consumer load. All core subscription products are undelivered. All core subscription products will be offered at BPA's posted rates.

2. Customized Subscription Products

Customized products are available to customers who request firm power load requirements service to serve load (core products) and who want additional flexibility to reshape their purchases from BPA in order to optimize their nonfederal resource operations. These products will have bilaterally negotiated pricing for all modifications to core products and any additional products and services customers wish to purchase. BPA anticipates that the price for customized products that differ substantially from the core products will be negotiated under the Firm Power Products and Services (FPS) rate schedule. The Slice of the System is a firm power requirements product and a surplus service and will be priced by a formula to be developed during the power rate case.

PRODUCTS

CORE SUBSCRIPTION PRODUCTS

Full Service
Actual Partial Service
Block Partial Service
Factoring

CUSTOMIZED SUBSCRIPTION PRODUCTS

Variable Load Factor
Slice of System
Renewable Resource

NON-SUBSCRIPTION PRODUCTS

Bilateral Products & Services
*Power – Firm, Secondary, Commodity
(including loss compensation)*
Capacity w/out Energy
Storage
Resource Factoring
Displacement
Scheduling Services
Reserves, Resource Support
Supplemental AGC
Operating Reserves
Forced Outage Reserves
Complements to Core Products
Block Flexibility
Retail Access – Mitigation

3. Non-Subscription Products

This category broadly includes power products and services that BPA might sell to any customer in the marketplace. These products will have prices negotiated under BPA's Firm Power Products and Services (FPS) rate schedule within the existing cost-based cap for that rate schedule.

The products in each category are identified in the following table. For detailed product descriptions, refer to the BPA Power Product Catalog available from BPA account executives or on the Power Business Line Web site.

C. Slice of the System

BPA will offer a new product, a Slice of the System arrangement, in subscription. The final details of the Slice product will be developed in working sessions open to interested parties. These discussions are expected to conclude before the end of January 1999.

The Slice product is a firm power sale that reflects, by formula, the operating shape of BPA's resources. The product includes the right to modify the rate of delivery of energy within the day, week, month and year proportional to BPA's own generation capability. Generation capability in this context means the maximum and minimum rate of delivery in any given hour that BPA must itself observe in combination with its ability to store and release energy. BPA and other federal agencies will continue to establish FCRPS operating constraints and those will not be affected by the Slice.

Slice purchases will be used to meet the net firm power requirements loads of public agencies and cooperatives in the Pacific Northwest. However, the Slice product will provide more power in certain periods than the purchaser's net firm load requirements alone. In these periods of the year, the Slice product also will provide surplus firm power and nonfirm energy to purchasers. The firm component of Slice purchases will be limited by the customer's net requirements, as determined by BPA's forecast of the purchaser's firm consumer loads and the declared firm resources of the purchaser under section 5(b) of the Northwest Power Act. Because the share of generation capability available to the purchaser may exceed that purchaser's monthly or hourly requirements under section 5(b)(1) of the Northwest Power Act, BPA will contractually establish a mechanism to buy back the "excess" if and when necessary to assure service to BPA's other statutory or contractual commitments in the Pacific Northwest. The specific methodology for the buy-back will be developed in discussions with interested parties prior to the power rate case.

Slice commitments will be for 10 or more years. The product may be purchased in combination with annual firm blocks but not with full service or actual partial service. A Slice purchaser will have the right to buy BPA firm power after the Slice contract expires.

Payment for Slice will be based on a percentage of BPA's Power Business Line revenue requirements for each year of the contract. The only excluded costs are the costs of short-term power purchases, costs of resource acquisitions that are not for public purposes or for relief of the initial inventory constraint, and payments to the Transmission Business Line for transmission of federal power from generating resources to other purchasers. (This exclusion does not include any costs of GTA service that are part of the PBL revenue requirement.) Purchasers of Slice shares will pay their proportionate share of the net costs of relieving the expected FCRPS inventory constraint, whether that solution is power purchases, cash payments or another solution. Purchasers of Slice shares will assume an appropriate share of planned net revenues for risk, either by assuming risks directly or by adjustment to the Slice payment. The specific methodology that will be used, if any, will be developed in further discussions with interested parties prior to the power rate case.

Slice is a bundled product with a melded set of Power Business Line costs. Purchasers of Slice accept a broad and diverse set of risks commensurate with the broad features of the product. Initial attempts to identify cost shifts between Slice purchasers and purchasers of other products demonstrated results that were inconclusive and highly dependent on assumptions used. BPA does not plan to evaluate in detail the potential costs shifts to or from Slice purchasers in the power rate case.

III. Pricing

A. Public Agency Customers

Subscription power sales (contracts signed before the close of the subscription window) to public agency customers will be under the PF rate. New public agency sales made after the subscription window will pay, during an interim notice period, the PF rate plus an individually targeted adjustment charge. The adjustment charge would reflect Federal Base System (FBS) resources, if any are available to serve the new sale, and the market price of power BPA purchased to serve that sale, if any. New sales would continue to pay the PF rate with the targeted adjustment charge until the next rate period in which those sales could be reflected in BPA's rate studies. At that point these sales would pay a PF rate without the targeted adjustment charge. The costs to serve these new sales would be melded with other costs to recalculate the PF rate for these loads for the 2006–2011 period. New large single loads will be served at the NR rate.

Option fees have been dropped from the subscription strategy. Instead, only customers who make commitments greater than five years will get a contractual guarantee of BPA's lowest cost-based rate beyond FY 2006.

BPA intends to assure that this guarantee will provide benefits to those customers that make a longer-term commitment. One approach that would provide such a benefit would be the following: BPA could decide that this lowest cost-based rate would bear the costs associated with loss of system capability but, in the future, would be protected from costs associated with serving additional load placed on BPA after the subscription window closes. BPA could decide that there would be a separate melded rate that includes the costs associated with serving these additional loads.

There may be other approaches that deliver a clear benefit to those who make long-term subscription commitments. A final decision on the rate construct to assure this benefit will be made in future rate cases.

In addition, the PF surcharge rate described in the Sept. 18 Power Subscription Strategy Proposal is being retained for sales to a customer's regional net firm loads that were previously served by its 5(b)(1)(A) and 5(b)(1)(B) generating resources, including long-term power purchase agreements.

1. Stair-Stepped Rates

BPA expects its costs will be higher in the later years of the rate period because of the unpredictability of certain costs in those years due to market volatility, fish and wildlife funding and resource capability. To account for the potential increase in its costs, BPA intends to develop a two-part, stair-stepped posted rate. The rate step will increase in the fourth year of the rate period. The three-year rate will recover forecast costs, including risk, for that period. The last two years will cover those forecast costs and any increased costs and risks.

As described in section IV.D. below, a customer may choose to enter into either a three-year or longer contract. For the longer contract, the rate for years one through three will be the lower stair-stepped rate and the rate for years four and five will be the higher rate established in the 1999 rate case. A customer who signs a three-year contract will pay the lower stair-stepped rate, established in the 1999 rate case, for those three years. If that customer subsequently signs a contract for years four and five, that customer will pay a rate that will be established in a separate 7(i) process that will occur after the 1999 rate case.

It is important to note that the entire five-year posted two-part rate is the "lowest-cost-based rate." Typically in the rate setting process, rate models calculate a "rate" for each year of the rate period, and

then those rates are averaged to establish the single posted rate. We propose to use a similar calculation, but average only the first three years of the rate period and then the last two years, to develop the entire five-year rate. This concept will be more fully developed in the power rate case initial proposal. In addition, BPA will post a five-year average rate to be applied to the pre-subscription contracts BPA has already entered into for the post-2001 rate period.

2. Low Density Discount (LDD)

BPA plans to continue the Low Density Discount including the calculation of the kilowatt-to-investment (k/i) ratio. Some modifications will be proposed to avoid increases in program costs.

B. Residential Exchange

PF Exchange Rate

IOUs and public agencies with residential and small farm loads will have the ability to continue the Residential Exchange Program under section 5(c) of the Northwest Power Act, subject to in lieu transactions. Such sales will be made at the PF Exchange Rate. The section 7(b)(2) rate test will be run consistent with the Northwest Power Act and the description in section I.B above. A PF Preference rate and a PF Exchange rate will be published. If the 7(b)(2) rate test does not trigger, the PF Preference and PF Exchange rates will be equal; if the 7(b)(2) rate test does trigger, then the PF Preference rate and the PF Exchange rate will differ. The current Average System Cost (ASC) methodology will be used for any Residential Exchange forecasts. Because the Residential Purchase and Sale Agreements (RPSAs) that implement the Residential Exchange program have been terminated or will terminate in 2001, new RPSAs must be negotiated if any utility chooses to participate in the Residential Exchange Program after 2001. BPA will determine the payment of negative deemer balances at the time BPA negotiates new RPSAs.

C. Investor-Owned Utility Residential and Small Farm Loads

1. Physical Deliveries

Instead of participating in the Residential Exchange Program, IOUs may enter into a settlement of the program comprising a power sale and, potentially, a financial payment. BPA expects that the statutory mechanism for providing such sales will be either under section 5(b) or section 5(c) of the Northwest Power Act. It will be determined in subsequent discussions which mechanism will be employed.

Consistent with the principles described in section I.B above, BPA will sell a limited amount of power to the IOUs for their residential and small farm loads. These sales will be at a rate approximately equal to the PF Preference rate, subject to establishment in BPA's rate case and consistent with BPA's rate directives. These sales will be made under at least the following terms and conditions:

- The purchaser (IOUs with residential and small farm loads) will waive the right to request further benefits under section 5(c) of the Northwest Power Act for the term of the subscription contract;
- If subscription sales are made under section 5(b), BPA will serve additional requirements requests from IOUs under section 5(b) at the NR rate.

The rate proposed for the 2007-2011 period, subject to establishment in a section 7(i) hearing, would be approximately equal to the PF Preference rate established for that period.

2. Financial Component

For the amount of subscription sales not made through physical power deliveries, BPA will provide a cash payment that reflects the difference between the market price of power forecast in the rate case and the rate used to make such subscription sales.

D. Direct Service Industries

Subscription sales to DSIs from BPA's firm inventory may be made pursuant to section 5(d) of the Northwest Power Act. Subscription sales to the DSIs will be made at an IP rate approximately equivalent to PF consistent with rate directives and subject to establishment in BPA's rate case.

E. General Transfer Agreements (GTAs)

A General Transfer Agreement is a contract in which BPA pays a fee to transfer BPA power over another utility's transmission system for delivery to a BPA customer. BPA intends to continue existing GTA service to customers for delivery of federal power through the term of their subscription contracts. The costs for this GTA service or replacement service for federal power deliveries will be spread over all Power Business Line power sales.

This service will not be available to new preference customers or to existing preference customers for service territory expansions. For GTA agreements that expire before 2006, BPA will attempt to negotiate their extensions through 2006. If unsuccessful in this attempt, BPA will arrange for open access tariff transmission to replace the GTA for delivery of federal power to GTA points of delivery. Any GTA charges that are directly assigned to customers will conform with the BPA Transmission Business Line's Direct Assignment Guidelines. GTA costs associated with significant energy imbalance "overruns" may result in the Power Business Line requiring individual GTA customers to pre-schedule and to be directly assigned any energy imbalance charges incurred. This is most likely to occur in situations where large industrial loads fluctuate with no advance notice. GTA customers will purchase ancillary products, such as load regulation, from the Transmission Business Line.

The Power Business Line will not provide for delivery of nonfederal power to GTA points of delivery.

F. Conservation and Renewables

BPA enjoys an important role in providing support for the development of energy conservation and renewable resources. Although BPA plans no generating resource acquisitions in the near future, the region is moving into load resource deficit. As the region moves into a new era of resource development, the need for critical priorities on energy conservation and renewable resources increases. BPA wants to serve as a catalyst in encouraging its customers to make investments in these important and valuable resources. Further, BPA wants to complement and supplement the efforts of state legislatures and the Northwest Power Planning Council in addressing the regional need to develop these resources. BPA plans to seek out a variety of means by which it can add to the regional momentum toward capturing the value of conservation, renewables and emerging distributed energy technologies. Rate design and the conservation and renewables discount proposals are only part of this effort.

BPA believes it can use its power pricing to best communicate the cost of resources and the priorities for developing conservation and renewable resources. The rate design for the new rate period will reflect new values of on-peak and off-peak energy. On-peak energy purchases will likely increase in price while off-peak purchases will decrease in price. These changes should motivate customers to take conservation actions to reduce their peak use of energy.

In addition, BPA intends to use its power rates to support power customers who voluntarily choose to finance

their own development of conservation or renewable resources. Specifically, in the rate case BPA plans to propose a base discount not to exceed 0.5 mills per kilowatt-hour (approximately a total annual discount of \$30 million). This base discount would be dollar-for-dollar. Very small customers would have requirements that reflect their specific capabilities. BPA intends to offer an additional discount if the agency's actual financial performance turns out to be substantially better than the rate case plan (see the "dividend" discussion in section II. A). The first \$15 million of a dividend distribution would go to customers who carry out incremental conservation and renewables activities. This money could be leveraged with a 2-for-1 discount structure to create an incentive for significant additional investment on top of the base discount. This rate discount should provide an incentive for customers to meet the Comprehensive Review's goal of supporting conservation and renewables through local action. BPA will also take into consideration actions by the states such as uniform public benefits charges. To make it simple to administer, BPA intends to rely on a regional forum to propose actions that would qualify for the discount.

G. Indexed Cost-Based Rates

Customers may choose to convert their fixed price net firm load requirements service rates to a market-indexed price, adjusted for BPA's risk, that reflects equivalent expected revenues at the time the contract is signed. This will be offered as BPA currently does under the PF and NR rate schedules. Customers may also choose to purchase surplus firm power indexed to the California-Oregon Border, New York Mercantile Exchange or other mutually agreed-to indices.

IV. Contract Elements

A. Bilateral Contract Negotiations

BPA intends to conduct bilateral negotiations with each of its customers to develop a contract that establishes the specific business relationship between that customer and BPA. Each contract will be based upon the subscription strategy and decisions contained in BPA's final Record of Decision on subscription contracts.

B. Standard Provisions

Although BPA intends to bilaterally negotiate contracts with its customers, some issues will be guided by a framework of standard provisions that would apply consistently across all subscription contracts. In all contracts, BPA and the customer will preserve their rights concerning emergency cost recovery through transmission rates.

BPA plans to sponsor a public review of standard contract provisions on dispute resolution, uncontrollable forces and cost recovery.

C. Contract Types

BPA will no longer make a distinction between umbrella and commercial contracts. By offering bilateral negotiations to its customers, BPA already is open to negotiate different types of arrangements to meet the needs of individual customers. The contracts BPA offers will be flexible enough to allow customers to purchase power with a portfolio of the rate choices applicable to that customer's purchases.

D. Contract Length

In subscription, BPA is attempting to provide various incentives for customers to choose between three-year contracts, five-year contracts and contracts longer than five years.

BPA and its customers have several business goals that can be met by having power sales contracts of various lengths (or terms). For example, by staggering or varying the terms among power sales contracts BPA will

reduce its exposure to a future revenue "cliff" (a condition that occurs when all contracts expire simultaneously). Some BPA customers have consumers who are also interested in shorter-duration power purchase commitments. Also, contracts of varying terms will give BPA the ability, if necessary, to collect greater revenues if costs, and the market, increase in the later years of the rate period. BPA proposes to use the following two-part incentive to encourage differing contract terms.

1. Contracts Shorter than Five Years

BPA will offer contract incentives to customers who choose to purchase a three-year contract. Specifically, BPA would waive the take-or-pay provisions for the risk of losing load due to retail open access. That is, if a customer purchases requirements power for a three-year period, the customer will not need to purchase one of the products described in sections IV.G and IV.H. of this document to mitigate customer risk due to retail load loss. As described in section III.A.1, customers will likely pay a lower stair-stepped rate in years one through three than would apply in years four and five. In addition, BPA may develop other contract incentives.

2. Contracts Longer than Five Years

The Comprehensive Review recommended that BPA preserve its lowest cost-based rates for customers who make long-term purchase commitments. Contracts between five and 20 years are another element in BPA's strategy to reduce risk. Therefore, for customers who commit to purchasing for longer than five years, BPA will provide a contractual guarantee to power at the lowest applicable cost-based rate. One approach to assuring that this contractual guarantee has value is discussed in section III.A.

E. Future Price Guarantees

BPA will not offer price guarantees for cost-based purchases beyond the period covered by a customer's contract and the associated rates. Customers who want such financial arrangements can purchase them from other providers in the market.

F. Take-or-Pay and Retail Access Load Loss Risk

Previous BPA power sales contracts gave customers considerable flexibility to increase or reduce their purchases by adding or removing non-BPA firm resource power supplies on relatively short notice. BPA proposes that most of its contracts will require customers to continue to purchase federal power under most circumstances. However, eligible customers will still be able to purchase a net firm load requirements service in which BPA absorbs load fluctuations due to weather, plant closures and load growth.

BPA uses the term "take-or-pay" to describe the contractual situation in which the customers will not be permitted to replace BPA as the power provider for the load the customer has contracted with BPA to serve. The customer will bear the risk of losing load due to retail open access whether that access is voluntary or legally mandated. This risk of load loss due to retail access is a largely new risk factor that must be managed. Most customers are likely to mitigate their take-or-pay risk by having "at risk" consumers sign power purchase contracts in the event of legally mandated retail open access laws. BPA will take on the risk of retail load loss under limited circumstances: (1) For full service customers, BPA will accept the risk of retail access load loss for loads smaller than 250 average kilowatts; and (2) BPA will accept all risk of retail access load loss for customers who purchase power from the agency for a contract term of three years or less.

In a retail competition environment, there are at least two ways that consumer load within the territory of a net requirements customer of BPA could explicitly avoid being served with power the utility purchases from BPA: (1) The consumer could choose to purchase from a supplier other than the utility or (2) the consumer could

choose a utility-offered portfolio option other than the BPA-power option. In such cases, BPA will consider that consumer load to no longer be part of that utility's net firm load requirement. Should that load later take action to become part of that utility's net firm load requirement, BPA will treat that load as if it were a new request coming after the close of the subscription window. In such cases, the load will be served according to the notice and rate treatment described for such circumstances in section III.A.

In addition, BPA plans to offer two product mitigation measures and two contract mitigation measures for customers who do not mitigate this risk themselves. With the exception of the walled-off load measure, customers may postpone selecting an appropriate mitigation measure until the state in which it is operating adopts a retail access plan. Once that occurs, customers will have a limited period (120 days) to make their selection. In some cases, it may not be possible to offer mitigation if the customer has lost the load prior to selecting a mitigation measure. The measures available to mitigate a customer's financial risk due to take-or-pay are listed below.

G. Contract Mitigation Measures

1. Conversion to Excess Federal Power (EFP)

BPA will offer a contract provision that allows the conversion of PF purchases to EFP if the EFP is available and the customer loses load due to retail access and cannot serve that load with its take-or-pay power purchase obligation. A conversion to available EFP will allow the customer to resell the power. Before making the conversion, however, BPA will have the option of reducing the customer's take-or-pay obligation and taking back the power. BPA's decision whether to exercise the option to reduce the customer's take-or-pay obligation, concurrent with disapproving the conversion to EFP, will be driven by its statutory obligations and its load/resource situation. For example, if BPA had requests for requirements service that it could not meet within the existing FBS, it could not approve a conversion to EFP.

2. Walled-off Loads

As an alternative, and prior to execution of the contract, BPA and a full service customer may agree that neither BPA nor the customer will be obligated to provide firm power to a specific retail load that desires to purchase power from another source. A specified portion of the load of a full service customer may be excluded from the utility's BPA purchase. The utility will be eligible to purchase from BPA power service for only the remaining portion of its load. If that specified load later takes action to become part of the utility's net firm load requirement, BPA will serve that load according to the notice and rate treatment described for new loads in section III.A.

Walled-off loads must be separately metered on an hourly basis. The utility must hold BPA harmless and indemnify BPA from any third-party claim. This service will only be available before the contract is signed and can not be elected during the term of the contract. The ability to wall-off a load is not a customer right. It is a discretionary decision to be made by BPA working with the customer. The decision to allow only full service or to give partial service customers the ability to "wall-off" a load will be decided on a case-by-case basis and will depend, in part, on the business risk to BPA.

H. Product Mitigation Measures

BPA will continue to offer products that customers may purchase to mitigate the effects of take-or-pay due to retail access.

1. Insurance

The customer may purchase an insurance product to reduce the financial risk associated with retail load losses under firm power take-or-pay contracts if the law mandates retail open access.

2. Remarketing

The customer may purchase a product that uses BPA's services to remarket the power to an alternate source if the customer loses load due to retail open access. The customer must continue to pay for the power but BPA will provide a credit to the customer for the amount of energy remarketed based on a formula using the Dow Jones Mid-Columbia Daily Diurnal Index or some similar index. The amount of this credit will not be capped at the sum of the PF rate plus the remarketing fee owed to BPA.

I. Customer Pooling of Requirements Purchases

BPA has had a policy based on the directives and purposes in the Bonneville Project Act and the Northwest Power Act that sales of power to individual utility customers is based on the difference between a utility's firm resources and its firm consumer load in the region. A few customers have asked about creating an entity that would allow the utilities to pool their 5(b)(1) net firm power load requirements purchases. This would provide both administrative savings and enhanced risk management opportunities. Currently, requirements firm power is not pooled but sold for an individual customer's net firm load. Legislation that had been pending, but which died in the 105th Congress, would have allowed BPA to sell such power to a "joint operating entity." If appropriate legislation is passed in the future and if any customers create a joint operating entity to purchase and pool federal power, BPA will consider the modification of customers' contracts on mutually acceptable terms and conditions. Customers may create other pooling arrangements and BPA will remain open to examining those in light of its statutory directives.

Appendix

Fish and Wildlife Funding Principles for Bonneville Power Administration Rates and Contracts

September 16, 1998

PREAMBLE

The purpose of these principles is to conclude the fish and wildlife funding process in which Bonneville has been engaged with various interests in the region and provide a set of guidelines for structuring Bonneville's subscription and power rate processes. The principles are intended to "keep the options open" for future fish and wildlife decisions that are anticipated to be made in late 1999 on reconfiguration of the hydrosystem and in early 2000 on the Northwest Power Planning Council's Fish and Wildlife Program.

The agreement resulting from these principles is significantly different from the last Bonneville Fish and Wildlife Budget Memorandum of Agreement. Bonneville and the other participants are not establishing a budget for the 2002-2006 period, and Bonneville will not be picking a single number for the rate case.

These principles will ensure that Bonneville's rates and power contracts give a very high probability of meeting all post-2001 financial obligations, including the future fish and wildlife budget commitment, and that all these obligations can be met without creating a new contract and rate "cliff" at the end of the next five-year rate period in 2006. Bonneville anticipates that after 1999 its fish and wildlife budget commitment for the post-2001 period will be set out in a budget agreement that, among other things, addresses accountability and provides that funds carried forward under the agreement will remain available for expenditure for the benefit of fish and wildlife.

Bonneville's contracts and rates historically have been set in a manner that assumes there is a low, but not zero probability that it will be unable to cover its costs. Continuing this approach, in such circumstances (e.g. low markets, low water, etc.) all of Bonneville's costs will be reviewed, recognizing that fish and wildlife obligations are one of its highest priorities. Guided by the principles below, Bonneville's goal is to reduce the chances of its being unable to cover its costs to an acceptably low level. Bonneville commits to use these principles and financial mechanisms to achieve this goal. These principles have been reviewed by the Office of Management and Budget and are consistent with the administration's principles and priorities.

PRINCIPLES

Bonneville will proceed with its power rate case and contracts for its subscription products for the period 2002-2006 using the following principles:

1. Bonneville will meet all of its fish and wildlife obligations once they have been established, including its trust and treaty responsibilities.
2. Bonneville will take into account the full range of potential fish and wildlife costs.
 - Bonneville will use the full range of potential fish and wildlife costs and financial impacts during the 2002-2006 rate period (currently estimated at \$438 million to \$721 million) for planning purposes. This

range is based upon the current calculation of the five-year average financial impact on Bonneville of 13 long-term alternatives being evaluated in the Region for configuration of the Federal Columbia River Power System and an estimated range of costs for implementing the Northwest Power Planning Council's Fish and Wildlife Program to protect, mitigate, and enhance fish and wildlife on the Columbia River and its tributaries.

- In setting its rates Bonneville will incorporate the range of \$438 million to \$721 million in its revenue requirement using a method that calculates probabilities across a range of costs in the same manner as Bonneville treats other cost and revenue uncertainties in its rate setting. Because of the uncertainties of the decisions on fish and wildlife at this time, Bonneville will conduct an analysis that assumes that all 13 system configuration alternatives are equally likely to occur. For the direct program, Bonneville will assume that costs have an equal probability of falling anywhere within the current range of \$100 million - \$179 million.
3. Bonneville will demonstrate a high probability of Treasury payment in full and on time over the 5-year rate period.
 - A 100 percent probability of Treasury payment is not achievable, but BPA's new rates must be designed to maintain or improve Treasury payment probability, even in view of the range of fish costs.
 - Bonneville will demonstrate a probability of Treasury payment in full and on time over the 5-year rate period at least equal to the 80 percent level established in the last rate case and will seek to achieve an 88 percent level.
 4. Given the range of potential fish and wildlife costs, Bonneville will design rates and contracts which will position Bonneville to achieve similarly high Treasury payment probability for the post-2006 period by building financial reserve levels and through other mechanisms.
 5. Bonneville will minimize rate impacts on Pacific Northwest power and transmission customers.
 - Bonneville's goal is to avoid a wholesale rate increase for requirements customers (including small farm and residential customers of investor owned utilities) by seeking an additional cost reduction of \$130 million in internally manageable costs that are not fish and wildlife costs.
 6. Bonneville will adopt rates and contract strategies that are easy to implement and administer.
 7. Bonneville will adopt an approach that is flexible in order to respond to a variety of different fish and wildlife cost scenarios.
 - To create financial flexibility and to avoid another contract "cliff" in 2006, Bonneville's goal will be to have 35 percent to 45 percent of its total post-2001 power sales, including secondary sales, in contract terms of three years or less, in short-term surplus sales and/or in cost-based indexed sales.
 - All sales to requirements customers will be renewable at cost-based rates which will reflect changes in Bonneville's costs subsequent to those reflected in the initial subscription rate.

8. Bonneville will use a combination of the following mechanisms to achieve principles 1-7. The specific mix and design of these mechanisms will be determined in the rate case and subscription process, but the mix chosen will meet the above principles:
- Implementing prudent additional cost-reduction efforts to reduce internally manageable costs before exercising any contingent stranded cost recovery mechanism
 - Use of Bonneville's existing authorities if needed to implement stranded costs recovery on the transmission system, while simultaneously seeking more robust authorities legislatively.
 - Selling subscription products on staggered contract terms - some shorter than five years (see Principle 6) and some for longer than five years.
 - A cost recovery adjustment clause (CRAC) in power contracts for subscription customers.
 - An option fee from some customers in return for increased price predictability after the initial contract period.
 - Cost-based indexed pricing for some of its products.
 - Using reserve balances carried into the 2002-2006 rate period from the prior period.

ADMINISTRATION COMMITMENTS

- The Administration will extend the availability of section 4(h)(10)(C) credits for Bonneville's costs related to its fish and wildlife programs for the period 2002-2006 on the same terms as established for the 1995-2001 period.
- The Administration will confirm continued access through 2006 to any funds remaining in the Fish Cost Contingency Fund on September 30, 2001, on the same terms as those established for the period 1995-2001.
- The Administration commits to support Bonneville in its Cost Review and revenue enhancement objectives.