Testimony
Of
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Subcommittee on Water and Power
House Committee on Resources

Hearing on

"How the Federal Power Marketing Administrations are Implementing the Energy Policy Act of 2005, and an Assessment of the Proposed Fiscal Year 2007 Budgets for These Agencies"

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Introduction

Mr. Chairman, members of the subcommittee, thank you for this opportunity to testify at today's hearing. I am James H. Pope, General Manager of the Northern California Power Agency (NCPA), a joint action agency that serves as the supplemental power supplier for 15 public power systems that purchase power from the Western Area Power Administration (Western). For our members – municipal utilities, irrigation and special purpose districts, the Bay Area Rapid Transit System, and a rural electric cooperative – the power they receive from Western is an integral part of their power supply, and an essential component in providing their communities and consumers with reliable and affordable electricity. Given the importance of Western to our communities and districts, we commend the subcommittee for providing this important oversight hearing.

Overview

- Western's third-party transmission activities require close oversight.
- Bureau of Reclamation's (Reclamation's) dam security costs must be reviewed, controlled and properly allocated.
- The Office of Management and Budget's (OMB's) "agency rate" proposal appears to have a nominal rate impact on CVP customers – but sets an unsound policy precedent.
- No costs for the Folsom Dam replacement bridge should be assigned to power and water customers.
- The Administration's request for Western's "purchased power and wheeling" account should be supported.
- OMB's initiative to limit third-party financing of Bonneville Power Administration (BPA) transmission should be rejected. BPA and Western should be encouraged to further enhance transmission capability between the Pacific Northwest and the Pacific Southwest.
- The Department Interior's review of Central Valley Project Improvement Act (CVPIA) activities should continue.
- The Central Valley Project should switch to Forecast Based Operation.

Background on the Western Area Power Administration and the Central Valley Project Customers

The federal Central Valley Project (CVP) consists of 11 power plants at federal multipurpose projects with a combined generating capacity of almost 2,000 MW. Western also owns almost 900 miles of high-voltage transmission lines that deliver power from the federal dams to Western's customers. The costs of the CVP system are repaid – in full and with interest – by the power customers. In addition, the power customers pay for significant fish and wildlife measures, and assist in repayment of the irrigation investment. CVP power, on average, meets more than 30% of NCPA member communities' and districts' energy needs.

But this is not a static partnership. Rather, it is one that has grown and evolved:

- CVP customers provided advanced funding for rewinding the generators and replacing the turbine runners at Shasta Dam, a collaborative effort that extended the life of these units, resulted in an efficiency gain of 2%, and produces an additional 98 megawatts of electricity;

- CVP customers, acting through the Transmission Agency of Northern California (TANC), partnered with Western to construct the California-Oregon Transmission Project, the third major link between California and the Pacific Northwest;

- TANC – comprised of public power systems – played a prominent role in promoting completion of the Path 15 transmission project that relieved congestion and improved the reliability of the California grid;

- CVP customers provide direct customer financing for important CVP capital and operational expenditures to ensure that, in light of constrained federal appropriations, the facilities continue to operate reliably, efficiently and cost-effectively, and;

- CVP customers worked collectively to create the Sacramento Municipal Utility District/Western Area Power Administration Control Area to ensure that Western's transmission facilities operate efficiently and in compliance with the statutory purposes and obligations of the Central Valley Project.

There is an effective partnership between Western and its customers – and the Subcommittee on Water and Power has played an important role in fostering that partnership which has produced many public benefits.

Western Area Power Administration-Related Provisions of the Energy Policy Act

One of the key Western-related features of the Energy Policy Act of 2005 is the provision authorizing Western to accept third-party funds to construct transmission facilities. As noted above, NCPA supports, and has participated in, cooperative arrangements with Western to facilitate transmission construction. Partnering with Western provides a number of advantages, including the ability to integrate with Western's backbone facilities, use of federal eminent domain authority, and Western's proven track-record of project design and construction.

As we noted during congressional debate of this provision, however, it is important that use of this new authority be used judiciously and appropriately. It is important that this provision neither distract Western from its core mission of operating the federal facilities, nor result in the direct or indirect transfer of costs from third-party transmission projects to federal power customers.

The Subcommittee on Water and Power should provide careful and consistent oversight of Western's activities under this provision.

Dam Security Costs Must be Reviewed, Controlled and Properly Allocated

Reclamation has incurred significant expenses in its post-September 11 security program. Historical precedent argues that these security costs should be fully non-reimbursable (not subject to repayment by CVP customers). Further, the facilities are on the national critical infrastructure list and, therefore, a small number of citizens should not be responsible for paying for security costs that benefit the entire nation. However, Reclamation's May 1, 2005 report to Congress assigned CVP power customers the obligation to pay for roughly two-thirds of the CVP security costs – an amount that is not commensurate with the underlying multipurpose project cost allocation based on the multiple public purposes of these projects.

Congress stipulated in the FY 2006 Energy and Water Development Appropriations Act that only $10 million of the Reclamation's security costs could be recovered from water and power customers of the CVP. Reclamation has also been told by the

Congress that it needs to better allocate costs to align with the purpose of the funding, and provide improved cost accountability and transparency.

NCPA is supportive of an appropriate assignment of CVP security costs to power customers, provided that the costs are quantifiable and reflect a proper allocation, and that customers are provided appropriate cost review and input. In fact, there have been positive developments in this regard as Reclamation now appears ready to adjust cost allocations so that CVP power customers are assigned a percentage of costs that match the underlying multipurpose cost allocation.

Yet, there are two remaining areas of concern that warrant congressional review:

- The President's 2007 budget removes the $10 million cost cap on reimbursable security measures.

- Reclamation seeks to require customers to provide up-front funding for the power share of these costs. While this mechanism could provide needed customer involvement and oversight, this funding tool is being called upon in this instance without any customer consultation, nor analysis to determine if the advanced customer funds could be properly credited on their bills. Moreover, the customer funding contracts only allow for funding of direct power operations and maintenance costs – and not multipurpose activities.

NCPA is willing to create a true cost-sharing partnership for Reclamation's post-September 11 security costs. In order to succeed, this partnership must provide customers with assurance that costs will be legitimate, known and limited. We greatly appreciate the efforts of Chairman Pombo and Chairman Radanovich to promote a fair and transparent process, and look forward to continuing to work with this Subcommittee to advance these objectives.

OMB Interest Rate Adjustment Sets Troubling Precedent

The FY 2007 budget stipulates that the Department of Energy will alter its policy governing interest rates for investments by the federal power marketing administrations (PMAs), including Western. This change will affect only those facilities, such as the CVP, where the interest rate is not set by law. Under the proposal, new investments will incur an interest charge similar to the rate at which federal corporations borrow funds from the Treasury. The budget claims that this "agency rate" was .4% higher on average than PMA rates from 1997-2005.

OMB claims this change will have a minimal rate impact – and NCPA is still evaluating the rate consequences. However, we are troubled by the precedent of making significant changes in policy without adequate consultation with and review by Congress. As this Subcommittee knows, over the years OMB – under both Democratic and Republican Administrations – has attempted to make discriminatory and punitive changes to the rate policies of the federal power marketing agencies. Enabling major shifts in repayment policies through a simple change in an obscure Department of Energy budget directive could result in significant rate increases for consumers, jeopardize the operations and viability of these important multipurpose projects, and undermine the essential role of Congress in setting and overseeing the policies affecting the nation's water and power resources.

Given the history of numerous assaults on PMA rate setting policies, we believe such changes should only be made with the express consent of Congress. Ideally, we would hope Congress would reject this incursion in the repayment policies of the PMAs. ***At a minimum, the Subcommittee on Water and Power should take necessary steps to convey its dissatisfaction with this presumptive action, and to prevent OMB from making further changes in PMA ratemaking and repayment policies without the direct approval of Congress.***

Folsom Dam Bridge Replacement

NPCA supports efforts to build a new bridge downstream of Folsom Dam to address traffic congestion created by the closure of the Folsom Dam road for security purposes. However, because the bridge project will not provide any benefit to power and water customers, the costs of the bridge should therefore not be assigned to these customers for repayment. Assigning costs to project purposes where there is not a direct and corresponding benefit sets an unsound policy precedent that could undermine cooperation between stakeholder groups, and jeopardize other project investments.

The Subcommittee on Water and Power should carefully monitor this process to ensure that the federal government's share of the new bridge remains a non-reimbursable expense.

Purchased Power and Wheeling

Each year, Western and the other PMAs receive a federal appropriation to cover the costs of purchasing power to "firm" power sales and arrange for transmission. In the case of the CVP, Western's purchased power and wheeling (PPW) expenses have dropped significantly as a result of the post-2004 marketing plan – but the activity remains critical for Western to meet its obligations to some of its smaller California customers, including BART and the Lassen Municipal Utility District. These PPW appropriations are repaid to the Treasury within the same fiscal year from revenues collected from PMA customers. In recognition of this fact, Congress adjusted the budget rules so that these appropriations do not "score" as part of the federal budget. Nonetheless, there are often annual debates over the level of the PPW account.

This year appears to be an exception to the rule, as the FY 2007 budget includes the appropriations needed to fully fund for Western's Purchased Power and Wheeling activities for the coming year.

NCPA is pleased that the FY 2007 budget includes an adequate appropriation for Western's PPW activities and urges Congress to support this amount.

Third-Party Financing of BPA Transmission Facilities

As the members of this Subcommittee know, California and the Pacific Northwest are joined at the hip – we are physically integrated, make considerable sales between the regions to take advantage of seasonal diversity, and support each other to advance system reliability.

Consequently, investments in the Northwest transmission grid are important for all of California as well. It is with this in mind that I raise with the Subcommittee NCPA's concern regarding with the persistent effort of OMB to limit the ability of BPA to finance and construct needed transmission.

Unlike Western, BPA has direct borrowing authority from the U.S. Treasury to finance transmission additions and upgrades. Recently, Congress increased that borrowing authority, but directed BPA to seek partnerships with non-federal parties in order to leverage the limited borrowing authority and include others in the planning and financing of its facilities. As we have noted, these partnerships have great potential to meet the infrastructure demands of the West – and it is for such purposes that Congress authorized Western to enter into these types of arrangements.

It is, therefore, highly ironic that after directing BPA to pursue third-party financing, and granting Western authority to enter into arrangements with third-parties, that OMB has proposed to undercut this important tool. In July of last year, OMB sent legislation to Congress, which it reasserts in the FY 2007 budget, that would count third-party financings against BPA's limited borrowing authority – effectively denying any value in pursuing these arrangements, and leaving BPA in a precarious position with only sufficient borrowing authority to meet its infrastructure needs through 2011.

The Subcommittee on Water and Power should take appropriate action to affirmatively reject this treatment of third-party financing of BPA transmission, and encourage BPA and Western to participate in further enhancements to transmission capability between the Pacific Northwest and California.

Review of CVPIA Activities

The Department of Interior's review of certain activities under the Central Valley Project Improvement Act (CVPIA) is receiving considerable attention. Let me take this opportunity to clarify certain facts:

- CVPIA established a Restoration Fund to be used along with federal and state appropriations to accomplish 33 specific objectives. CVP water and power customers were statutorily obligated to contribute $30 million annually (adjusted for inflation) to the Restoration Fund.

- Neither the federal nor state financed share of the Restoration Fund has fully materialized, but to date, CVP water and power contractors have contributed over $500 million toward the accomplishment of the objectives.

- The CVPIA calls for cutting contributions to the Restoration Fund in half once the objectives are completed, and Congress expressly anticipated that such action would occur within 10 years of enactment.

- It has now been 13 years, and no meaningful review of programmatic accomplishments has been conducted, and no metric exists to measure program accomplishments.

- NCPA joined with CVP water customers in preparing our own assessment of the CVPIA accomplishments, and determined that our obligations regarding the 33 objectives have been met.

- The Department of Interior received our analysis and, while it did not choose to exercise its statutory discretion to reduce Restoration Fund contributions, it did realize that a rigorous analysis of the program's status, accomplishments, goals and objectives was necessary.

- At the direction of the Office of Management and Budget, The Department of Interior is reviewing the CVPIA Section 3406 objectives as part of the Department's Program Assessment Rating Tool (PART) process.

- The Department of Interior's process is both public and open, with broad stakeholder participation.

The Department of Interior is conducting this review with broad stakeholder participation, and we look forward to the establishment of program objectives, milestones, and measurements to allow for effective implementation of the Act.

Forecast Based Operations

The CVP system plays an important role in providing flood control protection to the Sacramento Valley and beyond. NCPA believes, however, that the CVP can meet the same or higher level of flood protection by releasing water based on accurate weather forecasts rather than through overly stringent adherence to rigid operating rules.

Today, the Bureau of Reclamation releases water through the CVP system – at the direction of the Corps of Engineers – to stay within a storage requirement known as the "flood control curve." Under this regime, water is released anytime storage exceeds a specific amount – without adequate consideration of what the forecast for additional precipitation might be in the following days. As a result, we have witnessed instances in which significant water releases are followed by dramatic flow reductions, when a more levelized release schedule would have been possible. These high, unnecessary water releases necessitate bypassing the dam's power generating facilities, resulting in a loss of generation and power revenues. Similarly, when the reservoir inflows and rain forecast make it highly likely that flood releases are imminent, then increasing flow up to the power plant, rather than bypassing the generators, would capture more energy.

Let me illustrate this situation. On February 3, the Corps of Engineers directed Reclamation to release 30,000 cfs from Shasta due to the emergence of a small storm. These high releases continued until February 8, at which time the flow rate was reduced to 16,000 cfs. Then flows were reduced to below 10,000 cfs a few days later. Since only 16,000 cfs can go through the generators, bypasses were required, and the value of the energy bypassed totaled approximately $3.5 million. Yet, the weather forecast unequivocally indicated that we would have clear weather after that small storm. Consequently, if Reclamation had maintained releases at 16,000 cfs, it would have taken a few more days to get within the flood control curve, but we would have had the same level of flood protection, and would have avoided a $3.5 million loss of resource value.

Forecasting has improved to the point where we should be capable of making sound resource and business decisions for flood control releases through Forecast Based Operations, rather than through an overly strict interpretation of the flood control curve, and we would urge the Subcommittee on Water and Power to encourage the Bureau and Corps to take the necessary steps to implement this methodology.

Conclusion

Western remains a vibrant and important player in promoting a reliable, affordable power supply in California and throughout the West. We appreciate the role of this Subcommittee in maintaining that value, and conducting this important oversight hearing.

Thank you for this opportunity to testify, and I welcome your questions.