TABLE OF CONTENTS

REBUTTAL TESTIMONY of

ANNAMARIE E. WEEKLEY, DANIEL H. FISHER, and EMILY G. TRAETOW

Witnesses for Bonneville Power Administration

SUBJECT: TIER 2 RATES AND REMARKETING VALUE **Page**

Section 1: Introduction and Purpose of Testimony 1

Section 2: Tier 2 Rates and Remarketing Value 1

Section 2.1 Purpose of the Remarketing Value 1

Section 2.2 Using Market Forecasts to Determine the Remarketing Value 3

Section 2.3 Tier 2 Overhead Adder 9

Section 2.4 Serving Tier 2 with the Federal System 10

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REBUTTAL TESTIMONY of

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SUBJECT: TIER 2 RATES AND REMARKETING VALUE

Section 1: Introduction and Purpose of Testimony

Q. Please state your names and qualifications.

A. My name is Annamarie E. Weekley, and my qualifications are contained in BP-18-Q-BPA-41.

A. My name is Daniel H. Fisher, and my qualifications are contained in BP-18-Q-BPA-08.

A. My name is Emily G. Traetow, and my qualifications are contained in BP-18-Q-BPA-39.

Q. What is the purpose of your testimony?

A. The purpose of our testimony is to respond to the direct testimony of Pacific Northwest Generating Cooperative (PNGC) and Northwest Requirements Utilities (NRU) on the calculation of Tier 2 rates and the Remarketing Value.

Section 2: Tier 2 Rates and Remarketing Value

Section 2.1 Purpose of the Remarketing Value

Q. What is the Remarketing Value?

A. The Remarketing Value is a mills-per-kilowatthour rate calculated in the rate case and published in the General Rate Schedule Provisions (GRSPs). The Remarketing Value is used for three situations. First, BPA uses the Remarketing Value to determine credits for customers with power purchases at Tier 2 rates and/or non-Federal resources that are being remarketed by BPA in accordance with section 10 of the Contract High Water Mark (CHWM) Contracts. Because Tier 2 service and some non-Federal resources must be committed to before determining a customer's Above-Rate Period High Water Mark

(RHWM) Load, section 10 of the CHWM Contracts allows BPA to remarket any excess amounts. Second, BPA uses the Remarketing Value to calculate the forecast cost of acquiring power for Tier 2 loads in circumstances when BPA has not already secured the power. Third, BPA uses the Remarketing Value to price Tier 2 power sourced from the Federal Columbia River Power System (FCRPS).

In the Initial Proposal, the Remarketing Value for a fiscal year is proposed to be based on either (1) the rate case market price forecast using critical water, called the "augmentation price," or (2) the weighted average price of BPA's acquisitions to support Tier 2 power sales made in FY 2017, but no later than May 31, 2017. 2018 Power Rate Schedules and General Rate Schedule Provisions, BP-18-E-BPA-10, § III.A.24.

Q. You mentioned above that the Remarketing Value is used to price BPA's acquisition costs of supplying power for Tier 2 loads when BPA has not already secured the power purchase. Please explain.

A. The methodology for determining Tier 2 rates includes the cost of power used to serve load at Tier 2 rates. If BPA's obligation to serve load at Tier 2 rates is greater than the amount of power it has already purchased for the Tier 2 Cost Pools, then BPA must acquire additional power (from the FCRPS or another source) to meet its Tier 2 obligations. If BPA has not yet acquired all such power prior to publishing final rates, then BPA uses the Remarketing Value to price the power not yet acquired to serve Tier 2 loads when calculating Tier 2 rates.

Q. Is this occurring in the BP-18 rate case?

A. No. We expect to source the remaining Tier 2 obligation with Firm Surplus from the FCRPS in FY 2018 and largely with a market purchase in FY 2019. Power Rates Study, BP-18-E-BPA-01, § 3.2.2.1; Weekley *et al*., BP-18-E-BPA-23, at 5. Since publication of the Initial Proposal, BPA made a market purchase for Tier 2 service for FY 2019, and we

still expect to use Firm Surplus power from the FCRPS to serve the Tier 2 obligation in FY 2018.

Section 2.2 Using Market Forecasts to Determine the Remarketing Value

Q. You mentioned above that the Remarketing Value for a fiscal year is proposed to be based on either the augmentation price or the weighted average price of BPA's acquisitions to support Tier 2 power sales. Is the augmentation price a market price forecast?

A. Yes. BPA uses two market price forecasts when setting rates. One forecast is calculated using hydro generation from the critical water year (1937), while the other forecast is calculated using hydro generation from all 80 water years. Both market price forecasts are considered spot price forecasts and are calculated using AURORAxmp®. Power Market Price Study and Documentation, BP-18-E-BPA-04, at 32. The critical water year forecast is the basis for the augmentation price, while the 80-water-year forecast is the basis for BPA's Resource Shaping and Load Shaping rates.

Q. Has BPA used the augmentation price to determine the Remarketing Value in prior BPA rate cases?

A. Yes. BPA used the augmentation price to calculate the Remarketing Value in each BPA power rate case since BPA first set rates under the Tiered Rate Methodology (TRM), which began with the BP-12 rate case. Chalier *et al*., BP-12-E-BPA-19, at 5; Chalier *et al*., BP-14-E-BPA-17, at 9; Stiffler *et al*., BP-16-E-BPA-17, at 4; Power Rates Study, BP-16-FS-BPA-01, at 68, 71–72. When setting rates, BPA values (1) prospective power acquisitions to serve BPA obligations at the augmentation price, (2) prospective surplus power sales at the market price forecast using 80 water years, and (3) power purchases or power sales secured before setting rates at the associated transaction value.

Q. Why does Staff use the augmentation price to calculate the Remarketing Value?

A. We use the augmentation price because we believe it is a reasonable approximation of the price for the power being remarketed, and for the cost of acquiring power for Tier 2 loads in circumstances when BPA has not already secured the power. BPA's augmentation price is above the average spot market price forecast because it assumes critical water conditions instead of average water conditions. This higher market price, in our view, is an approximation of the market premium charged to lock in the cost of power well in advance of delivery. This premium covers risk to BPA and helps ensure that Tier 2 rates are not subsidized by Tier 1 rates, and also provides a forward price premium to customers remarketing their excess resources well in advance of delivery. Power Rates Study, BP-18-E-BPA-01, § 3.2.2.4; Weekley *et al*., BP-18-E-BPA-23, at 5–6.

Q. Do PNGC and NRU agree with Staff's proposal to continue to calculate the Remarketing Value using the augmentation price?

A. No. Both PNGC and NRU disagree with our proposal. PNGC argues that the augmentation price should not be used to calculate the Remarketing Value because it is higher than other market forecasts. PNGC states that "[i]t is inappropriate because the forecast augmentation price represents a materially higher price as compared to other comparable market prices from a publicly available index from the Intercontinental Exchange (ICE), and BPA's own [f]lat [b]lock Resource Shaping Charge (RSC) price." Mendonca, BP-18-E-PN-01, at 3. PNGC argues BPA is overcharging Tier 2 customers to cover the single perceived risk of a cost shift between the Tier 1 cost pool and Tier 2. *Id.* at 5.

NRU argues that using the augmentation price to determine the Remarketing Value is inconsistent with the TRM. NRU states "[i]t is inconsistent with the TRM if the remarketing credit is subsidized via the costs allocated to the Short-Term Tier 2 cost pool because the pricing structure uses augmentation pricing, which, by definition, occurs very

rarely, instead of market pricing, which the TRM explicitly says should be used to price the Short-Term Tier 2 rate." Stratman & Weathers, BP-18-E-NR-01, at 16.

Q. Do you agree with PNGC's and NRU's arguments?

A. No. Their arguments ignore both BPA's long-term consistent use of the augmentation price, and the fact that continuously available firm power from the Federal system—guaranteed well in advance of delivery—provides assurance against risk as required by section 6.3 the TRM. Tiered Rate Methodology, BP-12-A-03, at 81. These assurances are not otherwise provided by most market-based products, particularly spot market-based products. As such, critical water planning, and thereby the augmentation price, is the consistently used and correct metric to assess the cost of power that BPA has not purchased but must guarantee to be available on a continuous basis under all conditions.

Q. Do you agree that the TRM requires that only market pricing should be used to price the Short-Term Tier 2 rate?

A. No. Section 3.7 of the TRM allows BPA to use the Tier 1 System to serve load at the Tier 2 rate when it is forecast to be available and priced accordingly. Tiered Rate Methodology, BP-12-A-03, § 2.2.4. TRM section 3.7 states:

> BPA will acquire the resources necessary to serve customers' Above-RHWM Load that the customers elect to place on BPA and will recover the costs through Tier 2 Rates. BPA may use energy from the Tier 1 System for service to loads at Tier 2 Rates to the extent any such energy is forecasted by BPA for ratemaking purposes to be available for the Rate Period as a result of unused RHWM amounts. BPA will allocate the forecast marginal cost of such energy to the appropriate Tier 2 Cost Pool . . . .

Id. at § 3.7. Thus, the TRM does not require BPA to use a flat block market purchase or flat block market price when pricing available Tier 1 System power for Tier 2 energy needs. Rather, the TRM directs that such energy be priced at the "forecast marginal cost of such energy." *Id.* In setting the forecast marginal cost, we believe it is appropriate to

consider the type of product being provided. In this instance, the Tier 1 System for service to Tier 2 loads reflects a firm power supply, based on a critical water planning forecast, which includes all risks reflected in such planning for the use of such energy. As noted previously, we believe securing a market purchase, in advance, includes a market premium. Thus, BPA's use of the augmentation price, which approximates the market premium *and is also* a forecast market price, is an appropriate forecast of the marginal cost to serve Tier 2 loads.

Q. What methods do PNGC and NRU propose for calculating the Remarketing Value?

A. Both parties propose that BPA use its average market price forecast that uses 80 water years instead of BPA's critical water market price forecast (*i.e.*, augmentation price) to determine the Remarketing Value. Mendonca, BP-18-E-PN-01, at 9; Stratman & Weathers, BP-18-E-NR-01, at 15. PNGC further proposes that the Remarketing Value should be reduced by the Tier 2 Overhead Adder. Mendonca, BP-18-E-PN-01, at 9.

Q. Why do PNGC and NRU believe using the average market price forecast rather than the augmentation price is more appropriate for calculating the Remarketing Value?

A. PNGC believes its proposal is more appropriate because it prevents Short-Term Tier 2 customers from paying higher prices and "do[es] not pose any cost shift[s] or revenue risk to BPA[.]" *Id*. at 6. Furthermore, PNGC argues that BPA is using inconsistent assumptions by forecasting a market price for Tier 2 customers using critical hydro while pricing Firm Surplus using the average market price forecast based on 80 water years. *Id*. at 6–7.

NRU contends the TRM is clear that all costs associated with one cost pool must be kept separate and distinct from others. NRU also argues the TRM is clear that the Short-Term Tier 2 rate should be sourced with flat block market purchases, and to the extent such purchases are not yet made, the rate may be comprised of both "known and projected costs of the energy from market purchases." Stratman & Weathers,

BP-18-E-NR-01, at 14–15 (*quoting* Tiered Rate Methodology, BP-12-A-03, § 6.3.1, at 81). In NRU's view, the TRM directs that the cost of reallocated power will be "forecast to occur at the market price of power." Stratman & Weathers, BP-18-E-NR-01, at 15 (*quoting* Tiered Rate Methodology, BP-12-A-03, § 3.4, at 27).

Q. Do you agree?

A. No. We believe the average market price forecast using 80 water years would not accurately reflect the price of these purchases and would be inconsistent with the TRM. Specifically, the TRM states if BPA has not already acquired power to supply Tier 2 energy sales, then BPA must estimate its cost of the prospective acquisition by using a forecast market price. In developing that market price, the TRM permits BPA to include a risk component. Tiered Rate Methodology, BP-12-A-03, § 6.3.1. TRM section 6.3.1 states:

> [. . .] BPA may not have actually made all the market purchases needed to serve the loads at this [Tier 2] rate. Consequently, this type of rate may be comprised of both known and projected costs of the energy from market purchases, a risk component to cover the expected risks of providing service at a set forward price (which could take the form of some combination of planned net revenues for risk and rate adjustments or true-ups), and an Overhead Cost Adder.

Id. at 81.

Furthermore, because BPA's average market price forecast using 80 water years is a spot forecast and does not include a risk component, there is a 50 percent probability that there *will* be a cost shift or revenue risk to Tier 1 ratepayers if BPA adopted PNGC's and NRU's proposal. Finally, using a critical water assumption to price prospective power purchases for Tier 2 reduces the possibility of cost shifts due to risk exposure to supply and price.

Q. Do PNGC's or NRU's proposals to use the average market price forecast using 80 water years to determine the Remarketing Value include any type of risk considerations or risk mitigation tools?

A. No. PNGC believes the average market price forecast "in the applicable period will have any premium already built into the quote." Mendonca, BP-18-E-PN-01, at 5. NRU agrees that "[t]here may be some uncertainty in the price BPA will ultimately pay for a market purchase[.]" Stratman & Weathers, BP-18-E-NR-01, at 17. NRU goes on to state that BPA should use the market price using all 80 water years, instead of critical water, to determine the Remarketing Value since it "maintains consistency with how BPA prices fifteen different components within its power rates study, including firm surplus power sales and the load shaping rate. BPA staff themselves say that the load shaping rate is 'an unbiased estimate of the market value of the power.'" *Id.* at 17 (footnotes omitted).

Q. Do you agree?

A. No. The average market price forecast using 80 water years is a spot market price forecast and does not include any premium for locking in a price ahead of service. The market price forecast is an unbiased estimate of the market value of power during the upcoming rate period. It is not, however, an estimate of the market value of power when locking in a price ahead of service and, therefore, an additional risk component is necessary. NRU correctly states that the market price forecast using all 80 water years is used in many aspects of Tier 1 rate design; however, unlike Tier 2 rates, Tier 1 rates are also subject to a number of risk mitigation tools, including rate adjustments and financial reserves. Power and Transmission Risk Study, BP-18-E-BPA-05, § 4.2.1.

Section 2.3 Tier 2 Overhead Adder

Q. Does PNGC make any other arguments regarding the calculation of the Remarketing Value?

A. Yes. PNGC also states that BPA should reduce the Remarketing Value by the Tier 2 Overhead Adder. Mendonca, BP-18-E-PN-01, at 9.

Q. Do you agree with the proposal to reduce the Remarketing Value by the Tier 2 Overhead Adder to determine remarketed energy proceeds?

A. No. Section 6.4.1 of the TRM states:

> The total proceeds of the remarketed energy will be reduced for aggregated transaction costs, including such costs as broker fees or other marketing fees, transmission costs, transmission losses, and odd lot remarketing costs.

Tiered Rate Methodology, BP-12-A-03, at 83. PNGC suggests that BPA should reduce the Remarketing Value by the Tier 2 Overhead Adder in place of reducing the total proceeds of the remarketed energy by aggregated transaction costs. Mendonca, BP-18-E-PN-01, at 8–9. The Tier 2 Overhead Adder is calculated in accordance with section 6.3.3 of the TRM and is set at a level that will reasonably compensate the Composite Cost Pool for the costs of providing power at Tier 2 rates. We have not revisited the concept of applying a transaction cost (including broker fees, marketing fees, transmission costs, transmission losses, and odd lot remarketing costs) adjustment to remarketing energy proceeds since the BP-14 rate case, when BPA determined the cost was *de minimis* given the small amount of remarketing BPA was doing among existing cost pools. Tier 2 and RSS Testimony, BP-14-E-BPA-17, at 13. As such, we do not believe that PNGC's argument to reduce the proceeds for remarketed energy by transaction costs should be considered at this time because this is a substantial change to the methodology for calculating the credit customers receive from BPA for remarketing Tier 2 and

non-Federal energy. We think the better approach is to discuss possible methodologies for remarketing transaction costs in BP-20 workshops prior to the BP-20 Initial Proposal.

Q. Do you agree with the proposal to reduce the Remarketing Value by transaction costs?

A. No. Although we are open to revisiting, in BP-20 workshops, the BP-14 decision to not apply a transaction cost to proceeds for remarketed energy, we do not support reducing the Remarketing Value by transaction costs. The Remarketing Value has multiple purposes and was designed to be the common starting point before any adjustments were applied for those multiple purposes. One such adjustment would be the upward Tier 2 Overhead Adder BPA uses to calculate Tier 2 rates. Another potential adjustment, as described above, would be a downward adjustment for calculating any net remarketing proceeds. Therefore, we cannot support PNGC's proposal to reduce the Remarketing Value itself by the Tier 2 Overhead Adder. Further, because the Remarketing Value is also used to calculate the cost of BPA's prospective acquisitions to supply Tier 2 energy, reducing the Remarketing Value by the amount of a transaction fee would effectively reduce Tier 2 rates, thus causing a potential cost shift from Tier 2 to Tier 1.

Section 2.4 Serving Tier 2 with the Federal System

Q. Does NRU make any other arguments regarding the calculation of the Remarketing Value?

A. Yes. NRU argues that it is not appropriate to use the augmentation price to calculate the Remarketing Value because the "TRM only provides for inclusion of a risk premium in a Tier 2 cost pool if the power has yet to be purchased," and that "the power that is being remarketed (and used to source the Short-Term Tier 2 rate) has already been acquired." Stratman & Weathers, BP-18-E-NR-01, at 16.

Q. Please respond.

A. NRU is correct that if BPA has already acquired the power needed to supply Tier 2 service, no risk premium would be necessary in the market price forecast because the actual cost of the acquisition would be included in the Tier 2 rates. As stated earlier, when setting rates BPA values (1) prospective power acquisitions to serve BPA obligations at the augmentation price, (2) prospective surplus power sales at the market price forecast using 80 water years, and (3) power purchases or power sales secured before setting rates at the associated transaction value. When BPA values prospective acquisitions using the augmentation price, it is accounting for two types of risk: price and supply. However, valuing power that has already been sourced, but does not have an associated purchase price, does not fit into the three previously mentioned methods used to set a value for power.

Q. Given NRU's argument, would it be reasonable to revise the method used for calculating the Remarketing Value that would be applied to Federal power serving Tier 2 loads?

A. Yes, in part. Currently, the definition of Remarketing Value sets the value at the augmentation price when the prospective acquisition is not yet purchased, or at the purchase price after the power is acquired. The definition of Remarketing Value could include a third possibility considering when the supply is present on the Federal system and a market purchase will not be made. This third possibility could be valued at the average of the two market price forecasts. Since the market price forecast using 80 water years does not include a risk premium, and for purposes of ratemaking the augmentation price includes a risk premium for supply and price risk, it would be reasonable to average the two price forecasts to approximate a price that includes a risk premium for locking down a price prior to delivery but does not include a risk premium for supply risk.

Q. How could the Remarketing Value definition be revised to accommodate NRU's argument?

A. The definition of Remarketing Value could be revised to the following:

> Remarketing Value is the value BPA provides to customers for remarketed energy (both Tier 2 and non-Federal). This value is also used to calculate the cost of unpurchased amounts of Tier 2 energy. The Remarketing Value for a fiscal year is based on~~either~~: (1) the rate case market price using the critical water "augmentation price" *when BPA has not yet acquired the power to supply Tier 2 service*; ~~or~~ (2) the weighted average price of the ~~actual Tier 2~~ power purchases ~~made in FY 2017, no later than May 31, 2017, made in FY 2017~~ *BPA has acquired (between October 1, 2016 and June 1, 2017~~for that same fiscal year~~) for the corresponding year to supply Tier 2 service; or (3) the average of the rate case market price using all 80 water years and the rate case market price using the critical water "augmentation price" when BPA is using Firm Surplus from the FCRPS for Tier 2 service and BPA does not make any actual power acquisitions (between October 1, 2016 and June 1, 2017) for the corresponding year to supply Tier 2 service.*

Q. Would this approach be consistent with the TRM?

A. Yes. This approach would include a risk component to cover the expected risk of providing service at a set forward price in accordance with section 6.3.1 of the TRM. In addition, BPA would be using forecast market prices for calculating the remarketing proceeds in accordance with section 6.4.1 of the TRM.

Q. Would this approach create cost shifts between Tier 1 and Tier 2?

A. No. Section 3.7 of the TRM states that if BPA is using the Tier 1 System for service to loads at Tier 2 rates, BPA will allocate the forecast marginal cost of such energy to the appropriate Tier 2 Cost Pool and credit the same marginal cost to the appropriate Tier 1 Cost Pools. Tiered Rate Methodology, BP-12-A-03, at 29. In its rate cases, BPA values power not yet sold (including Firm Surplus) at the market price forecast using 80 water years. Therefore, if BPA used Firm Surplus for Tier 2 service and valued such power at the average of the market price forecast using 80 water years and the augmentation price, Tier 1 would see the benefit of valuing a portion of Firm Surplus at something higher

than the market price forecast using all 80 water years. Furthermore, the Tier 2 rate would include a Risk Adder to cover the expected risks of providing service at a set forward price to avoid shifting costs to Tier 1. BPA would accommodate this change by revising the Firm Surplus Secondary Sales line in Table 2.3.8 of the Power Rate Study Documentation, BP-18-E-BPA-01A, at 54, to two lines: one for "Firm Surplus Secondary Sales Sold" for forecast revenue from power designated to serve loads at the Tier 2 rate, and one for "Firm Surplus Secondary Sales Unsold," for revenue from the remaining amount of firm surplus power that BPA is forecasting will be sold during the rate period.

In addition, this approach would avoid a cost shift between the Tier 2 Cost Pools because it would continue to use the Remarketing Value both for determining proceeds for remarketing energy and for determining the cost of prospective acquisitions to supply Tier 2 energy. It is possible that any customer purchasing Tier 2 energy may receive remarketing proceeds as a result of how its load changes over time in relation to its RHWM. Thus, we believe this approach is reasonable because it would properly balance how the Remarketing Value can result in credits to Tier 2 customers.

Q. Does this conclude your testimony?

A. Yes.