Committee on Resources
Subcommittee on Water & Power

Witness Statement

Testimony of Gary Zarker
Superintendent
Seattle City Light
Water and Power Subcommittee
House Committee on Resources
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Good afternoon. My name is Gary Zarker, and I am testifying here today in my capacity as the Superintendent of Seattle City Light. Seattle City Light is one of the nation's largest municipally-owned utilities in terms of the number of customers served. We serve a population of 690,000 people over an area of 130 square miles. Our current average consumption is about 1150 average megawatts; about 900 average megawatts are served with our primarily hydroelectric resources. We rely on purchases from the Bonneville Power Administration ("Bonneville") and from the west coast market for the remainder. We are proud of our tradition of meeting one-half of our load growth with electricity conservation.

Seattle City Light is a member of the Public Generating Pool ("PGP"), an association of five large consumer-owned electric utilities in Washington State. PGP members began developing low-cost hydroelectric and other generating facilities more than 80 years ago. Today, they own some of the largest FERC-licensed hydro projects in the U.S. and, collectively, are the largest generators of nonfederal hydropower in the nation.

PGP members make extensive use of the Bonneville transmission system to deliver and receive nonfederal power. Each PGP member has public preference rights to purchase wholesale power from Bonneville, and through these purchases, provides substantial funding for Bonneville's programs and obligations, including environmental programs and Treasury repayment. PGP members also directly fund their own fisheries, wildlife, cultural resource and recreational programs.

You have asked for testimony today regarding several Bonneville issues. I will address these issues, but focus my testimony on what we refer to as Bonneville's "slice" product.

Slice of the System

PGP first proposed the slice of system product to Bonneville in November of 1997. I want to describe the context in which the product was developed. Today, thanks to several consecutive high water years, some cost control on Bonneville's part, and a general increase in west coast power market prices, Bonneville offers attractive and competitive power rates. That wasn't the case in 1997, when Bonneville's rates were at or above market and projected to be non-competitive. Many customers were seeking to leave the federal system and the region was concerned about Bonneville's ability to meet all of its obligations, including Treasury payments.

It was during this period of uncertainty that the "slice" was proposed to BPA, to be developed as a product

that could be offered in the subscription process. We felt it was necessary for Northwest utilities to step forward and show Congress that we are committed to taking long term responsibility for the Columbia River System. Also, we saw that with significant changes occurring in utility structure and regulation, it was no longer appropriate to have Bonneville responsible to serve all of our net requirements. That places an open-ended burden on the U.S. Treasury, and gives the federal government too strong a hand in the competitive marketplace.

"Slice" is not a new or novel product; many utilities in our region already offer contracts similar to slice. Furthermore, the slice product came out of the recommendations made by the Comprehensive Review of the Northwest Energy System, or Regional Review. I served on the Steering Committee of the Regional Review. Our goals with respect to federal power marketing were straightforward -- ensure repayment of Bonneville's debt to the U.S. Treasury, and retain the long-term benefits of the federal system for the region. To accomplish these goals, the review proposed long-term (15 to 20 year) cost-based contracts that would enable Bonneville's customers to assume greater risks of variations in weather, system costs including fish and wildlife obligations, and changes in market conditions. The idea was to transition Bonneville away from being an aggressive power marketer in the coming competitive market, and disperse power marketing activities among its customers. The Slice product is the result of those recommendations.

That is how the concept was originated. Now I will describe how it works. A "slice" purchaser buys a fixed percentage of the federal system output for the same fraction of Bonneville's total costs. The costs include Bonneville's generation costs, obligations to the Treasury and WPPSS bondholders, residential/small farm exchange, public purposes, fish and wildlife and other environmental costs and obligations.

The energy output attributed to a "slice" fluctuates with Bonneville's output. The purchaser bears responsibility to manage these variations and the growth in its load, and accommodate those fluctuations received from the slice. The purchaser is able to meet these responsibilities by combining the slice purchase with other products in its portfolio – its own generation, other Bonneville products, or other market sources.

While the slice product behaves in some ways like the purchaser's own hydroelectric generation, I would emphasize that slice purchasers do not own the slice. Purchasers have no authority in river management, or over BPA investment or other management decisions. Slice does not impact Bonneville's statutory, legal or treaty obligations.

We are pleased that Bonneville has offered the product in its current subscription process. Bonneville has done a fine job of working with Northwest utilities on a direction that is helpful to the Northwest and to the federal taxpayer. The slice product not only provides us with an important risk-management tool; the product benefits customers, the region, Bonneville, and the Federal Treasury.Benefits of Slice

To discuss the benefits of slice, let me again refer to the goals and findings of the Regional Review which led to the proposal of slice. Slice enables Bonneville to share the risks of resource fluctuations and system costs and obligations with all slice purchasers, in turn helping to maintain the viability of the federal system. With some of the burdens of system obligations removed, Bonneville is better able to recover costs, which protects the U.S. Treasury and WPPSS bondholders. Also, with slice contracts, Bonneville's role in the Northwest is transitioned away from that of an aggressive federal power marketer, which we believe is inappropriate in the emerging competitive market.

You have asked if the product should be offered to everyone in the region; based upon this vision of sharing burdens and benefits, we initially proposed that the product be offered to all of Bonneville's customers.

Bonneville has decided to narrow the eligibility for slice, so only preference customers qualify at this time. However, my personal sense is that at some point, slice should be offered more broadly if the region as a whole is to take longer term economic and environmental responsibility for the federal system.

The Chairman has asked about the level of Bonneville's reserves. Our understanding is that the reserve level is not set in the abstract. It is the amount that is needed to meet Bonneville's firm obligations, including Treasury payments, across a range of market and water conditions. Bonneville's need for large reserves is primarily driven by power purchase costs to meet requirements contracts in bad water years. The number can be reduced, but not without increased risk. The slice product makes a real contribution here in reducing the size of the reserve needed, because buyers are not asking Bonneville to meet their net requirements in tight market conditions.

I've outlined the benefits of slice for the region and Federal System. In addition to these benefits, the slice product is economically attractive to Seattle City Light and other systems in the Northwest. When looking at the economic benefits of slice, I note that you must look at them in conjunction with other parts of a system's portfolio. No system will rely solely on the slice product; it is a percentage of an overall portfolio and a single tool in the kit. Why do we want the tool in our kit? Slice is well suited for today's rapidly changing, restructured marketplace. Bonneville manages the federal system to meet its power and non-power requirements; this is true whether we are talking about a slice contract or more traditional contract. Slice gives us no role in managing the federal system; however, the fluctuating character of slice offers us an opportunity to manage our whole portfolio in the best interest of customers. Being in closer proximity to our customers and our day to day needs than Bonneville can be, we believe we are in the best position to make decisions regarding marketing power we provide to customers. And in this competitive environment, we feel it is important that we pass on to customers the benefits of the greater efficiencies slice can provide.

Some questions have been raised about the economic risk of this product. We are looking at those risks right now. We own and operate hydro facilities on stretches of water with endangered salmon species. We face the vagaries of drought and surplus in our own system. And we have learned how to manage those risks. We can, if needed, add surcharges to retail rates to address a rapidly emerging problem. That action is not so easy for Bonneville.

Contract Length

You have asked for an opinion on the length of contract Bonneville should offer. The slice contract, as well as certain other Bonneville contracts, has been proposed to be available for ten years. Much has been made recently about whether Bonneville contracts should be limited to five years. I can answer the question about contract lengths in terms of what is workable and useful for customers. Slice requires at least a ten-year contract. The reason for that is simple: I don't know when the rain will fall. Slice is a regional risk-sharing mechanism, and it will involve fluctuations. Ten years is the minimum length needed for a system such as ours to absorb those risks. I wouldn't take slice for less than ten years, because as a risk-management tool, slice needs a sufficient horizon through which to average fluctuations. The Regional Review contemplated 15 to 20 year contracts; these are also desirable contract lengths, though Bonneville has opted to propose slice for a 10 year term.

Some have suggested that Bonneville should only sign short term contracts, out of concern that this will lock up existing allocations. In my view, long term contracts are not the problem. They would not prevent Congress from enacting legislation, if needed, to restructure the manner in which Bonneville's power is allocated, or modernize Bonneville. Contracts for Bonneville power will exist at any time legislation is

enacted. Finally, I would point out that for traditional 10-year contracts, the rate is guaranteed only for the first five years. There is no mechanism for customers to "lock in" a deal with Bonneville for more than five years.

Regional Transmission Organization ("RTO") Participation

You have asked me to comment on other issues today as well. With respect to Bonneville's role in an RTO, we would point out that Bonneville must of course participate in any regional RTO given its ownership of the bulk of the transmission system, but we would have concerns with any proposal that permits Bonneville to be the RTO. As FERC has stated in Order No. 2000, we believe RTOs should be independent from all market participants, both in perception and reality.

Conclusion

I want to conclude today by touching once again on the benefits of the slice product. It benefits the region by establishing a mechanism for sharing Bonneville's risks and responsibilities in good and bad water years. It benefits the Treasury by reducing the risk of a missed Treasury payment. It benefits WPPSS bondholders by reducing the risk that Bonneville cannot recover its costs. It benefits the purchaser and its customers, allowing the slice purchaser to optimize the use of its resources and make decisions in terms of marketing power that can best serve its customers. It reduces the size of the contingency fund that Bonneville will need. And, we believe it is the environmentally appropriate product because it allows environmental decisions to be made on the basis of sound science and economic prudence without the artificial economic constraints imposed by fixed price contracts. We appreciate the opportunity Bonneville has provided to work together to develop this important product.

Thank you for the opportunity to testify before you today. I will be glad to answer any questions you may have.

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