

Testimony of

**Ted Coombes, Executive Director
Southwestern Power Resources Association**

**“Power Marketing Administrations:
A Ratepayer Perspective”**

Before the

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Committee on Natural Resources
U.S. House of Representatives**

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Mr. Chairman, my name is Ted Coombes. I am Executive Director of Southwestern Power Resources Association (SPRA), which represents the preference customers of Southwestern Power Administration (SWPA). These preference customers are rural electric cooperatives, municipal utilities and state power agencies that, by federal law, have the first right to purchase hydropower from Corps of Engineers multipurpose water projects. SWPA markets the energy and capacity from 24 Corps dams in our region to SPRA members in Oklahoma, Arkansas, Missouri, Texas, Kansas and Louisiana.

Unlike most federal programs, the federal Power Marketing Administrations pay their own way. Every dollar spent on the federal power program is returned to the Treasury. This includes the construction, operation and maintenance and transmission costs incurred in generating and marketing the hydroelectric energy and capacity incurred by both the generating agency (Corps, in our case) and the PMA, plus interest on capital costs. Meanwhile, the Corps and the PMA must depend upon Congressional appropriations to meet their annual expenditures.

Today's hearing focuses on the customer's perspective of PMA Operations. In my testimony today, I would like to cover four points:

- A joint agreement between the Corps, SWPA and the its federal power customers, known as the Jonesboro Memorandum of Agreement, is a success story showing how cooperation can address dwindling federal appropriations for Corps hydropower maintenance, repair and replacement.
- To further reduce the need for future appropriations, there should be a special receipts disbursement account for SWPA established with U.S. Treasury.
- Implementation of the authority granted SWPA and Western Area Power Administration to participate with and assist nonfederal entities, including for-profit corporations, in the construction, operation, maintenance and/or ownership of new electric transmission facilities as authorized by Section 1222 of the Energy Policy Act of 2005; and
- Concerns PMA customers have over increasing involvement of Department of Energy headquarters in the day-to-day operation of the PMAs which is leading to "mission-creep."

Jonesboro MOA: A Success Story

Beginning in the 1990s, federal power customers began noticing increased unscheduled outages at Corps and Bureau of Reclamation hydropower plants. These outages were costing PMA customers and their retail electric consumers, because significant outages often make it necessary for PMAs to purchase expensive, on-peak replacement thermal energy (and sometimes capacity) to meet their contractual obligations to their wholesale customers. Further, because of federal budget cycles, waiting for appropriated funding for a crippled plant that requires significant equipment repair and/or replacement before returning to service might extend the outage – and the cost – over multiple years. In the best-case scenario, a forced outage due to equipment failure that occurs in June 2013 would not see appropriated funding until October 1, 2014. This is because the federal fiscal year begins October 1 and ends the following September 31. Even if federally appropriated funding is available, the project described would have missed the time

window to get money appropriated for FY 2014 (which begins October 1, 2013). That plant would remain idle and major repairs could not begin until October 1, 2014 – assuming the funding is appropriated for FY 2015. The outage would continue from that date until the equipment is acquired, transported and installed – a process itself that can consume months and even years. Meanwhile, until the unit is returned to service, the PMA will have to purchase more expensive replacement power whenever customer load exceeds federal hydro availability until the unit is returned to service.

Again, what I have described is a best-case scenario. Appropriations for major equipment repair and replacement does not often occur in the first full budget cycle after the failure event. For example, a unit at the Corps' Webbers Falls Lock and Dam was out of service for more than eight years before funding became available and the unit returned to service. That is an expensive outage for our retail electric customers – an outage outage, if you will.

As SPRA studied this problem, we noticed that the increased outages coincided with decreased appropriations for federal hydropower plant operation, maintenance, repair and replacement, including major rehabilitations. This co-incidence was no coincidence. Federal budgetary pressures led to reduced appropriations for this purpose. Reduced maintenance and timely equipment replacement led to increased and longer outages, which led to increased PMA expenses for replacement energy, which led to higher PMA rates and higher retail electric rates. How ironic it is that this should occur in a federal program that repays all of its costs – plus interest on capital costs – to the U.S. Treasury. Reduced appropriations to the federal power program do not represent savings to the U.S. Treasury. Had the funding been timely appropriated, it would have been returned to the Treasury. Instead, electric consumers faced higher costs.

As this same situation began to appear in other PMA regions, it became evident that it only made sense for us to devise a system whereby priority projects could be directly paid for by customers. After all, for us it's a "pay me now or pay me later" situation. We pay the costs, whether we provide the funding directly to the Corps or indirectly through appropriations that are subsequently returned to the Treasury. By paying up front, before the equipment failed, we could save millions of dollars for our utility customers.

Various PMA customer groups approached this problem in manners that best suited their abilities and the authorities of their generating agencies (Corps and Bureau) and marketing agencies (PMAs). At SPRA, together with the Corps and SWPA, we put together the Jonesboro Memorandum of Agreement (Jonesboro MOA). Under this agreement, the customers meet with the Corps and SWPA to determine the funding needs for the following fiscal year. Together we rank projects based on their need and risk of failure and choose the ones that should be funded in the next fiscal year. If one of those projects receives appropriated dollars, that's fine – it is marked off our "to-do list". If not, we put together a subagreement identifying the work to be done along with the estimated cost, and customers contribute these funds into an escrow account. The work does not begin until the necessary funding for the entire project is accumulated in the escrow account (even if it is a multi-year project).

This project has been a resounding success. Since 1999 we have funding 212 subagreements at an estimated cost of more than \$305 million. We have committed to the Corps that we can raise, through the Jonesboro MOA, about \$2.4 billion over the next 30 years to complete rehabilitation of all 24 Corps hydropower plants marketed by SWPA. We have demonstrated, through a cash-flow study, that we can raise that kind of capital over that period to get the job done.

Success stories like this are being reported by PMA customer groups in other regions around the country. We're not freeloaders – we pay our own way.

Receipts and Disbursement Fund

Southwestern has suffered through two severe droughts over the past eight years. These droughts are real challenges. Water is the fuel the Corps uses to run our hydro turbines. Less water means less energy, and ultimately, less available capacity. As energy production falls, more must be purchased from thermal generation to meet contractual obligations to federal power customers. A lot less water means a lot less energy, which means a LOT more money needed to purchase replacement energy and power.

Annual changes in hydrology mean annual changes in the amount of replacement energy required. SWPA has worked with its customers to devise rate mechanisms to reduce rate fluctuations caused by changes in hydrology. But severe drought can overwhelm even these precautions, leading to rate increases.

For example, in the 2005 – 2006 drought SWPA customers voluntarily agreed to reduce Southwestern's contractual obligations to them. Despite this voluntary reduction in demand, SWPA purchased \$67 million of thermal energy to supplement its available hydro energy. Despite our best efforts, total energy purchases required a 14% rate increase phased in over three years.

To reduce future large rate fluctuations due to changes in hydrologic conditions, SWPA instituted several changes, including increasing the amount of annual revenues to be available for power purchases. We have suffered another drought in the past year, but our power pools have refilled late this spring, and we are hopeful that the worst is behind us. Despite SWPA having to purchase another \$60 million of thermal energy during the most recent event, SWPA proposes a rate increase of about 4.5 percent beginning in 2014 – only a portion of that reflecting recovery of purchased power costs.

So the actions taken by Southwestern to counter drought-induced major rate increases have succeeded – so far. But we have not endured a drought as severe as our drought of record, which occurred in the 1950s. Unless additional action is taken, we cannot rule out the possibility that a severe drought might require SWPA to seek emergency appropriations to purchase sufficient thermal energy to meet its load requirements.

To avoid this, SPRA proposes that SWPA be authorized to establish within the Treasury a special fund, to be known as a receipts and disbursement account. Funds precollected from its customers for replacement power purchases could be deposited in the fund and disbursed as the

need exceeds SWPA's resources. This could do much to eliminate the need for major rate swings or need for special appropriations to SWPA during the conditions we have experienced and are likely to experience again.

Section 1222

Earlier I explained that in Section 1222 of the Energy Policy Act of 2005, Congress authorized SWPA and Western Area Power Administration (WAPA) to participate with and assist other entities in constructing, operating, maintaining and owning transmission facilities needed to serve the bulk power system. SWPA is now considering a plan submitted by Clean Line Partners LLP to assist with a high-voltage direct-current (HVDC) transmission line from Western Oklahoma through Arkansas for proposed delivery into a Tennessee Valley Authority switchyard north of Memphis. The proposed project would be about 750 miles long, capable of transmitting 3,500 megawatts (MW) of wind energy to points east, south and perhaps north of the terminus. Clean Line is considering proposing a similar project to take wind energy from southwestern Kansas and across Missouri for delivery to points north and northeast of its terminus. Other project(s) are reportedly being considered for submission to WAPA.

SPRA has concerns in general about implementation of Section 1222, and specifically about the proposed Plains and Eastern project. Of specific concern is the protection of SPRA's federal power customers from any and all liabilities arising from the planning, design, construction, operation, maintenance, and/or ownership of Section 1222 projects. Other concerns include the demonstrated need for any proposed project and that such projects promote interconnection of the grid in which they are located.

The SPRA Board of Directors adopted a position on these issues that includes the following elements:

- SWPA's original authority to construct transmission facilities is limited by Section 5 of the Flood Control Act of 1944 to "only such ... facilities as may be necessary in order to make the energy and power generated at ... [Corps] projects available" to its wholesale customers. SPRA is concerned about extending SWPA's authority to construct transmission facilities beyond this original mandate.
- If Section 1222 of the Energy Policy Act of 2005 is invoked, SWPA's hydropower customers should be held harmless by the United States from any liabilities, costs/ and or expenses, financial or legal, stemming from the purchase of right-of-way, ownership, operation, construction, maintenance or otherwise of any facilities constructed under the authority of Section 1222.
- SWPA's customers should have the right to inspect any agreements between the Department of Energy, SWPA and/or any third party involving implementation of Section 1222 to ensure to their satisfaction that the indemnification of preference customers satisfies the requirements stated above.

- New electric transmission lines – regardless of who builds them – should fill a demonstrated need and should strengthen and support the existing AC bulk power transmission system.
- While new transmission projects may enhance the ability to send electric energy from one area over long distances to another area, they should also provide benefits to electric consumers along their routes and promote interconnection of the grid in which they are located.
- Any agreement to provide assistance as authorized by Section 1222 should comply in full and in all aspects with the authorizing legislation of the Energy Policy Act of 2005 and all provisions of applicable Federal Register Notices prior to execution of any agreements between DOE, SWPA and/or a third party calling upon DOE or SWPA to exercise federal powers of eminent domain to acquire rights-of-way for the proposed project(s).

Clean Line has expressed a willingness to work with SPRA to identify contractual and other methods (such as purchase of insurance) to prevent hydropower customer liabilities as described above. We continue to work with Clean Line representatives in achieving this objective. However, it should be noted that it is virtually impossible to identify all potential liabilities and indemnify the hydropower customers from these liabilities. It also should be recognized that even the best-written contract could be abrogated in whole or in part in the event of a bankruptcy.

Mission Creep

Finally, a friend of mine often says that one of the smartest things Congress ever did was to direct that the headquarters of the PMAs be located in the regions they serve, not in Washington. This policy was set forth in the Department of Energy Organization Act of 1977, which separated the power marketing functions from the Bureau of Reclamation and vested them in the newly formed Western Area Power Administration, to be headquartered within its marketing area.

From a customer's perspective, it seems like there is much more DOE Headquarters involvement in the day-to-day activities of the PMAs – activities that should be reserved to the Administrator. It is difficult to measure this involvement. Perhaps we should consider a few examples.

First, there is former Secretary Chu's Memo of last spring that set forth a host of new activities and responsibilities the PMAs should consider, from improving grid access for renewable energies other than hydropower, to incentives to PMA customers to install electric vehicle charging stations. I attended a couple of the WAPA public meetings and workshops on this proposal. We could talk all day about the specifics of the proposal, and in some cases the lack thereof. Regardless of what one might think about the wisdom or folly of each tenet, it could be said that elements in the proposal certainly represented mission creep for the PMAs. This is not to say that the PMAs should be hide-bound. But personally, I worry that foisting a lot of new duties and responsibilities on the PMAs might take their focus away from their original, and

what should remain their primary, mission – the sale of federal hydropower to consumer-owned, not-for-profit electric utilities at the lowest possible cost consistent with sound business principles.

Then there was the proposal made from Headquarters last year to establish a PMA Lead Advisor – a PMA “czar”, if you will. All PMA Administrators would report to the Lead Advisor, who in turn would report to the Secretary and Deputy Secretary of Energy. Under the current regime, Administrators report directly to the Deputy Secretary. To federal power customers it would appear that this proposal simply adds another layer of bureaucracy between the customers and the Secretary of Energy. I understand that, because of sequestration and limits on DOE hiring, this position remains unfilled. I don’t think we’re any the worse off for that fact.

Conclusion

Mr. Chairman, it has been an honor to be among those chosen to testify before the Subcommittee today on a ratepayer’s perspective of the PMAs. Telling this distinguished group how important the federal power program is like carrying coals to Newcastle. I thank you for the opportunity, and I appreciate your consideration. I would be happy to answer any question you might have.