

TESTIMONY OF STEPHEN J. WRIGHT  
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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

BEFORE THE  
  
COMMITTEE ON RESOURCES  
SUBCOMMITTEE ON WATER AND POWER  
UNITED STATES HOUSE OF REPRESENTATIVES

MARCH 1, 2006

Mr. Chairman and Members of the Subcommittee, I appreciate the opportunity to be here today to discuss both the Bonneville Power Administration's (Bonneville) implementation of the Energy Policy Act of 2005 and the President's FY 2007 budget as it relates to Bonneville. The Subcommittee's attention and support have been and will continue to be essential as we move ahead.

In my testimony today, I will first share with the Committee how Bonneville is working to incorporate the provisions of the Energy Policy Act. I will then discuss Bonneville's significant successes over the past year and the challenges we are facing for the upcoming year, followed by an overview of the FY 2007 budget and its proposals.

### **ENERGY POLICY ACT IMPLEMENTATION**

The Energy Policy Act is far-reaching and has the potential to impact energy issues in the Pacific Northwest for a long time. Bonneville has a long history of providing reliable transmission service in the Pacific Northwest and has, since 1996, filed reciprocity tariffs with the Federal Energy Regulatory Commission (FERC) that apply transmission terms and conditions to all transmission users on a comparable, nondiscriminatory basis. Bonneville has also been at the forefront of regional and national efforts to strengthen system reliability. While the Energy Policy Act of 2005 does not single Bonneville out for action in any particular instance, it will cause changes to Bonneville's operating environment, and so we are proactively contributing to its implementation.

Two of the most important provisions potentially affecting Bonneville are Sections 1211 dealing with reliability and 1232 authorizing Bonneville to join a regional transmission entity.

Section 1211 provides for FERC to designate a single Electric Reliability Organization (ERO) for the United States. This entity will be authorized to propose, for FERC's review and approval, mandatory reliability standards that will govern the practices of all users, owners, and operators of the bulk power system, and to enforce them through a

system of sanctions and monetary penalties to be administered by regional reliability organizations. Bonneville has been actively contributing to the implementation of this system by working with the North American Electric Reliability Council (NERC), which will apply to FERC for certification as the Electric Reliability Organization (ERO), and with the Western Electricity Coordinating Council (WECC), which will seek the enforcement role in the Western Interconnection. The success of complex relationships between FERC and NERC and WECC, and the generation and transmission operators in the West is absolutely crucial to the smooth functioning of our part of the Nation's bulk power system. It is a part that is physically quite different from the East, so the challenge is to achieve a uniformly high quality of reliability through sometimes different regional means. This is an extremely complex undertaking and managing this transition is our highest priority in the coming year. FERC sent encouraging signals in their final rulemaking on Section 1211 by acknowledging and providing for accommodation of regional differences and by allowing NERC and the regional reliability organizations to create a first approach to specific application of many of the governance and process prescriptions of Section 1211.

Section 1232 authorizes The Secretary of Energy or, upon designation by the Secretary, the Bonneville Power Administration, to make arrangements for Bonneville to participate in a regional transmission organization under certain conditions. Bonneville is involved with efforts to address transmission functions that could be carried out by a regional transmission entity under a "one-utility" vision for Northwest transmission where the region's transmission system would be managed as though owned by a single utility. Although this is a vision for the Northwest power system that has guided regional policy making for decades, there is a wide divergence of opinion within the Northwest regarding the type of transmission organization that is appropriate for the Region.

An attachment is included with my testimony today that highlights Bonneville's approach to several other provisions of the Energy Policy Act. Our actions are designed to support the Administration's commitment to expand our Nation's energy supply by developing

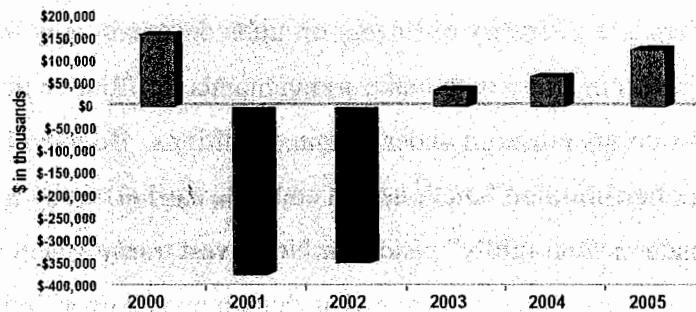
a diverse, dependable energy portfolio for the future, and the critical infrastructure that is necessary to sustain it.

### **BONNEVILLE'S RECENT SUCCESSES**

FY 2005 was marked by another major stride in improving Bonneville's financial health while making significant investments in our region's electric infrastructure. We exceeded our net revenue targets, earning just over \$126 million in modified net revenues, the highest since the big losses were suffered during the West Coast energy crisis. The table, which follows, shows a historical comparison of modified net revenue results. BPA has determined that modified net revenues are a better representation of the outcomes of normal operations and are more similar to calculations developed as part of the initial rates for the current rate period.

#### **B O N N E V I L L E P O W E R A D M I N I S T R A T I O N**

### **Modified Net Revenues**



For the twenty-second year in a row, Bonneville made its planned repayment to the Treasury on time and in full.

It was also a year of major milestones in our business. On the transmission side, we continued our program to shore up the region's reliability, meeting our target for

completing construction projects on schedule and within budget. The Grand Coulee-Bell 500-kilovolt line in eastern Washington, our largest transmission project in two decades and one of the largest in the Nation, was energized last December. The line relieves congestion from east to west and enhances system reliability while increasing capacity to move new generation to consumers.

On the power side, Bonneville conducted a public process called the Power Function Review (PFR) to help determine program funding levels for the next power rate period, 2007-2009. We completed a short-term Regional Dialogue to address power sales contract issues relevant through 2011. We also opened up a long-term Regional Dialogue on Bonneville's power supply role beyond 2011.

We met our 2005 targets for conservation savings and efficiency improvements to the generating system, achieving 43 megawatts of new conservation and 20 megawatts of additional hydro generation capability.

These and many of our other successes in 2005 were guided by the development of our long-term Strategic Plan that was completed in early 2004. This Plan laid out Agency direction through FY 2011 and grew out of the need to set long-term objectives along with strategies to reach those objectives. Bonneville has now moved into the implementation phase of this Plan with a focus on Bonneville's future power supply role along with infrastructure development, risk management, technological innovation, conservation and renewables, facilitation, and efficiency initiatives—all of which help set the stage for the region's long-term energy future.

## **UPCOMING CHALLENGES**

Bonneville markets wholesale power and provides other benefits to virtually every utility in the Pacific Northwest. With current power rates set to expire in 2006, Bonneville is in the midst of its first full-fledged wholesale power rate case in five years. In addition to the completed Power Function Review, Bonneville is currently initiating a second public

review of costs to seek further reductions in order to hold FY 2007-2009 rates down. Bonneville is scheduled to adopt a final proposed rate structure this July that will take effect October 1, 2006.

With existing power contracts due to expire in 2011, Bonneville must establish clearly its future power supply role and has initiated a long-term Regional Dialogue that is designed to create more certainty for the region and that should lead to more investment in electric system infrastructure. We believe increased clarity about how much power Bonneville will provide beyond 2011, and at what price, is essential to assuring adequate infrastructure investment by other parties.

Bonneville funds a diverse and comprehensive fish and wildlife program to mitigate impacts of Federal hydropower development on Columbia Basin fish and wildlife. All together, our direct fish and wildlife costs, plus foregone revenues, are expected to average nearly \$700 million annually in the FY 2007-2009 period. Litigation, dating back to 1995, continues over the operation of the Federal Columbia River Power System (FCRPS). Bonneville, the Army Corps of Engineers, the Bureau of Reclamation, the National Oceanic and Atmospheric Administration, and the Northwest States and Tribes are all currently collaborating to gain agreement on performance objectives, the scientific framework, and the Government's Proposed Action. Without such agreement, the stability and predictability of the hydro system is at great risk.

Bonneville is also focusing internally. We are in the midst of a multi-year, agencywide efficiency program designed to further lower our costs. Implementation of efficiency recommendations is occurring incrementally and has already led to consolidation and centralization of some agency functions, and simplification of operational processes.

## **BONNEVILLE'S BUDGET INITIATIVES**

Beginning in the President's fiscal year 2007 budget released to Congress and consistent with sound business practices required under the Federal Columbia River Transmission System Act of 1974, the budget provides that Bonneville Power Administration will use any surplus power sales (net secondary) revenues it earns in excess of \$500 million per year to make early payments on its federal bond debt to the US Treasury.

This administrative action will both reduce the federal deficit and provide BPA with needed financial flexibility to invest back into energy infrastructure and to pay down debt. BPA will make no additional payments to the Treasury as a result of this action if surplus revenues do not exceed \$500 million in a year.

BPA markets its surplus electricity production to customers both inside and outside the Pacific Northwest. In the last decade, BPA has an average of \$457 million per year in net secondary revenues. BPA will potentially realize record high levels of surplus revenues due to high wholesale electric prices in the West. The budget reflects a total of \$924 million from FY 2006-2016 from net secondary revenues greater than \$500 million per year.

The President's budget action would extend the use of Bonneville's borrowing cap with the U.S. Treasury by about three years. Absent the President's Budget, BPA could have run out of borrowing authority in the year 2011.

It is the Administration's position that it is sound business practice to use higher-than-historical net secondary revenues to pay down debt, consistent with statutory priority of payment requirements. The Administration believes this action will help to provide Bonneville with needed financial flexibility to meet its future energy investment needs, including new transmission capacity, and that long-term power and transmission customers of Bonneville will benefit from these advance amortization payments through lower long-term rates than would otherwise be the case.

BPA's surplus sales revenue lowers power rates today in the Pacific Northwest. The Budget does not reduce the historic level of regional benefit from such sales- it retains the benefit of all surplus sales revenues for BPA ratepayers, but changing the time frame that such benefits will be realized. This proposal is not expected to have a rate impact in 2007, but it could prevent rates from being about 5 percent lower for retail customers than they otherwise would have been in 2008 and 2009, without this early repayment program. This rate impact will be offset by benefits in future years.

In addition, the Budget provides that Energy Northwest will refinance a portion of its debt in the calendar year 2006 and 2007. The additional \$382 million freed up from these future refinancings will be used to pay down BPA federal debt.

The combined effect on the U.S. budget deficit of these two proposals is estimated to be \$1.3 billion. This is an amount that could be borrowed again by Bonneville in the future under its Congressional borrowing ceiling. This initiative takes advantage of a potential unique opportunity to make a long-term investment in the Pacific Northwest's electricity future. We are proceeding with implementation. The expedited rate case is scheduled to begin in July 2006.

## **FY 2007 BUDGET OVERVIEW**

Mr. Chairman, Bonneville is in sound financial condition. Our reserves are at a level that will assure we can make our full annual payment to the U.S. Treasury at the end of this fiscal year, despite having been through six straight below-average water years before this year. Bonneville's FY 2007 budget projects \$2,464 million for operating expenses, \$95 million for Projects Funded in Advance, and \$477 million for capital investments. Since its budget is funded by sales of power and transmission services, and proceeds of bond sales to the Treasury, Bonneville has not requested or received annual appropriations since 1974.



Bonneville's commitment to fish and wildlife mitigation and enhancement is exemplified in its direct program budget of \$178 million, capital and expense, for this purpose in FY 2007.

Bonneville's full time equivalent (FTE) staff projection included in this budget is 3,000 for FY 2007. Bonneville's cost management initiatives have brought this number down from the higher level we needed during the ramp-up of our infrastructure expansion program.

Bonneville utilizes numerous performance measures linked to its strategic vision and financial results. The President's budget performance measures for Bonneville encompass overall electric hydro availability, transmission reliability, repayment to the U.S. Treasury and safety. The safety measure includes a Department determined stretch target for FY 2007 of no more than 2.7 for Recordable Accident Frequency Rate.

Bonneville's budget assumes that the Spectrum Relocation Fund (SRF), established in the Treasury to facilitate the relocation of Federal radio communication systems, will provide Bonneville, through a non-expenditure transfer from the SRF, with full budget authority and cash to cover the cost of relocating Bonneville's 1710-1755 megahertz radio communication systems. The estimated Bonneville cost of this relocation is \$48.7 million.

The following table provides budget data (dollars in 1,000's) based on current services for FY 2005 through FY 2007:

	FY 2005	FY 2006	FY 2007
Capital Investments			
Power Business Line .....	116,007	210,000	201,000
Transmission Business Line .....	141,721	200,689	251,541
Capital Equipment & Bond Premium. ..	12,579	26,461	24,252
Total, Capital Investments .....	270,307	437,150	476,793
Accrued expenditures will require budget obligations of .....	270,307	437,150	476,793
Operating Expenses .....	2,572,513	2,633,300	2,464,963
Projects Funded in Advance .....	80,256	71,887	94,989
Capital Transfers (cash) .....	657,983	436,783	877,573
Bonneville Net Outlays .....	(155,000)	(80,000)	(480,000)
Bonneville Staffing (FTE) .....	3,046	3,025	3,000

**The accompanying notes are an integral part of this table.**

Budget estimates included in this budget are subject to change due to rapidly changing economic and institutional conditions in the evolving competitive electric utility industry.

Bonneville Bond Amortization/Capital Transfers in this FY 2007 budget reflect, beginning in FY 2007, advance amortization payments to the United States Treasury on Bonneville's bond obligations. The advance payments are dependent on an equivalent amount of assumed net secondary revenues over \$500 million and anticipated debt optimization refinancing of ENW obligations, consistent with both the President's budget and the sound business practices required under the Federal Columbia River Transmission System Act of 1974. The policy of the President's budget regarding use of extraordinary net secondary sales revenues will be implemented through a Bonneville rate proceeding.

Amounts of such estimated payments to Treasury vary from associated net secondary revenues and debt optimization amounts due to timing of Treasury payments and other factors. Actual associated net secondary revenues and debt optimization effects could vary due to volatility of secondary power markets, stream flow variability, volatility of financial markets affecting ENW debt optimization, and other uncertainties.

## **BONNEVILLE TREASURY PAYMENTS**

Bonneville made its planned payments to the U.S. Treasury on time and in full in FY 2005, for the twenty-second consecutive year. Included in these payments totaling \$1,088 million was \$313 million in early amortization of our Treasury debt. Since its creation in 1937, through FY 2005, Bonneville has returned \$21.6 billion to the U.S. Treasury. During FY 2007, we anticipate paying \$1,329 million to the Treasury, of which \$878 million will be repayment of principal, \$430 million will be interest, and the balance of \$21 million will be applied to the unfunded liability of the Civil Service Retirement System.

In recent years, Bonneville has made amortization payments in excess of those scheduled in its FERC-approved rate filings resulting in a balance of advance repayment. The cumulative amount of advance amortization payments as of the end of FY 2005 is about \$1,460 million.

## **CONCLUSION**

In conclusion, I am pleased to say we have made significant progress in regaining Bonneville's financial health since the West Coast energy crisis of 2001-2002, and we are well on our way to meeting the upcoming challenges facing us today. Bonneville will continue its efforts toward long-term financial stability and its commitment to meeting its overall responsibilities to keep the lights on in the Pacific Northwest. Bonneville is well positioned as it looks forward.

**Attachment A:**

Additional Energy Policy Act Provisions Likely to Have  
A Significant Impact on Northwest Electric Power Issues  
In Which Bonneville is Actively Involved

Section 368 provides for the Federal Government to designate “energy corridors” on Federal lands that would be used for electric power transmission lines, and pipelines to transport oil, natural gas, hydrogen, and potentially other fuels. Bonneville is supporting this effort in the Pacific Northwest. DOE is coordinating the Federal agencies involved in this issue. Bonneville believes it is important to assure that safety, security, and electric reliability issues are not created when pipelines are considered for location in proximity to electric power transmission lines.

Section 1221 provides for the Federal Government to designate “public interest corridors” for siting of new transmission needed for reliability. Bonneville is actively involved in supporting DOE’s efforts to identify potential transmission corridors in the Northwest. Bonneville expects to stay engaged in this effort through its completion.

Section 1231 provides FERC authority to require by rule or order that transmitting utilities that are public bodies, like Bonneville, provide their unregulated transmission service at rates comparable to those the utility charges its own generation, and on terms and conditions that are similarly comparable and not unduly discriminating or preferential. Bonneville believes it already meets these standards and has been operating this way since 1996. FERC has opened an inquiry regarding revisions to its pro-forma tariff, and Bonneville is actively contributing to that process.

Section 1233(b) assures that load-serving utilities, like Bonneville, will continue to be entitled to use transmission rights to meet their service obligations. FERC has recently issued a Notice of Proposed Rulemaking on this issue. Bonneville expects to comment to FERC on its proposed new rule and participate in this important policy development.

Section 1234 provides that the Secretary of Energy must conduct annual studies of the procedures used by electric utilities to perform economic dispatch, of possible revisions to those procedures, and of potential benefits to consumers from improving such procedures. The Secretary is also directed to recommend appropriate legislative and regulatory actions with respect to economic dispatch. Bonneville has provided comment regarding the important differences between thermal and hydro systems and the need to take these into account when considering economic dispatch.

Section 1286 grants the Federal Energy Regulatory Commission (FERC) refund authority when a non-jurisdictional utility's sale of 31 days or less, made through an organized market in which the rates for the sale are established by a Commission-approved tariff (rather than by contract), violates the tariff or FERC rule. Bonneville actively monitors FERC's requirements and its own operations to assure it is not violating the tariff or FERC rule.

Section 1834 instructs the Departments of Energy, Defense and Interior to jointly conduct a study of the potential for increasing electric power production capability at federally owned or operated water regulation, storage, and conveyance facilities. Bonneville and other Power Marketing Administrations in the Department of Energy have been working with the U.S. Army Corps of Engineers and the Bureau of Reclamation on such a study. Results from the study are expected to become available in early 2007.

Additionally, Bonneville has for several years been funding projects within the hydroelectric investment program that support generation efficiency improvements within the Federal Columbia River Power System. This has included replacement of existing turbine runners with higher efficiency ones and development of operational process improvements that have resulted in increased efficiency. The program to date is estimated to have achieved an increase of 87 annual average megawatts, assuming average water conditions.

Subtitle G of Title XII contains several provisions that deal with electricity market transparency, enforcement and consumer protection. Bonneville is actively following FERC developments in this area. Bonneville is subject to these new rules and has taken steps to assure that it is in compliance with their requirements. Bonneville believes these new rules are an important tool to address market manipulation that plagued the West Coast market in 2000 and 2001.

Subtitle A of Title I relating to Energy Efficiency contains a number of provisions that affect Bonneville's procurement practices. For example, Section 104 provides for agencies to procure products that meet certain energy standards. In many instances, Bonneville had implemented procurement policies that meet or exceed the requirements of the Act before its enactment. In other instances, Bonneville may need to update its practices. For example, Bonneville has had a standard policy to purchase recycled concrete products, where feasible, for many years, as now required by Section 108. Bonneville is looking into whether these and similar procurement policies may need to be updated in light of the new Act.

Title VI contains provisions relating to nuclear energy. Through Energy Northwest, Bonneville receives power from Columbia Generating Station, a large nuclear power plant located in Richland, Washington. Several provisions change various requirements for operators of nuclear facilities. For example, Subtitle D adopts a number of security-related practices for nuclear operators. Bonneville and Energy Northwest either have made appropriate modifications in policy to comply with the Act, or are in the process of doing so.

The Act contains many provisions encouraging energy efficiency, new technological developments, and renewable resources within the electric power sector of our economy. Bonneville has been active in these areas for many years. Bonneville has a very active and successful energy efficiency program which yielded 43 aMW of new electricity savings in 2005, adding to a total of 900 aMW achieved over the last 25 years.

Bonneville has supported more stringent energy standards for appliances, buildings, and other electric-power-consuming applications for many years.

Bonneville is also an active participant in the Department's GridWise program where it is working with the Pacific Northwest National Laboratory and other Northwest utilities to test devices installed in Northwest home appliances, such as water heaters and clothes dryers, that detect system problems and automatically respond by shutting the appliance off or on, as appropriate, to respond to system conditions. This is a promising technology that Bonneville believes could pave the way for cost-effective demand response and a "smart grid" that detects and responds automatically to system disturbances and related operational problems.

Section 503(a) amends the Energy Policy Act of 1992 to provide that each Power Marketing Administration (PMA) Administrator shall encourage Indian tribal energy development by taking such actions as the Administrators determine to be appropriate, and that an Administrator may provide technical assistance to Indian tribes seeking to use the high-voltage transmission system for delivery of electric power. Bonneville is developing long-term contracts and policies that we believe will encourage resource development by tribes and other resource developers in the Pacific Northwest, and we routinely provide transmission technical assistance to tribes. Bonneville provides the tribes open, non-discriminatory access pursuant to its FERC-approved transmission tariff. Bonneville has also assisted tribes in forming electric distribution utilities to provide retail service to tribal facilities and communities. This section also provides that, within two years of passage of the Act, the Secretary of Energy is to submit to Congress a report that, among other things, describes tribal use of PMA power and barriers that impede tribal access to and use of Federal power, including an assessment of

opportunities to remove those barriers and improve the ability of power marketing administrations to deliver Federal power. We will actively support and contribute to that report.

Energy Policy Act Provisions that may have  
A Significant Impact on Northwest Electric Power Issues  
that Bonneville is Following, but Not Directly Involved

Section 1303 extends the renewable energy production tax incentive through 2007. Bonneville is purchasing substantial quantities of wind generation now, but is not seeking new renewable power purchases at this time. A number of utilities in the Northwest are pursuing wind acquisition strategies. Bonneville is taking a number of actions to facilitate these efforts by regional utilities. Bonneville has received and is processing a number of requests for integration studies, and has also received requests to reserve transmission for many of these projects.

Subtitle F to Title XII contains provisions that repeal the Public Utility Holding Company Act. Bonneville is following developments in this area because of the potential for utilities in the Pacific Northwest and nearby areas to become involved in mergers and acquisitions. Currently three Northwest utilities are involved in potential change of ownership: Portland General Electric (which is being sold by Enron Corporation), PacifiCorp (which is being acquired by Mid-America), and Northwestern (which is being solicited by several potential buyers). A change of ownership of these utilities could change the approach they have had historically toward investing in new transmission and generation, supporting a regional transmission organization, and working with Bonneville on common issues of interest.