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On Enhancing Federal Power Generation and Transmission
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Mr. Chairman and Members of the Subcommittee, I am Ted Coombes, Executive Director of Southwestern Power Resources Association (SPRA). For 48 years, our association has represented the rural electric cooperatives and municipally owned electric utilities that purchase the hydroelectric energy and capacity generated at 24 Corps of Engineers multipurpose water resource projects in our area of the country. This energy and capacity is marketed to us by Southwestern Power Administration (SWPA), an agency of the U.S. Department of Energy. Ultimately this federal energy and power reaches between 6 million and 7 million people in the states of Oklahoma, Arkansas, Missouri, Texas, Kansas and Louisiana. This is in keeping with Section 5 of the Flood Control Act of 1944, which directed SWPA to provide widespread dissemination of federal energy and power at the lowest possible costs, consistent with sound business principles. This same legislation – like numerous other statutes authorizing the production and distribution of federal power dating back to the Reclamation Act of 1902 – embraced the “preference principal.” This principal states that “preference in the sale of such [federal] energy and power shall be given to public bodies and cooperatives” – in other words, rural electric cooperatives, municipally owned electric utilities and public power agencies, authorities and districts would have the first right to purchase the energy and power generated at federal dams. We will revisit this concept a little later in my testimony.

Thank you for the opportunity to testify at this hearing on “Opportunities and Challenges on Enhancing Federal Power Generation and Transmission.” To be honest, Mr. Chairman, my first draft of this testimony differed substantially from the product I am proffering today. Originally I took the bit between my teeth and produced words that acknowledged the challenge of maintaining the reliability of the federal power system in the face of diminishing federal appropriations. Ever the optimist, however, I embraced the opportunities to address these challenges through new methods of funding the necessary operation, maintenance, replacement and rehabilitation of our federal power infrastructure, both within the power marketing administrations (PMAs) and the Corps of Engineers. I was encouraged by rumors that the Administration’s budget message would endorse use of PMA receipts to fund Corps of Engineers hydropower functions and a “net-zero” appropriations concept for funding the PMAs themselves. I was prepared to tell you how our association has championed non-traditional funding methods for these purposes, such as the Jonesboro Memorandum of Agreement that has enabled SWPA wholesale power customers to fund more than \$50.6 million in Corps hydropower operation and maintenance projects that the preference customers deem are critical to maintaining the reliability and deliverability of federal power. I was going to report to you that just last month, our Board of Directors adopted a resolution endorsing the net-zero appropriations concept for SWPA.

You see, Mr. Chairman, I didn’t want to dwell on the challenges that face the federal power program. I wanted to embrace the opportunities we have to face these challenges and resolve them. Although I’m not from Kansas, I guess I’m just a cock-eyed optimist.

At least, I was until last Friday, when we learned that the Administration’s FY 2006 budget request will include a recommendation that the PMAs, including SWPA, charge market-based rates for federal power – breaking a contract with the American people that dates to the turn of the 20th Century. That’s when I tore up my original draft and began rewriting this testimony. If we abandon the concept of cost-based rates for PMAs, there is no reason for optimism whatsoever.

Some Historical Perspective

I can unabashedly state, without fear of contradiction, that President Roosevelt was the father of the federal power system, the preference principal and cost-based rates for federal power. It might surprise you to learn that I am not speaking of Franklin Roosevelt, but Teddy Roosevelt. It was the Great Conservationist who used his “bully pulpit” to advocate the development and conservation of interstate water resources through the federal development of multipurpose water resource projects. TR believed firmly that the nation’s water resources belonged to all the nation’s people – not to any one company or individual – and that they should be developed and conserved by the federal government to serve as many people as possible. The benefits from these projects should go directly to the people wherever possible, and not be siphoned off as profits by some middle man, such as a private power company. This was the basis for both the

preference principal and cost-based rates for federal power. The preference principal relies on consumer-owned, not-for-profit utilities, wherever possible, to deliver federal power to retail consumers. This, combined with the requirement that the federal government dispose of its hydropower at the cost required to produce it (including the construction, operation and maintenance costs of the generation and transmission facilities and interest on the capital costs) insure that no one – not the federal agency generating or marketing the power or the utilities distributing this energy to retail consumers – is profiteering off the public's resources. This concept was first incorporated in the Reclamation Act of 1902, which authorized construction of the appropriately named Roosevelt Dam, which became the keystone of the Salt River Project in Arizona.

This issue was next joined when the government built a hydroelectric dam at Muscle Shoals, Alabama, to power the munitions industry supplying explosives and weapons for World War I. After the war, there was much controversy about what to do with the dam. The private power companies and investor-owned utilities wanted the federal government to sell the project to them, so that they could market the power produced by the dam at a profit. They were challenged by Senator George Norris, another Republican, from the state of Nebraska. Senator Norris reiterated the policies initially espoused by President Teddy Roosevelt – this was a federally built project that conserved and developed the water resources that belonged to the public. Thus, the preference principal and cost-based rates should apply. Senator Norris won the day, and the Muscle Shoals project went on to become the first power project of the Tennessee Valley Authority (TVA).

None of what has been said is to belittle the role of Franklin D. Roosevelt. He was the one to administratively establish SWPA and the Rural Electrification Administration before they were subsequently statutorily authorized by Congress. His advocacy of public power to provide a yardstick for competition for private power companies led to the formation of the New York Power Authority. And certainly TVA would never have been born without his leadership.

The point is that it wasn't the Democrats or Republicans who established the federal power program. Rather, it took leadership from both parties to bring this magnificent system to fruition. The continuation of SWPA and its sister PMAs is a tribute to the fact that the federal power program continues to enjoy bipartisan support, both from within our six-state region and throughout the country. From Teddy Roosevelt to George Norris to Franklin Roosevelt to Senator Warren Magnuson to Senator Mark Hatfield to Congressman Charlie Norwood, Congresswoman Jo Ann Emerson, Congressman Roy Blunt and to you, Mr. Chairman, and to the members of your Subcommittee and Committee, the continued existence and successes of the federal power program are a tribute to both Republican and Democrat leaders in the Congress and the White House.

So I am left to ponder the question, "Why would this budget ignore these revered Republican leaders from the past and present and abandon cost-based rates for PMAs? Why would it allow the government to profiteer from the sale of resources that belong to the people and were developed by the federal government to benefit these people?"

The Impacts on Electric Consumers

Until relatively recently, cost-based rates were the norm for virtually all electric utility transactions, including sales by the investor-owned, for-profit utilities. However, beginning in the 1990s, the Federal Energy Regulatory Commission (FERC) began to allow investor-owned utilities and a new class of generators known as independent power producers or power marketers to charge market-based rates for wholesale power – in other words, they could charge what the market would bear for these transactions. This authority was based on the premise that sufficient competition exists in wholesale markets and thus market-based rates would reflect "just and reasonable charges". I'm probably making the understatement of the decade, but here goes: Events over the past five years have cast doubts on this premise that there is sufficient competition in the wholesale electricity market to allow competition alone to set just and reasonable rates. Even FERC is reconsidering and establishing a market power test; utilities who fail to pass these tests may have their authority to charge market-based rates revoked.

Now the Administration wants the PMAs to join in this folly of pricing the wholesale power they sell at market-based rates. Not satisfied with recovering all of the costs of building and operating the federal power system, plus interest on the capital investment, this budget would make a profit on the nation's water resources. How much profit? Well, it depends on what the market rates are – what the market will bear. Electricity isn't like oil or gas or hog bellies. It can't be efficiently stored to supplement supplies when demand is high. Generation must instantly match demand, or the lights go out. As a result, market prices for electricity are extremely volatile. Some recent summer months have seen market prices for the same quantity of on-peak energy vary by 724% from one day to the next and by as much as 7,658% within a month. If SWPA were required to charge market rates, my members' lowest cost on-peak resource would become their highest-cost resource. The difference will come out of the pockets of your constituents.

Let me give you an example. There was some talk in the fall of 1999 of requiring PMAs to charge market rates. That summer, spot market prices had been particularly volatile in our region. I conducted a short analysis to determine what some of SWPA's wholesale customers would have paid during the month of July 1999 if SWPA had charged the spot market price

for the electricity. First, I selected a few municipal and co-op SWPA customers in each of the six states served by the PMA. I determined how much firm, on-peak energy each of these customers purchased from SWPA daily during that month (because we were measuring peak-power prices, off-peak times of nights, weekends and holidays were excluded). I determined how much each of these customers paid each day for this electricity they purchased from SWPA. Then I determined what the average spot market price was each day during this period by consulting the trade periodical Megawatt Daily. This publication reports the high, low and average prices paid in different regions of the country for both on-peak and off-peak electricity on a daily basis. I chose the average on-peak price for energy sold into the Entergy market, which generally reflects our region. With this data, I then computed for each day what these SWPA customers would have paid had they been charged the average day-ahead spot market price for the energy they purchased from SWPA.

The total increase per utility varied, of course, depending upon how much SWPA energy each utility purchased on any given day. The impact per consumer of these utilities also varied, depending upon what percentage of the utility's total load was served by the energy purchased from SWPA. Nonetheless, the results were astounding. Take, for example, the Town of Skiatook, Oklahoma. This is a very small community in northeastern Oklahoma, and most of its electric load is met by purchases from SWPA. During the month of July 1999, Skiatook purchased 1,760 megawatt-hours (MWh) of electricity from SWPA on peak. The municipal utility paid SWPA \$40,550 in energy and capacity charges for this on-peak electricity. The daily spot-market prices in our region for this same amount of electricity was \$622,160. If SWPA had been charging these market rates in July 1999, the higher prices to the Skiatook Utility Department would have cost each of its customers \$263 – for the month of July alone! The city of Duncan, Oklahoma, is larger than Skiatook and the energy it purchases from SWPA represents a smaller portion of its total electrical load. But even in this instance, if SWPA had charged the market rates for the on-peak power it sold to the city utility in July 1999, it would have cost each customer \$218 for this one month alone. At City Water and Light of Jonesboro, Arkansas, the additional cost would have been \$157 per customer. At the Malden Board of Public Works, located in the bootheel of Missouri, the cost would have been \$102 per customer.

I have attached some of these examples to my testimony. It is true that in July 1999, market prices for electricity were extremely volatile for our region. However, as I stated earlier, that is the nature of market prices for electricity. While the impact will be less in some months, when load is down due to temperature and weather and supply is plentiful, it can become even greater on hot, humid summer afternoons when unplanned outages occur at large generating units or the transfer demand exceeds the capacity of key transmission lines. I would like to have updated these impact estimations for this testimony, but there were only 16 working hours after the Administration made its surprise announcement Friday evening and before this testimony was due. However, if the Subcommittee desires, I would be glad to provide additional, more up-to-date information for the record.

I understand this budget would “soften” the blow of increasing your constituents’ electric bills by transitioning the PMAs to market rates over a period of years, limiting annual increases in PMA rates to only 20 percent every year for five years, for a total of 149 percent. I’m sure that assurance just warms the cockles of the hearts of consumers in Skiatook and Hominy, Oklahoma, who depend on SWPA energy to meet almost all of their electrical demand. They can rest easier at night, knowing that their government is so concerned over the financial strains on their family budgets.

But what happens that day in the future when PMA rates have been raised to market rates? Not only will your constituents’ electric bills be much higher, but the cost for PMA electricity will fluctuate daily, even hourly, depending upon the whims of the weather and the caprices of supply and demand. What a glorious day that will be. If you think I am exaggerating, visit with some of the consumers of San Diego Gas & Electric. Ask them what happened when their utility was required to purchase all its energy on the spot market and pass the costs along to its customers.

Other Impacts

Generating hydroelectricity is only one of several important public purposes Corps of Engineers multipurpose dams perform. These reservoirs also provide flood control protection, municipal water supply storage, make inland navigation possible, conserve fish and wildlife resources and make tremendous recreation activities possible. Tinkering with the pricing of federal power could jeopardize each of these other important public purposes.

Again, let’s look to that glorious day in the future when, thanks to this budget proposal, PMAs are charging full market rates for the hydropower generated at federal dams. It doesn’t take a Harvard MBA to recognize that, if we hold the water behind the dam until the temperature soars, humidity is stifling and demand is roaring, the electricity generated with this water will make the government a lot more money. After all, that’s what this whole proposal is about, isn’t it – making the government more money? Once we’ve abandoned the concept that federal water resources belong to the people and the benefits thereof should be made available at the lowest possible rates, why not fully embrace the government-for-profit motive?

If we want to maximize government profit through hydroelectric generation, we want to conserve every drop of water behind the dams so that it can be released through the generators only when demand – and prices – are greatest. Releasing

water through the spillway, for whatever good purpose, costs the government hydro profits. Reallocating storage behind the dams to provide additional, needed municipal water supply will cut into the government hydro profits. Which will win out?

SWPA is asked annually to release water through the generators at one of its dams to support a weekend Boy Scout canoe race. Sorry, kids, but in the radiant future of federal hydro profiteering, these operations cost the government money – you lose. SWPA, its customers, the Corps and the Arkansas Game and Fish Commission hammered out an agreement to implement minimum flow releases from two dams to further enhance the blue ribbon White River trout fishery downstream. But it would reduce the dependable capacity of one of the power plants and deny the federal government an average of almost \$1 million every year in hydropower sales at market rates. I guess that deal is a goner.

In fact, now that the Office of Management and Budget has decided the federal government should profiteer from hydropower sales, why stop there? Why not apply this profit motive to the other public purposes of federal water projects? The Carroll-Boone rural water district in Arkansas needs additional water supply storage in Beaver Lake? Great. Your federal government will sell it to you if you line our pockets with profits that are even greater than we could make by using that storage to generate hydropower. Recreation fees at Corps lakes recover only about 30 percent of the annual operation and maintenance costs of its recreation facilities – and none of the construction costs. But all that will change in the new era of government-for-profit. You want to launch your boat at a Corps lake? We'll charge you what it would cost at a private lake. After all, that's the definition of market rates. You want to build a boat dock or a marina? Wow, the federal government could make a bundle off that. Want to stay overnight in a Corps campground? Okay, the cost will be the same as what you would pay at a KOA Campground – maybe even more, if we can get it, what with the beautiful scenery, water access and all. Want to take a swim at a Corps beach? Only if we can make a profit. If you carry this policy to its logical conclusion, you can expect to see pay toilets at Corps campgrounds.

Sound ridiculous? That's because it's a ridiculous proposal with expensive consequences for your constituents.

If it Waddles and it Quacks...

When the government charges a fee to recover its costs of providing a good or service, that's a user charge. When it charges a fee that is greater than the cost of producing the good or service so that government makes a profit – that is a tax.

Mr. Chairman and subcommittee members, this proposal waddles and it quacks. Let's call it what it is – an electricity tax on your constituents. Not a tax on cigarettes, not a tax on the lottery or other forms of gambling – a tax on a commodity necessary for every family's day-to-day life.

How big a tax? Well, the Office of Management and Budget hastens to tell you that it won't amount to much. After all, we'll limit it to only 20 percent a year. By the time this federally taxed electricity is blended with the other sources of energy your local utility uses, OMB assures us, Joe Sixpack won't hardly notice it at all.

OMB says that this proposal will "recover" from electricity consumers \$12.4 billion over the next 10 years. I think that is a very low estimate, but it's still enough to make one blanche. How can this Administration contemplate a 10-year, \$12.4 billion tax hike on electricity bills?

How can you?

The customer associations assembled at this table are joining the battle. We will take it to the House and Senate Budget Committees. We will take it to the chamber floors when the budget resolution comes up for full House and Senate consideration. If it becomes a part of budget reconciliation, we will take the battle to this Committee and to its counterpart in the other body.

We need your help. Your constituents need your help. Please, just say NO! to federal hydropower profiteering. Just say NO! to this \$12.4 billion tax hike on electricity consumers. No matter how you slice it, Mr. Chairman, it's still just budget bologna. Thank you for your attention and consideration.