

# PICK-SLOAN PROJECT

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OVERSIGHT HEARING  
BEFORE THE  
SUBCOMMITTEE ON WATER  
AND POWER RESOURCES  
OF THE  
COMMITTEE ON RESOURCES  
HOUSE OF REPRESENTATIVES  
ONE HUNDRED FOURTH CONGRESS  
SECOND SESSION  
ON  
**PICK-SLOAN PROJECT REPAYMENT ISSUES**

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MAY 2, 1996—WASHINGTON, DC  
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**Serial No. 104-74**  
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Printed for the use of the Committee on Resources



U.S. GOVERNMENT PRINTING OFFICE

WASHINGTON : 1996

25-483cc

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For sale by the U.S. Government Printing Office  
Superintendent of Documents, Congressional Sales Office, Washington, DC 20402

ISBN 0-16-052957-3

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# PICK-SLOAN PROJECT REPAYMENT ISSUES

THURSDAY, MAY 2, 1996

HOUSE OF REPRESENTATIVES,  
SUBCOMMITTEE ON WATER AND POWER RESOURCES,  
COMMITTEE ON RESOURCES,  
*Washington, DC.*

The Subcommittee met, pursuant to call, at 10:07 a.m., in room 1334, Longworth House Office Building, Hon. John T. Doolittle (Chairman of the Subcommittee) presiding.

## **STATEMENT OF HON. JOHN T. DOOLITTLE, A U.S. REPRESENTATIVE FROM CALIFORNIA; AND CHAIRMAN, SUBCOMMITTEE ON WATER AND POWER RESOURCES**

Mr. DOOLITTLE. The Subcommittee on Water and Power Resources will come to order. The Subcommittee is meeting today to hold an oversight hearing on the Pick-Sloan Project Repayment Issues. I want to welcome each of the witnesses testifying here today on issues relating to the repayment cost allocations for the Pick-Sloan Missouri Basin Program.

This is not a new issue, although it has received considerably more national attention since it was publicly brought to light last fall. It turns out that there are longstanding concerns that certain repayment costs are not being recouped because they have been allocated to irrigation features of the program that will never be built. Last December, I asked the General Accounting Office to examine the cost allocations of the Pick-Sloan Program, and I look forward to hearing their findings today.

The Pick-Sloan Missouri Basin Program was originally authorized under the Flood Control Act of 1944. Prior to that, in 1939, Congress asked the Bureau of Reclamation to provide a plan of relief for the drought-plagued lands of the region. Four years later, motivated by devastating floods, the House Committee on Flood Control asked the Corps of Engineers to produce a plan for "flood control and other purposes" in the Missouri Basin.

Reclamation and the Corps each prepared plans for management of the Missouri River Basin. However, because of the different missions of the two agencies, they took a different approach to basinwide management. When Congress authorized the resulting Missouri River Basin Program as part of the Flood Control Act of 1944, it quickly grafted the two plans together. As a result, implementation of the program has been difficult.

While the thrust of this hearing is Western Area Power Administration's power rates in the region, these power rates directly relate to the underlying cost repayment allocations. According to the

GAO, approximately 25 percent of the repayment for the project was to come from the scores of irrigation projects that were proposed as part of the plan.

Although the Federal Government proposed these irrigation projects to offset the loss of the hundreds of thousands of acres that were flooded by the water storage reservoirs, it has simply proven infeasible to construct most of these irrigation projects.

Therefore, in the intervening 50 years, only about one-fourth of the acreage planned for irrigation has been developed. Consequently, irrigation remains a small beneficiary of the program, and most of the irrigation services never went "on line" to begin repaying "their" share of the Federal investment.

However, the cost allocations for the Pick-Sloan Program are based on the "ultimate development" concept. In other words, cost repayment allocations were based on the benefits each class of beneficiaries could be expected to receive when all the individual projects were completed. Approximately \$454 million of the Federal investment in the Pick-Sloan Program's hydropower facilities and water storage reservoirs is unrecoverable unless the project repayment allocations are revised.

While the Bureau of Reclamation and the Western Area Power Administration cannot unilaterally reallocate power costs, I am concerned that the Bureau of Reclamation has failed to follow through on commitments the agency made in response to a 1993 Inspector General's report on Pick-Sloan Program cost allocations. At that time, Reclamation agreed to submit several study proposals on this issue to the Congress by early 1995 but has not yet done so.

There have been attempts to resolve this issue in the past. The Congress addressed this problem in part under the provisions of the Garrison Unit Reformulation Act of 1986, which deauthorized certain irrigation features of the Pick-Sloan Program, and allowed a reallocation of costs associated with these features.

This resulted in \$147 million being reallocated to power users for repayment. It is my understanding that, according to the WAPA officials, the power rate was not appreciably affected by this reallocation.

In closing, let me reiterate that I look forward to the testimony of each of our witnesses. It is a complex issue. The Federal Government is out of pocket nearly half a billion dollars, and this sum is being added to at the rate of \$30 million each year. It is important that we thoroughly examine the allocation of costs to ensure that the Federal investment in these Pick-Sloan facilities is recouped in an equitable manner.

Mr. DOOLITTLE. Mr. Johnson, we welcome you, and at this point, you would be serving the role of the ranking member. Would you care to make a statement?

**STATEMENT OF HON. TIM JOHNSON, A U.S. REPRESENTATIVE  
FROM SOUTH DAKOTA**

Mr. JOHNSON. Well, thank you, Mr. Chairman, and I appreciate the courtesy on the part of the Chairman of permitting a member of the Committee but not a member of the Subcommittee to sit in on this hearing. I think the matters being taken up here are very

important. I look forward to the testimony of the witnesses. And I may submit a fuller statement for the record. Thank you, Mr. Chairman.

Mr. DOOLITTLE. Thank you. At this point, we will invite our first panel of witnesses to come forward, and if you would, remain standing for the oath. We have with us Victor Rezendes, Director of Energy, Resources and Science Issues, Resources, Community and Economic Development Division of the U.S. General Accounting Office; and Mr. James Shafer, Administrator of the Western Area Power Administration; and the Honorable Patricia J. Beneke, the Assistant Secretary for Water and Science, U.S. Department of the Interior. And, Ms. Beneke, you have someone accompanying you. Is that right?

Ms. BENEKE. Yes, Mr. Chairman, Neil Stessman who is the Regional Director for the Great Plains Region, Bureau of Reclamation.

Mr. DOOLITTLE. Great. Welcome, Mr. Stessman.

[Witnesses sworn.]

Mr. DOOLITTLE. Thank you. Let the record reflect that each answered in the affirmative. Please be seated. Ordinarily, we operate under the procedures of having the witnesses each take five minutes. I know you are all familiar with those lights. But I think in the sense the hearing really is centered around the GAO report, we are going to give Mr. Rezendes 10 minutes in which to make his presentation.

**STATEMENT OF VICTOR S. REZENDES, DIRECTOR, ENERGY, RESOURCES AND SCIENCE ISSUES, RESOURCES, COMMUNITY AND ECONOMIC DEVELOPMENT DIVISION, U.S. GENERAL ACCOUNTING OFFICE**

Mr. REZENDES. Thank you, Mr. Chairman. I will try to cover this in about 10 minutes. I was asked to give you some of the history and some of the information on cost and reimbursement. I will try to not make this a boring accounting presentation.

I basically have two points I want to leave you with today. The first is that under the current repayment criteria, approximately \$454 million of Federal investment in hydrofacilities and water storage reservoirs is unrecoverable because a portion of these completed facilities, which were intended for irrigation, are no longer considered feasible and will not be built. The second point I want to leave you with is changing that determination will require congressional action.

Let me go back now to a little bit of the history of the Pick-Sloan Program. As you know, that was a combination of two basic programs. Originally, the Sloan Program, which was put together by William Sloan, the Assistant Regional Director for the Bureau, basically involved irrigation projects in the Upper Missouri River Basin. The second part was put together by Colonel Lewis Pick, who is from the Corps Program, and that basically involved flood control and navigation issues in the Lower Missouri River Basin.

Obviously, to accomplish these multiple objectives, there were compromises. For example, some people, in exchange for having their land flooded permanently for such benefits as water and electricity production, hoped that they would get future irrigation

projects. To date, we have spent roughly about \$4.5 billion on this of which \$2.6 billion is reimbursable through power revenues.

Obviously, a program of that size can't all be built at the same time. These projects had to be phased in. Basically, deciding which ones were done first and which ones are still left to be done is the issue today. I believe Marc Reisner in his book, *Cadillac Desert*, captured it pretty well when he said that the Corps projects, which were basically the downriver flood control navigation, became the here-and-now projects, where the upper river irrigation projects became the then-and-later projects. And that is basically the issue we have today.

Pick-Sloan, as it was originally envisioned in 1944, has not been constructed completely. There are still projects that are out there that will not be built. Under the original plan, about a third of the generating capacity for electricity was designed to pump water for irrigation in these projects.

As things progressed, only about half of that electricity, roughly 15 percent of the capacity of Pick-Sloan, was planned to be used to irrigate the land. And that is because, as you mentioned, Mr. Chairman, only 25 percent of the acreage originally planned for irrigation has come on-line. For those irrigation facilities that have come on-line, I do want to mention that is roughly about I believe \$56 million that is scheduled for repayment and will be coming in.

I want to concentrate now a little bit about those projects that are not being built. The Bureau now considers all but one of 104 incomplete irrigation facilities to be infeasible and believes that these projects will not likely be constructed.

They used criteria years ago when they looked at these, and although they haven't been updated officially, the time-consuming effort to do that, they believe, would not change their original estimate which is that these projects aren't economically feasible today. As a result, we have \$454 million in these completed facilities that is basically deferred. The real question now is why is that a concern?

To understand that, I want to briefly talk about what is reimbursable and not reimbursable under the program. Under what is not reimbursable is flood control and navigation. Costs relating to, however, electricity production, transmission, municipal water, and industrial supplies, and irrigation are, in fact, reimbursable. And this is the problem we have here.

Roughly, we have built watersheds of a larger size than needed to produce electricity. We have excess electricity capacity to pump water to these irrigation projects that are not going to be built. That total investment, again, is \$454 million. Since these water projects aren't coming on-line, we have no irrigators out there who will come forward and pay this. So the real question is what do we do with those costs?

That is a congressional decision. As you know, there is currently legislation that precludes reallocation—the investment of these projects to another project—without congressional authorization. The 1977 DOE Reorganization Act precludes revision by the Bureau of cost allocations without prior congressional approval. In addition, the Water Resource Development Act, as you mentioned, in 1986 requires them to proceed as if all projects will be completed.

You also mentioned, and I want to highlight just briefly, that there is precedence for moving these costs. The Garrison Diversion Unit Reformulation Act of 1986 did just that. At that time, Congress terminated the development of over 800,000 acres of irrigation and shifted the \$147 million costs associated with that to repayment through power revenues.

In our discussions with Western, we were told that basically it did not have an appreciable impact on the rate because, as you know, those rates are set to recover those costs over a 50-year period, which is a very long period of time.

I want to get back now to the \$454 million and talk about what effect that would have if that were shifted to electricity. I want to emphasize, and I can't emphasize this enough, that assessing these rate impacts is very speculative. And there are a number of factors that need to be considered, and I will go through those in a little bit.

But assuming that we use the same criteria that we had previously, which is that we allocate these to power and those are spread over 50 years with interest, we were told by Western that they ran some calculations for us, and they estimate that if the total cost were passed through to the wholesale rate that that would increase the wholesale rate roughly 14.6 percent.

I want to emphasize again though that there are a number of factors that could impact on that. Western is currently going through a restructuring. If there are cost savings that they could achieve through that restructuring, that could, obviously, impact any rate increase. There are also questions about whether, even if, in fact, the wholesale rate did go up whether that would translate into a comparable or equal rate or any rate impact at all at the retail level.

Other things could happen. These rates could be phased in over time, and they could also be—as you know, if there was ever a general reassessment of the costs and benefits of the program, that could totally change the allocation of these costs.

You also mentioned that in 1993 the IG had similar conclusions and recommended that the Department, in essence, request that Congress deobligate these projects and those costs be passed on to the electricity consumers. We will let the Department speak for that themselves, but currently, although they originally agreed with those recommendations and said they would have a list by 1995. They are still working on it and still assessing some of the options.

I want to get back to one last point that I want to emphasize here. While it is certainly within the congressional prerogative to move these costs to power, I do want to mention one point which is basically that in 1944 when these projects were put together, there were agreements reached.

As I mentioned, some people accepted flooding for benefits such as electricity or other things in the hopes of getting irrigation. If Congress deobligates these projects, there is an equity question that you may have to revisit in terms of those participants who aren't getting what they originally thought they were getting in the deal in 1944. With that, Mr. Chairman, I would be happy to answer any questions.

[Statement of Mr. Rezendes may be found at end of hearing.]

Mr. DOOLITTLE. Thank you. We will recognize Mr. Shafer for his testimony.

**STATEMENT OF J.M. SHAFER, ADMINISTRATOR, WESTERN AREA POWER ADMINISTRATION, U.S. DEPARTMENT OF ENERGY**

Mr. SHAFER. Thank you, Mr. Chairman. I appreciate the opportunity to appear before you today to discuss Western's role in the Pick-Sloan Missouri Basin Program. I have submitted my written testimony for the record so I will limit my comments to a few of the highlights.

As mentioned, the Pick-Sloan Missouri Basin Program was authorized in Section 9 of the 1944 Flood Control Act as a multipurpose ultimate development project. Western's role in this multipurpose program was defined in the Department of Energy Organization Act of 1977. This Act authorized Western to market the power generated by the Federal resources at rates adequate to recover the costs assigned to the power function for repayment.

In the Pick-Sloan Program that includes the power-related costs plus irrigation-related costs as determined by the U.S. Bureau of Reclamation that were deemed to be beyond the irrigators' ability to repay. The DOE Act also directed that no changes in the cost allocation or project evaluation standards could be made without congressional action.

The ultimate development concept has been an element of the program that has been questioned and reviewed in eight investigation reports that I am aware of since 1968. And each of those investigation reports has reaffirmed Congress's intent that the ultimate development concept be used in suballocation of power costs. Legislation subsequent to the 1944 Flood Control Act has ratified the concept as well.

Western's program and financial status is reported to Congress annually, and included in that report is a verification from an independent auditor confirming the compliance of the accounting processes in accordance with generally accepted accounting principles.

All of the power that is generated by the Pick-Sloan Program that is in excess of the present pumping needs is marketed at cost-based rates to assure repayment of Federal investment within the scheduled timeframe. Power identified as ultimately being used for irrigation purposes on projects as they are developed is marketed on a withdrawable basis at the same rate as all other power.

The repayment of the Pick-Sloan Program investment assigned to the power function repayment is on track to be paid in the timeframe as defined by law. And at present, Western's power repayment study indicate that approximately 43 percent of the Pick-Sloan power investment—excluding irrigation aid—has been repaid. The unpaid balance at the end of fiscal year 1995 carried an effective interest rate of approximately six and a half percent. That concludes my statement, and I will be pleased to answer any questions that you might have.

[Statement of Mr. Shafer may be found at end of hearing.]

Mr. DOOLITTLE. Thank you very much. The Chair recognizes Ms. Beneke, the Assistant Secretary, for her testimony.

**STATEMENT OF THE HONORABLE PATRICIA J. BENEKE, ASSISTANT SECRETARY FOR WATER AND SCIENCE, U.S. DEPARTMENT OF THE INTERIOR; ACCOMPANIED BY NEIL STESSMAN, REGIONAL DIRECTOR, BUREAU OF RECLAMATION, U.S. DEPARTMENT OF THE INTERIOR**

Ms. BENEKE. Mr. Chairman, members of the Subcommittee, it is a pleasure to be here today. I appreciate the opportunity to discuss the status of irrigation projects authorized as part of the Pick-Sloan Missouri Basin Program, as well as the repayment relating to Pick-Sloan facilities.

The Flood Control Act of 1944 envisioned a comprehensive plan to manage the water and power resources of the Missouri River Basin. The original program was to include an extensive system of flood control, navigation improvement, irrigation, municipal and industrial water supply, and hydroelectric power generation facilities for the 10 Missouri River Basin states.

At the time, this program was seen as a significant effort to boost the economy and population of the Great Plains which had suffered a decline during the Dust Bowl era of the 1930's and during World War II. It was hoped that the Pick-Sloan Program would provide economic stability and hydropower for a growing nation and contribute important flood control, navigation, and irrigation benefits.

The 1944 Act was based on preliminary plans and estimates. Congress recognized that some elements of the program would change as further investigations were completed. In reality, we now know that the original plan overestimated irrigation and navigation development and underestimated hydropower and recreation.

While Pick-Sloan has not been fully constructed, the program has provided significant benefits such as water supply, flood control, navigation, recreation, and hydropower. It has fallen short of its stated goals for irrigation.

Overall, only about 11 percent of the irrigation anticipated in the Pick-Sloan plan, less than 600,000 acres, has actually been federally developed. This is due to a combination of factors such as a limited growing season, market conditions, and soil characteristics.

In 1958, Reclamation and the Corps completed a report making cost allocations for multipurpose projects in Pick-Sloan. In 1964, the Congress adopted a law that required that all Federal facilities originally authorized to be built as part of the Pick-Sloan Program but which were not yet completed must be reauthorized by the Congress. Since June 30, 1964, nine facilities have been reauthorized, and construction activities have taken place on four of the projects. The others remain inactive.

We do not expect that the entire Pick-Sloan Program will be realized given current economic and financial conditions. Nonetheless, costs continue to be allocated to program purposes based on the assumptions that full program development will occur. Reclamation is prohibited by law from reallocating the costs of the Pick-Sloan Program without authorization from Congress.

In 1993, the Department of the Interior's Inspector General conducted an audit of the Pick-Sloan's cost allocations and repayment. The IG expressed concerns that the government's investment was not adequately protected under the cost allocations in Pick-Sloan.

In response to the IG, Reclamation is undertaking an in-depth review of program costs based on currently planned development, contemporary uses, and applying currently used project evaluation and economic analysis. We intend to keep the Subcommittee apprised of our findings and to seek guidance from the Congress and legislative authority as appropriate. This concludes my statement, and I would be happy to answer any questions.

[Statement of Ms. Beneke may be found at end of hearing.]

Mr. DOOLITTLE. Thank you very much. Now, the Bureau of Reclamation promised this Committee that study that was due in February of 1995. When do you expect we will have that?

Ms. BENEKE. Well, Mr. Chairman, we are continuing to work on the study. As soon as the IG completed its work on this matter, the Bureau engaged in the study. We committed at that time to taking an active role in analyzing this issue. We have been doing that.

If I recall correctly, our commitment was to provide a study proposal for the fiscal year '96 budget. That did not happen for a variety of reasons. I guess one of the reasons that I have been advised that it didn't happen was that there was some sentiment that we should defer working on this while the PMA legislative proposals were pending up here, because that could potentially so change the complexion of our analysis that it would be prudent to hold off for a bit. So the Bureau did hold off, but now we are actively engaged, and we fully intend to keep you apprised of our progress.

Mr. DOOLITTLE. Do you have in mind how many weeks will elapse before we receive this?

Ms. BENEKE. I do not have a specific deadline to give you or date to give you here today. I have been around long enough to know better than to do that. But I am hopeful that we will be able to share some additional information with you soon.

We have, of course, already provided preliminary information on irrigation projects that under our current analysis appear to be infeasible. That was provided to the Subcommittee. It was also provided to GAO. That was part of what we said that we would do in response to the IG report.

Mr. DOOLITTLE. Do you concur that we would be talking weeks as opposed to months, though, for this report to come in?

Ms. BENEKE. You know, I don't know the answer to that. It is, again, a very complex subject area. There are a lot of considerations to be made in the course of this analysis. One of those considerations is equity, as the witness from GAO mentioned. There are considerations with respect to impacts on power costs, but we are working on it and will continue to do so. And we will do our best to be responsive to the Subcommittee.

Mr. DOOLITTLE. Well, Madam Secretary, I would feel more comfortable if I heard a specific date since your agencies have been working on this since the Inspector General's report came out in 1993.

Let me say I think your recommendations would be very helpful to us and should precede whatever we do on PMA reform rather than be deferred while waiting for us. I think, frankly, the insight that would come from your recommendations would be helpful to us.

Ms. BENEKE. Well, let me say that, of course, this needs to be an interagency activity. We need to work closely with Western in this analysis and also closely with the Corps. I would be happy to confer with those other agencies and with the team that has been working on this at Interior and try to get back to you with a more specific timeframe.

Mr. DOOLITTLE. I would appreciate that. Maybe you can give us a status report.

Ms. BENEKE. Yes.

Mr. DOOLITTLE. I think this is an important submission to be made; it is a fairly high priority, and I would appreciate your getting back to us on it.

Ms. BENEKE. We will do our best to do that, sir.

Mr. DOOLITTLE. Thank you. Mr. Rezendes, thank you for your excellent report which has been very helpful to the Subcommittee. What actions do you think are going to be needed to recover the \$454 million that the GAO referred to as "unrecoverable," plus the annual \$30 million that will be added to that sum each year?

Mr. REZENDES. In essence, if you want to recover that money, particularly through power rates, which is the most likely suspect here, Congress will have to act as they did in the Garrison Diversion Unit Act which is basically shifting those power costs over.

You have a couple of options there. You could either deobligate the authorized projects, recognize that and shift the costs, or Congress could, as it has on other occasions, just shift the cost and not deobligate the projects. Or a third option is Congress could decide that those costs should not go to power and basically absorb them themselves. We have done all three, I guess, in the past in various forms and various other issues.

Mr. DOOLITTLE. Mr. Shafer, your auditors, Peat Marwick, raised the issue of the meters not being calibrated. I guess these are the meters that you use to dispense power out to your customers. You have stipulated you agree with the idea that they should be calibrated on an annual basis. Let me ask you, how many meters are there, and are they all in that situation of not being calibrated on an annual basis?

Mr. SHAFER. Mr. Chairman, we have a maintenance policy that we do routinely calibrate our revenue meters. I am not aware of the specifics that you are talking about as far as that report. We do routinely calibrate those meters. We have approximately 300 customers in the Pick-Sloan Program region. I am not sure that is exactly the same number of meters but in that neighborhood I would say.

Mr. DOOLITTLE. So approximately how many meters do you think there are?

Mr. SHAFER. I am guessing in relation to the number of customers about 300 meters also.

Mr. DOOLITTLE. OK. So each customer has its own meter, you mean?

Mr. SHAFER. Conceivably, they could have, yes. It depends on—there are some that are metered through joint action agencies, but some do have their own.

Mr. DOOLITTLE. I am looking at the KPMG Peat Marwick independent auditors report on the internal control structure, which is

dated September 30, 1995 and 1994. It says that under timely calibration of meters, "We commented in the report on the internal control structure of fiscal year '94 that Western should enforce the requirement to calibrate all meters at least once a year.

"Management concurred with the audit recommendation and stated that the Loveland Area Office would review the schedule for meter testing and recalibration to ensure requirements are enforced timely. Limited testing of 14 meter records at LAO showed that LAO had not calibrated four meters," and they list the meter numbers here, "since 1993.

"LAO stated that operating and maintenance personnel lack sufficient time because of recent downsizing of the higher priority work to calibrate all meters annually. The lack of annual meter calibrations exposed Western to potential incorrect metering of electrical power charge to customers."

Maybe I can ask in the next panel what a private company would do, but calibration is really how you tell if you are charging customers the correct amount, isn't it? Right?

Mr. SHAFER. Absolutely. And I don't disagree that calibration should be there, and I will certainly follow up to see if that has been corrected. We do have a policy in place that we test our revenue meters on an annual basis.

Mr. DOOLITTLE. We have two Peat Marwick reports here. Apparently this has been recommended for three years running, and still they are finding four out of 14—a little less than a third, but still a substantial percentage—of meters that aren't calibrated. So if this problem has gone on for three years running, why do you believe that it has been fixed?

Mr. SHAFER. I guess what their report is saying is that they hadn't been tested—whether they would test bad or not would be a question. But I will certainly follow up to see it is being taken care of at this point.

[The following was submitted:]

## NORTH DAKOTA POPULATION NOT SERVED BY FIRM PMA POWER

According to Electric Sales and Revenue 1994 (Energy Information Administration, U.S. Department of Energy, November 1995), 38 electric Utilities Serve Residential consumers in the State of North Dakota.

The following table breaks out these utilities by class of ownership and number of residential consumers:

Class of ownership	Number of utilities	Number of residential consumers
Cooperatives .....	24	92,263 (34%)
Investor-Owned .....	3	170,449 (63%)
Publicly Owned .....	11	8,864 (3%)
Total .....	38	272,574

If it is assumed that all cooperatives and publicly owned utilities purchase firm PMA power, and none of the investor-owned utilities do, then 63 percent of North Dakota residential consumers did not have access to firm PMA power in 1994.

Mr. DOOLITTLE. OK. Well, my time is up. Let me recognize the gentleman from South Dakota, Mr. Johnson.

Mr. JOHNSON. Well, thank you, Mr. Chairman. There is no new news that a great deal of the irrigation projects envisioned by Pick-Sloan have never come about, and that consumers of the region in lieu of the development of their economies have had the utilization of the hydropower in the interim. I would ask Mr. Shafer, do any Pick-Sloan customers get free power as a result of the current suballocation? Could you elaborate on that for us please?

Mr. SHAFER. Yes, I can. Thank you, Congressman Johnson. No. From our perspective, there is no free power. All the power that is marketed is sold at rates that we determine are adequate to recover the investment assigned to power for repayment. On a long-term basis, when we have surplus power during good water years in excess of what our firm contractual commitments are, that surplus power is sold on the surplus market at market rates at the time.

Mr. JOHNSON. And are the Pick-Sloan repayment rates in violation of the law because they do not recover all costs?

Mr. SHAFER. No. Our rate and repayment studies assure that all of the costs that are assigned to power for repayment are recovered, and that the timeframe is such that it will be paid off in the time specified by law.

Mr. JOHNSON. And could you tell us what the weighted interest rate is for unpaid Pick-Sloan power investment?

Mr. SHAFER. At the end of fiscal year '95, the effective interest rate on the unpaid power investment was about six and a half percent.

Mr. JOHNSON. I appreciate your response to that. Just quickly in my time here to Mr. Rezendes, on January 18 of this year, 40 of my colleagues and I sent the GAO a letter requesting an assessment of the impacts of higher electric rates on customers and local economies of WAPA, SEPA, and Southwestern Power, plus the possible impacts on navigation, flood control, recreation, and other multipurpose functions if the present ownership and operations are changed.

We also requested recommendations of how the PMA's can improve efficiencies in output within the present ownership position. Could you tell us when the GAO will be able to respond to this request and when we can expect something in writing from the GAO?

Mr. REZENDES. Yes. We were working with the staffs of the 40 some Members who have requested the study. Right now, we are in what we call the methodology development and scope and objective phase. We have agreed to get back to your staffs and the other members by June to reach agreement on a methodology and a scope of what we plan to do with a specific timeframe. I don't have a specific timeframe yet. I know everyone is anxious to hear information on this issue. So I would say realistically we are talking about anywhere from nine months or so from today, maybe a year.

Mr. JOHNSON. Well, thank you. We will await that with some anticipation. And with that, Mr. Chairman, I yield back my time.

Mr. DOOLITTLE. Thank you. Mr. Pombo is recognized.

Mr. POMBO. Thank you. Ms. Beneke, in your opening statement you said that the allocation of irrigation was obviously overstated when this was put together from the beginning, but that from power and recreation and other uses that it had been understated. If we were to reallocate the cost of all of this, how much would go to not just power but to the recreation and multiuse side of this?

Ms. BENEKE. Well, it is difficult for me to give you any specific number without the Bureau going through the actual cost reallocation process. They have a very detailed analysis that is undertaken to allocate those costs. But it is safe to assume that, you know, a substantial share of the costs would be reallocated to the power side.

And I think some of the costs may well also be reallocated to recreation uses because in 1944, when the Congress was putting the program together, they assumed a much larger share of the program would go toward irrigation. And history has proven that not to be the case. Power I think is more than double what was originally anticipated. And irrigation—we have developed about 11 percent of what was originally anticipated in the program.

Mr. POMBO. Historically, we have not required flood control to repay?

Ms. BENEKE. Correct, as a matter of law.

Mr. POMBO. And in recreation, we have also—the Federal Government has eaten that portion of it?

Ms. BENEKE. Again, as a matter of law that generally is correct.

Mr. POMBO. If we are looking at reallocating this, should we not also look at the flood control and recreation benefits of a project like this and what, if any, repayment should come from those uses of these projects?

Ms. BENEKE. Well, that is certainly something that Congress would be free to do. It would be a great departure from longstanding policy and law, and I guess I am not really prepared to comment on the policy implications of that today.

Mr. POMBO. Now, we hear a lot about the power side of this and the irrigation side as to whether or not they are paying their fair share of the cost of these projects. But at the same time in many of these projects the recreational users use a lot of the resources of the Department of Interior, the Bureau of Reclamation. They do

on an ongoing basis cost a lot of money, and yet we don't even consider that, you know, when we figure this out as to what the real costs of carrying these projects are.

Ms. BENEKE. Well, there are substantial recreation benefits derived from almost all of our multipurpose projects. I believe there is a chart attached to my statement that is part of the record that quantifies some of those recreation benefits of the projects.

Mr. POMBO. Which chart is that?

Ms. BENEKE. It is attached to my statement.

Mr. POMBO. Is that this—

Ms. BENEKE. Yes. That may be the second chart. I think it is the second chart there.

Mr. POMBO. Now, when you have a dollar figure for regional benefits, what does that mean exactly?

Ms. BENEKE. I am going to let Mr. Stessman answer that because his staff was responsible for generating the figures.

Mr. STESSMAN. Actually, these figures were developed by the Corps of Engineers in connection with a NEPA compliance activity. And what it reflects is the estimate of the recreation benefits from Pick-Sloan reservoirs by states for the year 1994. In other words, it is an annual estimated benefit for recreation.

Mr. POMBO. Now, what do you mean by a benefit? Economic benefit to the area?

Mr. STESSMAN. Yes. It means economic benefit.

Mr. POMBO. So, for example, you have Montana here at \$10 million. The recreational benefits in Montana generate an additional \$10 million in income to all businesses in the State of Montana? Is that what you are—

Mr. STESSMAN. I think that is a fairly accurate sort of layman term for it, which is about as good as I can do too. But it is the—

Mr. POMBO. Well, I am a layman so that is—

Mr. STESSMAN. Sorry, Congressman. Economic benefit is the regionally experienced benefit that is received or reflected in Montana's economy from the recreational use of, in this case probably, Fort Peck Reservoir.

Mr. POMBO. Can you provide to us what this is based on—a more thorough report on how they came up with these numbers and what they actually mean?

Mr. STESSMAN. Yes, we could.

Mr. POMBO. I think that if we are going to go back into some of these agreements and begin to look at whether or not the costs were shared adequately, it would be also a good time to actually go in and see what benefits we are deriving from these projects as well.

I know from the projects in California many of them are extensively used for recreational uses, and at the same time that is an extremely high cost to the taxpayer to subsidize those recreational benefits. And I think that a full picture must be looked at if we are actually going to go back in and begin to look at these agreements again. Thank you, Mr. Chairman.

Mr. DOOLITTLE. Thank you. Mr. DeFazio is recognized.

Mr. DEFAZIO. Thank you, Mr. Chairman. I am sorry I missed the testimony. I was in another hearing with Secretary Peña. I guess sort of the crux of this is this so-called free power, and I just want

to get at this. My understanding is we have a proposal from Otter Tail to raise the rates to customers and increase revenues to the Federal Government in addition to taking a management fee.

Now, my question is if we wanted to—as I understand it, it would require an Act of Congress to reallocate costs and recover further costs, is that correct, in terms of these irrigation projects?

Ms. BENEKE. Yes. That is correct.

Mr. DEFAZIO. OK. So I don't know why we need Otter Tail if this is a great idea. Let me just put this forward. I mean, couldn't WAPA raise the rates and not charge us the \$10 million administration fee by \$100 million if we authorize that?

Mr. SHAFER. Yes. Whatever the law would provide for us to do we certainly can. We would apply that—

Mr. DEFAZIO. If Congress decided it was desirable to recoup some of the, you know, additional costs that are now unrecoverable because not as much irrigation occurred as was anticipated—more hydropower development—we could do that?

Mr. SHAFER. We certainly could.

Mr. DEFAZIO. OK. And it wouldn't cost you \$10 million to raise the rates to do that?

Mr. SHAFER. No, sir.

Mr. DEFAZIO. OK. I would like to ask the GAO—I have just had a chance to breeze through your report. I guess I am puzzled as to the allegation of free power, and I want to ask you, because you are a little more impartial than WAPA—obviously, they won't tell me the truth here—where is the free power? What free power are we talking about? Are we talking about this unallocated cost which Congress has prohibited—

Mr. REZENDES. Right.

Mr. DEFAZIO. [continuing]—from being recovered? Is that free power?

Mr. REZENDES. Yes.

Mr. DEFAZIO. Or are we talking about them actually giving away power to people?

Mr. REZENDES. Yes. We have been asked that question before, and from our perspective, there is no free power. In essence, Congress established a process of allocating costs and recovering costs that were to be covered by electricity rates. And a message I want to leave here is that everybody is acting exactly as Congress told them to act.

These costs are being deferred, and I think there was an impression when I hear the connotation "free power" that Western is, in fact, doing something outside the law or outside the realm of what they should be doing—something nefarious here. Really, everyone is acting exactly as the law provided them to act.

However, that doesn't mean though that there aren't \$454 million in deferred costs that are out there. And in the meantime, the benefits of that water are being used for production primarily of electricity, which, obviously, as that produces electricity, they sell that power. They sell it at the rates that they normally sell their other electricity for. So from the aspect of someone getting free electricity without paying a rate, no, that is not happening.

Mr. DEFAZIO. And WAPA, other than its outside power purchases to firm up load, does it pay for any other Federal power in

any different manner, I mean, in terms of whatever obligations there are that the Federal Government is required to be paid or repaid? I would address that to either—

Mr. SHAFER. No. Our rates for the Federal power, of course, are cost based. The revenues needed to reimburse for the Federal investment determine our rates. Some of that cost includes purchased power costs that we have to acquire during the year to firm up some of our contracts.

Mr. DEFAZIO. But basically, I mean, we could alter the terms of your other Federal projects or these Federal projects in such a way that it would require you to recapture more costs?

Mr. SHAFER. Yes, you could. Congress could do that.

Mr. DEFAZIO. But there is no issue of you getting some unique benefit from these projects because that power is free while you are paying for other power from other Federal projects in some different manner. You are not. It is whatever is required by law in terms of recapturing the Federal investment?

Mr. SHAFER. That is correct.

Mr. DEFAZIO. OK. So there is no inconsistency here?

Mr. SHAFER. That is correct.

Mr. DEFAZIO. Because, I read this, and it reads like something from, you know, the National Enquirer about aliens or something. I am shocked! Shocked! There is free power here. So I just wanted to make sure that I am not missing something really big because I don't want to end up on the front page of the Enquirer supporting you giving away free power when my constituents aren't getting it.

So that is what I mean. Mr. Johnson's constituents are getting it, and, I would support free power in my own district but not in his district. OK. I thank the gentleman. I look forward to further testimony from the next panel.

Mr. DOOLITTLE. Mr. Rezendes, I don't think anyone up here, or at least on our side, has used the term "free power." But is it not indeed the case that the law and the policy on this have produced an untoward result?

Mr. REZENDES. Correct. That is right.

Mr. DOOLITTLE. Because is it not indeed the case that there is a heavy subsidy to power users that was never intended as a result of not building out the irrigation projects that were contemplated when this original cost allocation was made in 1958?

Mr. REZENDES. To the tune of \$454 million. That is the thrust of my testimony, which is basically there were capacities built in the system for irrigation. Those costs were spent. That is money the Federal Government has already expended. The question is who is going to pay for that.

And, as you know, there are two basic issues here. Since the irrigation projects are not going to be complete, it is either the American taxpayer through the various tax codes and how we collect revenues who will pay for this, or it could be passed on to the generation of power and have the region recover these costs.

Mr. DOOLITTLE. And at present, who are paying for it? The taxpayers or the power users?

Mr. REZENDES. The taxpayer has already paid for this. I mean, the moneys have been expended. Those \$454 million are gone. The way it has basically happened, I guess the way to characterize this,

is we have paid the money already, and we have on our books sort of an accounts receivable, a hope of a future payment in the future sometime. And I guess the issue before this committee today is how realistic is that future accounts receivable? Is that money really going to come to pass?

Mr. DOOLITTLE. Let me ask which states have the largest share of the program's generating capacity?

Mr. REZENDES. Looking down my list here, the largest is certainly South Dakota. They have roughly about 1,800 megawatts of electricity. Next, Montana and North Dakota have roughly about 550. Those three are the big ones.

Mr. DOOLITTLE. OK. And, Mr. Shafer, in the Eastern Division where this power is generated in Montana and North and South Dakota, where is most of the firm power distributed?

Mr. SHAFER. I would have to provide that for the record because I don't have that in front of me. But we do have that information broken out according to state.

[The following was submitted:]

#### AUDIT FINDING ON METER CALIBRATION

The "Independent Auditors' Report on Internal Control Structure" prepared by KPMG Peat Marwick LLP, dated December 15, 1995, reported that limited testing of 14 meters' records of Western Area Power Administration's (Western's) Loveland Area Office found four meters that had not been calibrated since 1993, even though the stated policy in that Area Office is that all meters are to be calibrated at least once a year.

As of May, 1996, those four meters have now been calibrated.

A related policy issue Western is currently addressing is the appropriate time interval between meter calibrations. The Rocky Mountain Customer Service Region (formerly the Loveland Area Office) is conducting a cost/benefit study of meter calibration frequency. The results are expected by September, 1996. The Region will use the results of the study to make any necessary modifications to its current requirement for annual meter calibration. Preliminary results indicate that newer, solid-state meters maintain higher levels of accuracy than older, electromechanical meters; and this finding, if confirmed, may be incorporated into the revised meter calibration policy.

Mr. DOOLITTLE. It is my understanding, and maybe you can tell me if this rings true or not, that although most of this power is generated in Montana and North and South Dakota, it is, in fact, distributed to Minnesota, Iowa, and Nebraska?

Mr. SHAFER. That could be. The marketing area is defined as the Pick-Sloan marketing area and inclusive of the states you named, there are six states in that marketing area. The distribution is really in accordance with the location of the customers that are eligible as defined by preference law.

Mr. DOOLITTLE. It is my understanding that in North Dakota, for example, more than 80 percent of the population receives its power from nonPMA sources. Is that correct?

Mr. SHAFER. That could very well be.

Mr. DOOLITTLE. Maybe for the record you can—

Mr. SHAFER. Yes. I can supply that. We do have that broken down.

Mr. DOOLITTLE. [continuing]—clarify that answer. But let us assume for the sake of argument right now that that is correct.

Mr. SHAFER. OK.

[The following was submitted:]

PICK-SLOAN MISSOURI BASIN PROGRAM-EASTERN DIVISION FIRM SALES, ENERGY, REVENUE, AND CAPACITY  
BY STATE

	State	FY 95 data	Percent
<b>Iowa:</b>			
Energy Sales—kWh(000)		1,181,976	14
Power Revenues-\$		16,357,291	12
Capacity (kW)		260,385	10
<b>Minnesota:</b>			
Energy Sales—kWh(000)		2,064,953	24
Power Revenues-\$		28,242,790	21
Capacity (kW)		413,957	17
<b>Montana:</b>			
Energy Sales—kWh(000)		709,785	8
Power Revenues-\$		10,283,064	8
Capacity (kW)		154,227	17
<b>Nebraska:</b>			
Energy Sales—kWh(000)		1,798,396	21
Power Revenues-\$		33,642,726	25
Capacity (kW)		765,240	31
<b>North Dakota:</b>			
Energy Sales—kWh(000)		1,083,879	12
Power Revenues-\$		10,445,374	15
Capacity (kW)		441,047	18
<b>South Dakota:</b>			
Energy Sales—kWh(000)		1,885,782	21
Power Revenues-\$		26,308,211	19
Capacity (kW)		447,428	18
<b>Total:</b>			
Energy Sales—kWh(000)		8,694,771	100
Power Revenues-\$		135,279,456	100
Capacity (kW)		2,482,284	100

Mr. DOOLITTLE. So is it not indeed the case, that in North Dakota, they thought they were going to get these irrigation projects, and they didn't get them? But since 80 percent of their power is coming from nonPMA sources, aren't they carrying a huge burden as taxpayers paying for this subsidized power due to the misallocation?

Mr. SHAFER. Without actually knowing numbers, I wouldn't know if they were carrying an unfair burden. I think it is important to note that there is about \$300 million that is suballocated to power for repayment in this process that is zero interest bearing which I guess defines the perceived subsidy.

Mr. DOOLITTLE. If that is an accurate figure, and more than 80 percent of the population gets their power from nonPMA sources, that means they are not getting any of the benefit of this power, so the very people in the area are indeed burdened by this themselves?

Mr. SHAFER. They certainly are burdened to the proportion that the other taxpayers are.

Mr. DOOLITTLE. OK. Mr. DeFazio.

Mr. DEFazio. Thank you, Mr. Chairman. I guess I don't believe I have further questions for this panel. I would like to go back to the point I made originally which is WAPA is acting consistent under current Federal law in terms of the recapture of investment.

If a majority of the Congress and the President agree that it would be desirable to recapture additional investment or the so-called windfall, then we can put that mandate onto WAPA. WAPA

could raise the rates accordingly and do that without charging a 10 percent add-on for so-called administration. Is that correct?

Mr. SHAFER. That is correct.

Mr. DEFAZIO. OK. I just wanted to get that clear so, basically, the ball is in our court here in terms of what principles we want to apply to the repayment of this particular investment or other investments made by the Federal Government in these areas.

I mean, why does WAPA exist? I am wondering, why do we have Federal power in the West? What I thought was that there were a lot of rural areas that the IOU's didn't want to serve, and so in terms of rural electrification we decided since no one else would serve them, the government would. Was that sort of the basis of the history of this?

Mr. SHAFER. I think that is a very good explanation, Congressman. The fact is that there were areas in rural America that did not have the privilege of having some of the benefits that the urbanized communities had. And there were not enough incentives from a profit perspective to interest private companies to go out and supply power to rural areas.

So the Federal Government took that on as a societal responsibility and recognized that these projects that were being built for other reasons also had the benefit of hydropower that could certainly facilitate providing power benefits to rural America to bring them up to the living standards of other Americans.

So the Federal Government took on that responsibility and needed an agency, which initially, of course, was the Bureau of Reclamation in marketing that power to administer that program. And we fulfill that role at this time.

Mr. DEFAZIO. Have there been any defaults? Has the investment as made by the Federal Government, as required by Congress been amortized and recaptured? Have there been any defaults? I am not aware of any.

Mr. SHAFER. No. Right now our repayment studies are designed such that all the investment that has been made in accordance to law will be repaid in the timeframe specified by law.

Mr. DEFAZIO. OK. So if there is any problem here or any changes to be made, they all again come back to the Congress?

Mr. SHAFER. That is correct.

Mr. DEFAZIO. OK. Just one other thing on this metering. I had my meter checked once, not because I thought that the local utility was losing money, but because I thought that the meter was running excessively. Would it be possible that by neglecting to check these meters you are overcharging your customers?

Mr. SHAFER. That is a possibility. I have to say I think today's meters are extremely reliable. That doesn't mean we shouldn't check them on occasion. But, yes, it could go either direction.

Mr. DEFAZIO. Again, I thought there was a fair amount of reliability, but if there is a variance caused by whatever, a power surge or something that knocks it off kilter or somebody whatever—I don't know what knocks a meter off kilter—it could be either way?

Mr. SHAFER. It could slow the meter down.

Mr. DEFAZIO. So probably if we did a randomized sort of study, we would maybe come out even?

Mr. SHAFER. That is correct. That is possible.

Mr. DEFAZIO. OK. I think it would be desirable to service and check the meters regularly so that you don't undercharge some and overcharge others. But I don't think there is any tremendous amount of revenue at question here. Would you agree?

Mr. SHAFER. I would agree.

Mr. DEFAZIO. OK. Thank you.

Mr. DOOLITTLE. We will get to the meters in the second panel as well, but let me just say, I suspect that businesses that are in the business for profit pay a great deal of attention to these things.

And I think it is interesting that for three years it has been recommended that these meters be calibrated, and it hasn't been a high enough priority. Servicing the gates at Folsom Dam wasn't a high enough priority, and finally one ruptured, and we had a tremendous problem that is ongoing as a result of that.

Mr. Shafer, with this misallocation that you know about, why haven't you been calling that to our attention and urging that the projects be deauthorized and the costs reallocated? I mean, you are the expert in charge of this. What is going on here?

Mr. SHAFER. The misallocation you mean in the process as far as—

Mr. DOOLITTLE. The misallocation being that this whole Pick-Sloan multipurpose project is predicated upon irrigation projects that you, in fact, know will never be built.

Mr. SHAFER. OK. Yes. My understanding, Congressman, is that this has been looked at several times. In fact, if my recollection is right, there have been eight reports or investigations into the repayment and the allocation of costs since 1968 where it has been discussed and attention has been brought to the issue.

Mr. DOOLITTLE. Well, I am aware that over the years studies have been done of this and so forth—I think at least a couple of GAO reports and then an Inspector General's report. But you are really on the front end of all of this, dealing with the policies that Congress sets. I would like to encourage you to be reminding us of the need to change these assumptions when we know that they, in fact, are no longer valid. Otherwise, it is just an ongoing deficit that is being run up at the taxpayers' expense, isn't it?

Mr. SHAFER. I guess that is true. I think it is noteworthy that, again, we carry out our responsibilities in accordance with the law.

Mr. DOOLITTLE. And, I stipulate to that. There has been no allegation that what is happening here is unlawful. I think that is clear. But I think it is unwise. What do you think about that?

Mr. SHAFER. Unwise to—

Mr. DOOLITTLE. It is unwise, when we have over \$5 trillion of total national debt in an advanced post-modern society, that we have these kinds of black hole subsidies going on in 1996.

Mr. SHAFER. Yes. And I think that maybe this is one of many that we need to take a look at, and I look forward to working with the Bureau of Reclamation in looking at this. I think the original intent of Congress has been validated throughout these studies, and that there are some issues that definitely need to be looked at in the reallocation process.

It is not just a matter of assigning the cost that is not being recovered to power. I think there is an equity issue here that has to

be looked into, and Congress needs to be made aware of that so that they can use that in making their determination on how to address this issue.

Mr. DOOLITTLE. Well, before we make a determination, we would like to see these studies come forward from you folks. You are the experts. I mean, this was done in the Inspector General's report in 1993. This is three years later, and we still haven't seen these studies. So will you take it perhaps as more of an affirmative obligation to work with your counterparts in the Bureau there, both to please come forward, let us hear this year if we can of what—

Mr. SHAFER. We certainly stand ready to work with them very proactively.

Mr. DOOLITTLE. That would be good. We do want equity. It is just that you, in the front lines, will have a better perspective to recommend equity than just expecting the Congress on its own to come up with a solution. The Inspector General called for the Bureau to make a report, and we would like to have that report. We want to do what is equitable. We want to do what is right and fair and take all of these things into account, but we can't do it nearly as effectively without the recommendation. Now, let me ask in my limited time of Ms. Beneke, will you involve Mr. Shafer in this process?

Ms. BENEKE. Absolutely. We would be pleased to do that. In fact, we have already been consulting with Western on this subject, as well as with the Corps, I am advised, and will continue to do that and do our best to be responsive to the Subcommittee.

Mr. DOOLITTLE. Thank you. Mr. DeFazio is recognized for his questions.

Mr. DEFAZIO. Thank you, Mr. Chairman. I would just like to supplement the Chairman's line of inquiry and say in any cases where we do engage in such studies that we look at all users, you know.

And, for instance, if we were studying the bond-all system, I would expect we would study the irrigation uses and the tremendous subsidies which are extended there, both to the Federal Government, Bureau of Rec, and to the individual users.

We would study navigation subsidies. We would study flood benefits on all users. And I would assume in any case where one studies this, we won't just use it to launch an attack on public power, but we will look at any and all subsidies that exist.

For instance, I believe probably some—we could make a case some of the irrigation projects in California aren't being fully repaid to the Federal Government. So, I think that we just need to look at this in toto, and I am certain the Chairman would agree. So I thank you.

Mr. DOOLITTLE. OK. We thank our witnesses. We will probably have some additional questions and ask you to answer those as timely as you can. With that, we will excuse the members of the first panel and ask the members of the second panel to come forward. If the second panel members will remain standing for the oath, we have Mr. Ward Uggerud, Vice President for Operations of Otter Tail Power; Mr. Bruce Driver, Special Counsel, Land and Water Fund of the Rockies.

[Witnesses sworn.]

Mr. DOOLITTLE. Let the record show that each answered in the affirmative. Thank you very much. Please be seated. We are grateful to have you here as our witnesses, and you are familiar with the procedures. You heard it explained. Please try and confine your remarks to five minutes, and the lights will indicate. The yellow light goes on at the beginning of the fourth minute and the red light when the time is up. Mr. Uggerud, you are recognized for your testimony.

**STATEMENT OF WARD UGGERUD, VICE PRESIDENT FOR  
OPERATIONS, OTTER TAIL POWER**

Mr. UGGERUD. Thank you, Mr. Chairman and members of the committee, for inviting me here today, and I commend you for examining this important issue. My story today is one of astonishment. Last summer I received an invitation to a meeting of PMA customers to discuss strategies for opposing the privatization of the Federal Power Marketing Administrations. I was surprised I was invited there because Otter Tail strongly supports privatizing the PMA's.

The meeting was attended by about 150 people and included representatives of the National Rural Electric Cooperative Association and the American Public Power Association. In fact, Glen English and Alan Richardson were the primary presenters at the meeting.

Prior to this meeting, these groups had expressed absolute opposition to any type of privatization. Imagine my surprise then when I heard Richardson and English recommend switching strategies to offer to buy the PMA's for \$2.6 billion, a fraction of their market value. Fortunately, this plan was rejected by Congress.

The reason for this dramatic switch in strategies, however, was even more surprising. One participant, in explaining the urgency of making a quick purchase, suggested that a sale could put an end to the free power that the PMA customers received. Free power was their phrase, not mine.

The amount of the free power and its source were revealed in a study presented at that meeting. Irrigation projects, which have never been built, are the source of the free power, and the group was told that a sale could end that giveaway.

The study conducted by the PMA customers, which revealed and quantified this source of free power, is a part of the written material which I am submitting. At first I found the statement unbelievable, but after further investigation I found out it was true now that this abuse has been revealed and confirmed by the GAO.

The PMA customers are trying to put a new spin on it. They say that since the irrigation projects weren't built they should have this free power. They also say they pay the government on time and with interest. That is also not true. Numerous studies and audits say otherwise and point to the PMA's as being a raid on the Federal Treasury.

While water projects intended as a part of the Federal Power Program go unfunded, hundreds of towns continue to suffer because of floods and lack of water for irrigation, municipal, and industrial uses. The revenue lost in this free power giveaway would have been enough to complete many of those projects.

The PMA program was intended to help develop and sustain rural areas. Yet today, many PMA customers, the recipients of that free power, are shopping malls, country clubs, and posh resorts. If it were not for my accidental attendance at this meeting, this abuse of free power might never have been exposed.

The preference power customers might have been successful in purchasing the PMA's at a price that would have, in effect, continued this free power forever. In fact, that was their strategy. That was what they said. I am submitting a copy of my written notes of the meeting which confirm that this was their strategy.

The existence of free power has been obscured in archaic accounting standards and a campaign of misinformation by preference power customers. In fact, the financial records of WAPA, which are supposed to keep Congress and the U.S. taxpayers informed, make no mention of this free power. In spite of notice given by auditors year in and year out, nothing has changed in WAPA's accounting practices or rate treatment.

The PMA customers claim that they pay their own way and that they are entitled to perpetual Federal power. Their own studies and their own comments prove otherwise. The PMA customers are concerned about losing their subsidies, and they are especially concerned about losing their free power.

You only need to look at the record to see that the Federal Treasury is losing millions of dollars per year. Water projects go unfunded, and consequently rural and industrial development is sacrificed so that current PMA customers do not have to pay their true share of costs.

Thanks to the General Accounting Office and a misplaced invitation, the truth is out. And the truth is taxpayers are being defrauded while water projects go unfunded. I hope you are as astonished as I was. Thank you and I will be happy to answer your questions.

[Statement of Mr. Uggerud may be found at end of hearing.]

Mr. DOOLITTLE. Thank you. Mr. Driver, you are recognized for your testimony.

#### **STATEMENT OF BRUCE C. DRIVER, SPECIAL COUNSEL, LAND AND WATER FUND OF THE ROCKIES**

Mr. DRIVER. Thank you, Mr. Chairman. Good morning, Mr. Chairman, as well as members of the Subcommittee. I am Bruce Driver. Today I am speaking for the Land and Water Fund of the Rockies, Midwest Office of the Izaak Walton League of America, the Natural Resources Defense Council, and, finally, the National Wildlife Federation.

I have two topics to cover in my time with you today. First, I will talk a little bit about the Pick-Sloan Missouri Basin Project cost allocation issue. Then I want to spend a couple of minutes on a basic response to the Otter Tail Power Company's proposal to privatize the Eastern Division of the Pick-Sloan Missouri Basin Project.

With regard to the cost allocation issue, in the time that we had to prepare my testimony, we were unable to come up with a basic position with regard to whether Congress ought or ought not to reallocate the costs. However, we are concerned that should Congress decide to reallocate costs that the dollars somehow will be hijacked

in the region for unsound water projects like the original Garrison Diversion Project instead of flowing back to taxpayers who deserve that money.

Our concerns have been heightened by recent reports that there is going to be another run at some of these unsound water projects soon. In that regard, as I spell out in my testimony, the National Wildlife Federation reports that a Garrison Conservancy District proposal dated February 7, 1986, asks for \$800 million in Federal water and power funds to "finance irrigation projects to build what farmers had expected from the Federal Government over the past 51 years."

The proposal, the National Wildlife Federation indicates, requests even more; an additional \$400 million in Federal buy-out appropriations from Congress for a total of \$1.2 billion. With the Chair's permission, I would like to be able to supplement the record with some additional background documentation with regard to this new proposal that we have been hearing about.

With regard to the Otter Tail Power Company proposal, I have taken a hard look at it, and the people of the groups that I am representing today don't like it very much. In short, our key problem with it is that it proposes that one stakeholder among many of the Otter Tail Power Company take the lead in trying to privatize the Eastern Division resources.

That means that Otter Tail would be in a position to go out and raise the rates of potential competitors of Otter Tail over the next five years. That is a little bit like the fox in the henhouse because Otter Tail is beginning to have to compete with WAPA preference power utility customers right now. Within a few short years, they may actually be competing on a retail basis. If I were involved in the power business out there, I would love to have the opportunity to raise the rates of my competitors over the next five years.

Also, the Missouri Basin facilities that are used to generate power to be marketed by WAPA right now are actually multiple-use facilities. They provide water for navigation. They provide water for fish. They provide water to the tribes. There are lots of key stakeholders who need to be involved in any potential privatization.

It doesn't seem right to us that one electric utility—only one of many stakeholders in the region—gets to take the lead on this over the next five years. It is probably better that privatization be done by all of the stakeholders perhaps in a forum convened by the key Federal agencies.

Finally, there are a lot of key issues that the Otter Tail Power Company proposal does not address such as whether Otter Tail would or would not honor WAPA's integrated resource planning regulations, its rules with regard to contract extension.

All the Eastern Division contracts expire in the year 2000. Is Otter Tail asking for authority to ignore that particular regulation? I can't tell. I don't know. There is an awful lot that has not been spelled out. The basic fee arrangement is also pretty high too. I can see that the red light is on, and I will stop now. Thank you.

[Statement of Mr. Driver may be found at end of hearing.]

Mr. DOOLITTLE. Thank you. Mr. Uggerud, you are the Vice President for Operations of Otter Tail. Tell us about these meters. I

gather you make your money off the sale of power, so it must be fairly important that they be accurate. Obviously, if they are inaccurate, that could either be to your advantage or disadvantage. What is your experience with how often these meters are calibrated or should be calibrated?

Mr. UGGERUD. With regard to revenue meters, it is our requirement that on meters at the transfer level, at the bulk power level, which these are, that those have to be inspected at least annually. And I would agree with previous comments that meters can be recording either high or low, but I don't believe that from Otter Tail Power Company's perspective that is the issue—the possibility that it might net out. The issue is if it is a sound business practice to do so.

Mr. DOOLITTLE. Are you required by your public utilities commission to calibrate them every year? Is that simply something you do on your own?

Mr. UGGERUD. That is something that we do on our own. But as a general practice, many of our business practices are subject to audit and review by the Public Service Commissions. And though that one might not generate particular attention each and every year, I can assure you that in a given year that it drew attention that we would attend to it.

Mr. DOOLITTLE. OK. But, clearly, it is a sound business practice which is why I think the auditors of WAPA asked for it to be done. You have indicated that you have used the term free power although you didn't invent the term. The term was invented by the public power people, I presume.

By the way, for the record, I want to note that PMA customers were invited to testify today but were unable to be here. So we don't have the direct benefit of their opinions of these things. You indicated that you believe WAPA is delivering free power, and WAPA has testified that it is not, that it is acting according to law. Why do you believe that they are marketing free power?

Mr. UGGERUD. Well, because the power that is being sold, 17 percent or 16 percent—that range—of the costs are not being allocated to the product that is being sold. So by their own admission and by the PMA customers own admission, you have got a product that is being sold, and roughly 16–17 percent of the costs are not being assigned to the product. So a portion of every kilowatt hour that is being sold has got a free component in it.

Mr. DOOLITTLE. OK. One of the concerns that has been raised is that those power customers that would be affected by correcting the current misallocation of program repayment obligations are the same entities that have been affected by the failure to complete the proposed water projects. From your experience in the region, is this indeed the case?

Mr. UGGERUD. Well, the PMA customers have tried to make that a big part of their argument, but that is far from the truth. As was previously indicated in the previous panel, in North Dakota 80 percent of the customers do not receive Federal preference power. Yet, North Dakota and South Dakota were two of the states where the primary irrigation projects were intended to be.

There has also been mention that these projects were intended to go to rural customers and that there still are rural benefits. One

of Otter Tail's big points in this issue, Mr. Chairman, has been that there is no entitlement test whatsoever for Federal preference power.

There is no rural test. There is no means test. There is no entitlement test of any kind. Much of that power—in fact, 75 percent of it is going outside of the states of North Dakota and South Dakota to downstream states that receive the benefits of flood controls and the navigation and the recreation. And yet the states where the benefits were intended to be irrigation have not gotten that.

There are many very expensive residential complexes that are being developed that get free power, while there are poor people in neighborhoods right next door that do not. There is no entitlement. There is no means test.

Mr. DOOLITTLE. OK. Thank you. Mr. DeFazio is recognized.

Mr. DEFAZIO. Thank you, Mr. Chairman. Mr. Uggerud, I think part of what is going on here is clearly you represent an IOU, and we are involved in the age-old battle over public power, public preference, and the perceived benefits and that. And I understand that struggle, and that is fine.

But, I guess the question, having heard the earlier testimony—can you honestly say they may have used the word free power, but you understand that, in fact, there is no free power here. The question is how much of the Federal investment to recapture. Isn't that true? I mean, there is no free power.

Mr. UGGERUD. I think that I prefer the term free power. In fact, they said things at the meeting like this—

Mr. DEFAZIO. Well, you prefer it, but, I mean, you heard the GAO and you heard my questions and you realize that, in fact, it isn't that this power coming from these Federal projects is unique in any way.

It is given to WAPA unlike any other power from any other Federal project that goes to any other PMA so your problem is really with PMA's and their access to Federal power generally and all Federal power than it is with this particular project. Because you could certainly go to other PMA's and other projects and find out that they are not totally recapturing the cost because of mandates put on them by Congress.

Mr. UGGERUD. Well, 15 percent of the costs are not being assigned. That is free power. They called it a steal. You can put the term on it that you want.

Mr. DEFAZIO. Sure. Well, I am a little concerned by—again, and I don't think we are well served by hyperbole here. On page nine of your testimony, you talk about criminal implications. Would you care to elaborate on what the criminal things are that are occurring here? What is criminal other than we have public power?

Mr. UGGERUD. Well, I think that there are certain regulations with regard to what groups of business enterprises can get together and discuss. And certainly—

Mr. DEFAZIO. Do you have any allegations of improprieties, violations of existing Federal laws? If so, I think it would behoove you and your counsel to provide those allegations to the United States Attorney General.

Mr. UGGERUD. I think that that has been done.

Mr. DEFAZIO. OK. Well, we will look forward to the case. You know, on page five of your testimony, you talk about—I am really puzzled there. If you could refer to that at the top, you talk about the collapse of the economy in 1929.

I assume you are referring to the Insull empire and some other abuses done by private entities. And then you say that the PMA's aren't required to have these disclosures. Well, the PMA's, as I understand it, are governed by Congress since they are Federal entities and are given certain requirements by the Congress. And in the Chairman's wisdom or other Members of Congress's wisdom, we can expand those requirements.

But I am really puzzled as to what the relationship between the collapse of the Insull empire and the abuses of the private sector that occurred and brought about the requirements of the Security Exchange Commission and others—how that relates to public power?

Mr. UGGERUD. Well, I think we have heard in the previous panel that you had recommendations that were made back in 1993 with reports promised in January of 1995 that have not been forthcoming. It seems to me that the control—

Mr. DEFAZIO. Are we in some jeopardy of financial collapse or defrauding investors? That is what those laws were written to do. I mean—

Mr. UGGERUD. We are defrauding taxpayers.

Mr. DEFAZIO. Well, again, it is within the authority of this committee to change the repayment requirements, and only the Congress and the President can do that. And, we are airing that issue, and we can certainly decide to go further in terms of repayment requirements.

Tell me, in your management, have you assessed \$10 million of efficiencies? Basically, other than your jacking up the rates, how would you get your \$10 million fee? WAPA said if we order it, they can jack up the rates \$100 million and repay that to the Federal Treasury.

But, are we getting your services for free? Are there \$10 million of efficiencies and savings out there that you would get for us and that wouldn't go to your investors because, of course, part of all your earnings go to your investors?

Mr. UGGERUD. Well, first of all, Mr. DeFazio, there were \$100 million that we were returning to the Federal Treasury.

Mr. DEFAZIO. Right, and we can make WAPA do that by making them jack up the rates. OK. So what do we get for the \$10 million and how do you pay for it?

Mr. UGGERUD. How do we pay for the \$10 million? The \$10 million would be recovered as a part of the basic rate structure, and we have offered more than to just manage the PMA's. If you will take a detailed look at the proposal, we have offered to study in depth all of the PMA's, to take a look at what the customers are, take a look at the entitlements and the means test issues, and promise a thorough and detailed report to Congress at the end of five years.

Mr. DEFAZIO. Totally unbiased?

Mr. UGGERUD. Totally unbiased.

Mr. DEFAZIO. Totally unbiased.

Mr. UGGERUD. In fact, if you would like us to develop the outline of the requirements and have some independent accounting agency administer the test, we would be willing to do that. Nothing had been forthcoming with regard to changes in the status quo, and we thought it might be useful in this discussion if Otter Tail would come forward with a straightforward proposal, which doesn't take a rocket scientist—the rates are purely amortized—the remaining debt—the 30 years at eight percent.

That is how we get the rates. That is not jacking the rates up. That is applying sound business practices, and we thought it might be useful for the discussion for someone to come forward with an alternate proposal.

Mr. DEFAZIO. Well, I appreciate your public-spirited gesture, and we will certainly give it all due consideration.

Mr. UGGERUD. Thank you.

Mr. DEFAZIO. I think the Chairman is particularly interested. Thank you.

Mr. DOOLITTLE. Mrs. Chenoweth is recognized.

Mrs. CHENOWETH. Thank you, Mr. Chairman. I just have a couple of questions. Mr. Uggerud, I appreciate your testimony.

Mr. UGGERUD. Thank you.

Mrs. CHENOWETH. And I appreciate your bringing this to the attention of the Congress, and I think it is certainly a worthy problem that we should investigate and look at. Under FERC Section 211 authority reciprocity, is there any avenue that the FERC can govern in this case at all?

Mr. UGGERUD. I don't believe so. In fact, I think that Chair Mohler has perhaps testified, if not to this committee, to another committee of Congress. I have seen comments from Chair Mohler where she has said that really the Federal Energy Regulatory Commission is put in a position where they can only rubber stamp the rates as recommended by the PMA administrators. And I think that I have seen some things myself that indicate that their authority is to approve the rates but not to examine them.

Mrs. CHENOWETH. I see. Mr. Driver, I see that you represent not only the Izaak Walton League, but the Natural Resource Defense Council and the National Wildlife Federation. What is the National Wildlife Federation's stated position on the development of additional irrigation projects?

Mr. DRIVER. To be candid, I don't know actually what its stated position is. Its interest in this matter is, as I said earlier, to prevent money that if Congress decides to reallocate costs to power use, that money ought to come back to the Federal Treasury and not go to what the National Wildlife Federation believes are unsound water projects.

Mrs. CHENOWETH. Thank you. Thank you, Mr. Chairman.

Mr. DOOLITTLE. Thank you. Mr. Uggerud, Congress established a complex form of regulation over private electric utility companies because of their status as monopoly service providers. And, in addition, states have public utility commissions that oversee the private power industry.

You have looked into the cost allocation problem, and you have experience with the private power sector. In your experience, would this type of cost allocation problem be allowed to continue for this

long under FERC and the local PUC regulations that we have heard discussed here relative to the misallocation, the subject of this hearing?

Mr. UGGERUD. No, it would not, and there are two things that would prevent it. First of all, the commissions would prevent it. Secondly, our company would have gone broke and gone out of business long ago if we would have tried to do it that way.

Mr. Shafer indicated that the full costs are being allocated according to the law.

A couple of things that I would like to correct with regard to his answer at least from my observation. He indicated that the repayment schedule is resulting in an on-time repayment, but there was also testimony and comment made that that was supposed to be a 50-year period.

Now, the Pick-Sloan Project is 47 years old, and Mr. Shafer's testimony is that roughly two-thirds of that remains unpaid at the end of 47 years. I do not think that that is on time within the requirements of the Federal Flood Control Act of 1944.

Further, he indicated that the weighted average interest rate at the end of 1995 was roughly six percent. But Otter Tail's calculations show that over the 47 years of that project that the interest rate actually returned to the Federal Government has been 1.6 percent.

So I suggest that our commissions would have been deeply concerned about that practice. I think our outside auditors would have been deeply concerned about that. I think our board of directors would have been concerned about it, and I don't think our company would still be in business today if that is how we had operated.

Mr. DOOLITTLE. So is it your belief that no private company could ever operate in this fashion?

Mr. UGGERUD. Absolutely. And I think that in the Flood Control Act of 1944 there were concerns about how this would be operated. I think there is a paragraph in the authorizing legislation that says that sound business practices should be used to recover the repayments on time and with appropriate interest.

Mr. DOOLITTLE. Mr. Driver, you have been familiar with this problem. What do we do? What is your idea of how to address this misallocation problem?

Mr. DRIVER. You mean with regard to the cost reallocation?

Mr. DOOLITTLE. Yes, sir. Or did you consider that to be a problem?

Mr. DRIVER. I have to be careful here because I am actually speaking for four different groups, and we have not come up with a unified position with regard to what to do with this issue. But I can state the following: it is an important issue. Congress ought to be considering it, and at least one of the groups that I speak for I think would tend to favor Congress actually changing the power—the cost allocation rules in order to allow the Federal Treasury to recoup funds that are not now being recouped.

Mr. DOOLITTLE. Well, which group would that be?

Mr. DRIVER. Well, that would—I want to be careful here too because I am not exactly sure what their position is, but the National Wildlife Federation has always believed that it is inappropriate policy for the taxpayer to be overtly subsidizing power, and that

taxpayers may indeed be entitled to a little bit more revenue from power users.

Mr. DOOLITTLE. OK. Well, I think this has been a useful hearing. It is one of three that we will be having on this general subject matter. I would like to thank our witnesses on this panel for the trouble you have gone to to be here. We will have some other questions no doubt to ask you as well, and would ask you to please respond in a timely fashion when that happens. With that, the hearing is adjourned.

[Whereupon, at 11:40 a.m., the Subcommittee was adjourned; and the following was submitted for the record:]

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United States General Accounting Office

**GAO**

Testimony

Before the Subcommittee on Water and Power Resources,  
Committee on Resources, House of Representatives

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For Release on Delivery  
Expected at  
10 a.m. EDT  
May 2, 1996

## FEDERAL POWER

### Recovery of Federal Investment in Hydropower Facilities in the Pick-Sloan Program

Statement by Victor S. Rezendes,  
Director, Energy, Resources, and Science Issues,  
Resources, Community, and Economic  
Development Division



Mr. Chairman and Members of the Subcommittee:

Thank you for the opportunity to discuss the results of our work on the Department of Energy's (DOE) power marketing administrations. Our focus today is on the requirements under the Pick-Sloan Program for the Western Area Power Administration (Western) to repay the federal investment in the program's hydropower facilities. At your request, we reviewed the effect of policies under which repayment of a portion of the federal investment is deferred. Specifically, we are presenting information on (1) the amount of this investment that may not be recovered under the current repayment criteria and (2) potential actions for recovering the investment.

You also asked us to report on two related issues concerning the maintenance of federal hydropower facilities at the Department of Energy's Southeastern Power Administration and the accounting and ratemaking practices of the power marketing administrations. We will be reporting on these issues separately over the coming several months.

In summary, Mr. Chairman, our principal points about the Pick-Sloan Program are as follows:

- Under the current repayment criteria, approximately \$454 million of the federal investment in the Pick-Sloan Program's hydropower facilities and water storage

reservoirs is unrecoverable because a portion of these completed facilities were intended for use with irrigation facilities that have not been completed and are no longer considered feasible. In addition, as the overall federal investment in the other aspects of the completed hydropower facilities increases because of changes such as renovations and replacements, the amount of the federal investment that is unrecoverable will increase.

Changing the terms of repayment to recover any of the \$454 investment would require congressional action. Consistent with previous congressional action concerning the program, the Congress could direct Western to recover the investment through power revenues and to take action to minimize any impact on power rates. Estimating the potential impact on the rates of recovering the investment through power revenues is speculative and could vary significantly depending on, among other things, the terms of repayment and the amount Western passes on to its customers. Assuming that Western passes the entire amount on to its power customers, the wholesale power rate could increase by as much as 14.6 percent. Recognizing that the program incorporates agreements reached decades ago, any changes between the program's power and irrigation purposes may also necessitate reviewing other aspects of the agreements—specifically, the agreements involving areas that accepted permanent flooding from dams in anticipation of the construction of irrigation projects that are now not likely to be constructed.

## BACKGROUND

The Pick-Sloan Missouri Basin Program was authorized by the Flood Control Act of 1944 as a comprehensive plan to manage the water and hydropower resources of the Missouri River Basin.<sup>1</sup> The act was a combination of two plans: (1) the Sloan Plan, developed by the Department of the Interior's Bureau of Reclamation (Bureau) and designed primarily to irrigate lands in the Upper Missouri River Basin and (2) the Pick Plan, developed by the Department of the Army's Corps of Engineers (Corps) and designed primarily to control floods and provide for navigation on the Lower Missouri River Basin.

The program encompasses an extensive network of multipurpose projects that provide for, among other things, flood control, navigation, irrigation, municipal and industrial water supply, and power generation. (Fig. 1 shows the location of the program's hydropower generating facilities and the overall program area.) To accomplish these multiple purposes, the plan required compromise among the program's participants. For example, in exchange for having their land permanently flooded by dams to produce such benefits as electricity and flood control, some participants anticipated the construction of irrigation projects. The program is administered by three federal agencies: (1) the Bureau, which operates seven multipurpose projects and is responsible

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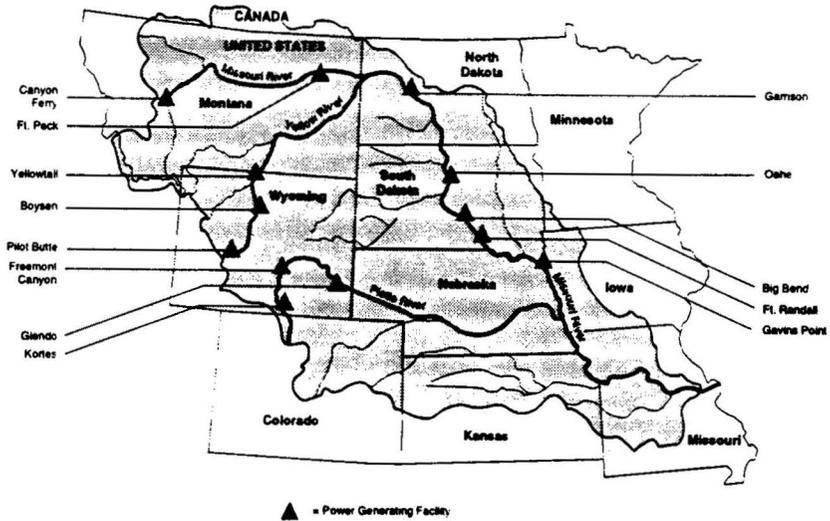
<sup>1</sup>The Pick-Sloan Missouri Basin Program encompasses those parts of Colorado, Iowa, Kansas, Minnesota, Missouri, Montana, Nebraska, North Dakota, South Dakota, and Wyoming from which water drains into the Missouri River.

for the water supply functions of the program's projects, (2) the Corps, which operates six multipurpose projects and administers the flood control and navigation aspects of the program's projects, and (3) Western, which markets the hydropower generated at the program's generating facilities and constructs, operates, and maintains the program's power transmission system.<sup>2</sup>

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<sup>2</sup>Our report Federal Electric Power: Operating and Financial Status of DOE's Power Marketing Administrations (GAO/RCED/AIMD-96-9FS, Oct. 13, 1995) provides additional information on Western and the other power marketing administrations.

Figure 1: Missouri River Basin, Showing Location of Pick-Sloan Program Hydropower Generating Facilities



Source: GAO's illustration based on information from the Bureau and Western.

The federal investment in the Pick-Sloan Program has nonreimbursable and reimbursable components. The nonreimbursable component consists of the capital costs of constructing, among other things, the program's flood control and navigation facilities. The reimbursable component consists of the capital costs of constructing the program's power generation and transmission, irrigation, and municipal and industrial water supply facilities. The reimbursable federal investment is further divided into investments repaid with interest (for power facilities and municipal and industrial water supply facilities) and investments repaid without interest (for irrigation facilities).<sup>3</sup> Irrigation fees, power revenues, and other revenues are used to repay the federal investment in constructing irrigation facilities. Irrigation fees repay the portion of the investment in irrigation facilities that the Secretary of the Interior determines to be within the irrigators' ability to pay. In general, power revenues are used to recoup both power costs and that portion of the investment determined to exceed the irrigators' ability to pay.<sup>4</sup>

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<sup>3</sup>The portion of the federal investment in an irrigation facility in the Pick-Sloan Program that is repaid through power revenues is generally repaid, without interest, within 50 years of the facility's being placed in service following a "development period," where applicable, of up to 10 years. The federal investment in a power facility is generally repaid, with interest, within 50 years of the facility's being placed in service.

<sup>4</sup>Repayment of the capital costs expended for the construction of irrigation facilities through power revenues is referred to as irrigation assistance. About \$643 million of the costs of irrigation construction in the Pick-Sloan Program had been incurred and were scheduled to be repaid through power revenues as of September 30, 1994—the most recent data available at the time of our analysis. In addition, completion of future irrigation facilities could result in the expenditure of over \$5 billion in additional irrigation assistance, according to Western's repayment information.

The Pick-Sloan Program accounted for about 33 percent of the operating revenues generated during fiscal year 1994 by the 14 separate programs from which Western markets and transmits power. In annual revenues from the sale and transmission of electric power, Pick-Sloan is Western's second largest program. The total federal investment in the program as of September 30, 1994, was about \$4.5 billion. About \$2.6 billion of the federal investment in the program is reimbursable through power revenues, and about \$898 million of that amount had been repaid through September 30, 1994.

#### INFEASIBILITY OF SOME IRRIGATION PROJECTS

#### MAKES REPAYMENT OF SOME COSTS UNLIKELY

Because certain of the Pick-Sloan Program's irrigation facilities will not be completed as planned, a portion of the federal investment is unrecoverable. As originally authorized in 1944, portions of the program's power facilities and water storage reservoirs were intended for use with irrigation facilities. The federal investment for these portions was thus considered an investment in irrigation, and repayment was to be made without interest and deferred until the irrigation facilities were completed. As a result of this deferral, power customers would not be obliged to repay the investment in facilities that were ultimately intended for irrigation.

Under the original plan, about 33 percent of the program's generating capacity was to be used to irrigate about 5.3 million acres. As the program progressed, only about 15

percent of the program's power capacity would be needed for irrigation because the acreage planned for irrigation was reduced to about 3.2 million acres.<sup>5</sup> As of September 30, 1994, the federal investment in power facilities was \$286 million, or about 15 percent of the approximately \$1.9 billion total for that purpose. In addition, a portion of the program's water storage reservoirs were intended for use with existing and planned irrigation facilities. As of September 30, 1994, the capital cost associated with this portion of the reservoirs totaled about \$224 million. Although the program's power facilities and storage reservoirs have been largely completed as planned, most of the planned irrigation facilities have not been constructed. As of September 30, 1994, only about 25 percent of the acreage planned for irrigation had been developed.

Some of the program's power facilities and reservoirs are now being used in conjunction with those irrigation facilities that have been completed.<sup>6</sup> As a result, the associated federal investment is now scheduled for repayment. Power facilities representing about \$7 million of the federal investment are now being used to provide irrigation pumping service to about 212,000 acres, and water storage reservoirs representing about \$49 million of the federal investment are now being used to provide

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<sup>5</sup>Not all irrigation facilities require the use of pumping equipment or water storage reservoirs. Because of their proximity to the Missouri River or its tributaries, some irrigation facilities can operate without using pumping equipment or relying on the program's reservoirs. Depending on their location, other facilities may require the use of pumping equipment and/or water from the program's reservoirs.

<sup>6</sup>Approximately 772,000 acres have been developed, requiring about 14 megawatts in generating capacity. In addition, according to Western officials, approximately 7 megawatts of generating capacity are available to Native American tribes for irrigation.

irrigation water to about 182,000 acres. These investments are scheduled for repayment between 2042 and 2047, according to Bureau officials. These officials also stated that the remaining portions of the program's power facilities and reservoirs, which are intended for use with future irrigation facilities, are currently used to generate electricity for sale to power customers.

The Bureau now considers all but one of the program's incomplete irrigation facilities to be infeasible and believes that these projects will likely not be constructed.<sup>7</sup> According to Bureau officials, the costs of developing the remaining acreage planned for irrigation outweigh the benefits that would accrue from irrigating that acreage. They said that although their conclusions are based on preliminary estimates, a more expensive and time-consuming analysis would probably not change their conclusions. As a result, the remaining federal investment—\$454 million—is deferred.

In addition, the amount of the federal investment that is considered unrecoverable will increase over time. As mentioned earlier, the portion of the power facilities planned for use with irrigation facilities represents about 15 percent of the program's overall power capacity. As the overall federal investment in power increases, the amount of the investment associated with irrigation increases correspondingly. For example, while the total federal investment in power facilities increased from about \$1.6 billion at the end of

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<sup>7</sup>According to Bureau officials, the portion of the Glendo irrigation unit located in Wyoming is largely complete and may be used when certain environmental issues are resolved.

fiscal year 1987 to about \$1.9 billion at the end of fiscal year 1994, the corresponding 15-percent portion of this investment that was associated with irrigation increased from about \$249 million to about \$286 million.

**CONGRESSIONAL ACTION WOULD BE  
NEEDED TO RECOVER COSTS**

Legislation currently precludes reallocation of the investment by the Bureau and Western from one purpose of the program to another without congressional authorization. The DOE Organization Act of 1977 precludes revision by the Bureau of the cost allocations and project evaluation standards without prior congressional approval. The Water Resources Development Act of 1986 directed that the program proceed to its ultimate development. According to Western officials, these acts preclude changes in the program's repayment criteria.

The Congress reallocated a portion of the federal investment in power facilities and storage reservoirs intended for irrigation when it passed the Garrison Diversion Unit Reformulation Act of 1986. The act implemented recommendations in the Garrison Diversion Unit Commission's Final Report, submitted to the Congress and to the Secretary of the Interior on December 20, 1984. The Commission was created by the Congress to review North Dakota's needs for water development and to propose modification to the Garrison Diversion Unit. Among other things, the act terminated the development of

about 876,000 of the acreage planned for irrigation under the program. Also as a result of the act, Western scheduled repayment of the existing federal investment in the power facilities and storage reservoirs intended for use in irrigating this acreage. Thus, about \$147 million in federal investment was reallocated for recovery through power revenues. The act directed that Western (1) attempt to minimize any rate increase and (2) phase in any such increase over a 10-year period. According to Western officials, because the investment is to be repaid over 50 years, the power rate was not appreciably affected by this reallocation of the federal investment.

The impact of recovering the \$454 million investment through power revenues could vary significantly depending on many factors, including the amount Western passes on to its power customers. Consistent with the way investments in power are typically repaid (within 50 years and with interest), recovering the full amount through power revenues could result in an increase in Western's wholesale power rate of as much as 14.6 percent, according to Western's calculations.<sup>8</sup> Western officials said the following about this scenario:

- The potential rate increase of 14.6 percent assumes that the entire amount of the increased financial requirement would be passed through to existing power

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<sup>8</sup>In preparing the estimate, Western officials assumed a composite 4-percent interest rate. The wholesale power rate could thus increase by 0.212 cents per kilowatt hour, a 14.6 percent increase over the 1.454 cents per kilowatt hour rate in effect as of September 30, 1994. This potential effect on the rate includes the annual principal payment to recover the \$454 million and an annual interest payment.

customers, without any offsetting reductions in the operating expenses of Western, the Corps, or the Bureau (any offsetting reductions could lessen the need for a rate increase). Western officials noted that such expenses could decrease as a result of Western's ongoing restructuring efforts.

- Since Pick-Sloan's power customers purchase power wholesale and resell it to retail customers, it is difficult to estimate accurately to what extent, if any, the retail customers would be affected by a rate increase at the wholesale level.
  
- Changes in the terms of repayment, such as phasing in a rate increase as was done in 1986, would lessen the effect of the increase.
  
- The estimated rate increase assumes repayment of the \$454 million through power revenues without an overall assessment of the program. Any general assessment of the program could lead to changes in the current cost allocations and rates.
  
- Factors outside of Western's control, such as the amount of water available for power generation, could affect any potential impact on the rates.
  
- The amount of the federal investment in storage reservoirs that would be redirected for repayment through power revenues is uncertain because some of

this investment could be assigned to other program purposes, thereby lessening any effect on the rates.

The Department of the Interior's Inspector General reported in 1993 on the unrecoverable federal investment in the Pick-Sloan Program attributable to infeasible irrigation projects.<sup>9</sup> Recognizing that the majority of the program's irrigation facilities were infeasible and thus would likely never be completed, the report was critical of the Bureau's continuing assumption that the project would ultimately be developed as planned. The Inspector General recommended, among other things, that the Bureau request that the Congress deauthorize—that is, terminate from the program—the infeasible acreage and reallocate the federal investment in the associated irrigation facilities for repayment through power revenues.

The Bureau concurred with the Inspector General's recommendations and agreed to a target date of February 1995 for submitting information to the Congress in response to these recommendations. The Bureau provided us with a draft copy of the list of the infeasible irrigation facilities that it developed in response to the Inspector General's report, but as of April 18, 1996, the Bureau had not yet submitted this information to the Congress.<sup>10</sup> According to Bureau officials, the Bureau is continuing to analyze the

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<sup>9</sup>Audit Report on the Pick-Sloan Missouri Basin Program Cost Allocation, Bureau of Reclamation, Department of the Interior, Office of Inspector General, W-IN-BOR-007-92, Sept. 30, 1993.

<sup>10</sup>The information in app. IV is taken from the Bureau's draft list.

potential alternatives for recovering the portion of the federal investment that is currently unrecoverable. For example, the Bureau is assessing the impact of reallocating the investment on the basis of the current use of the program's facilities rather than on the program's planned long-term development.

The Inspector General's 1993 report also identified another impact of recovering the \$454 million through power revenues. Based on 1992 data, the Inspector General calculated, using a 7.25 percent interest rate, that carrying the unrecoverable federal investment as an investment in irrigation facilities results in an interest cost to the Treasury of about \$30 million annually because the investment is carried without interest. Repaying the unrecoverable federal investment through power revenues would necessitate an annual interest charge. Western officials noted that such an interest payment would likely be less than that calculated by the Inspector General because Western would expect to use a lower interest rate (likely 4 percent) that is based on the weighted average of the interest rates associated with the program's outstanding debt.

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We provided a draft of this statement to and discussed its contents with the Bureau's Regional Director of the Great Plains Region; the Bureau's Washington Director, Policy and External Affairs; Western's Acting Area Manager for the Pick-Sloan Program; and the Deputy Assistant Administrator from the Department of Energy's Power Marketing Liaison

Office. They clarified several points about the estimate of the potential impact on the power rate of recovering a portion of the federal investment through power revenues. These officials also suggested several technical revisions to our statement, which we incorporated as appropriate. We conducted our review between December 1995 and April 1996 in accordance with generally accepted government auditing standards.

This concludes our prepared statement. It also concludes our work on this issue. Appendix I shows the operating characteristics of the Pick-Sloan Program's hydropower generating facilities; appendix II shows the allocation of the reimbursable and nonreimbursable federal investment among the program's purposes, appendix III shows the status of the federal investment reimbursable through power revenues, appendix IV shows the status of the program's irrigation facilities. We will be glad to answer any questions you may have.

APPENDIX I

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**OPERATING CHARACTERISTICS OF HYDROPOWER GENERATING FACILITIES  
IN THE PICK-SLOAN PROGRAM, AS OF SEPTEMBER 30, 1994**

Operating agency	Facility <sup>a</sup>	Number of generating units	Nameplate capacity (MW) <sup>b</sup>	Fiscal year of initial operation
<b>Eastern Division<sup>c</sup></b>				
Bureau	Canyon Ferry	3	60	1954
Bureau	Yellowtail <sup>d</sup>	4	288	1966
Corps	Big Bend	8	538	1965
Corps	Fort Peck	5	218	1943
Corps	Fort Randall	8	387	1954
Corps	Garrison	5	546	1956
Corps	Gavins Point	3	122	1956
Corps	Oahe	7	786	1962
Subtotal		43	2,945	
<b>Western Division<sup>c</sup></b>				
Bureau	Boysen	2	15	1952
Bureau	Fremont Canyon	2	66	1961
Bureau	Glendo	2	38	1959
Bureau	Kortes	3	36	1950
Bureau	Pilot Butte	2	2	1925
Subtotal		11	157	
<b>Total</b>		<b>54</b>	<b>3,102</b>	

<sup>a</sup>Not shown here are the generating facilities of the Bureau's Colorado-Big Thompson, Kendrick, Shoshone, and North Platte projects, which have been integrated with Pick-Sloan's Western Division for marketing and operating purposes.

<sup>b</sup>The nameplate capacity refers to the full-load, continuous rating under specified conditions, usually indicated on a plate attached physically to the equipment. Because stream flow largely

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dicates the amount of water available for generation, the average megawatts available for power generation from a hydropower generating facility may be well below the nameplate capacity. These numbers are rounded to the nearest megawatt (MW). A megawatt is 1 million watts.

\*For operational purposes, the Pick-Sloan Program is divided into two divisions. The Eastern Division markets power from eight hydropower generating facilities. The Western Division, which was operationally and contractually integrated in 1989 with Western's Fryingpan-Arkansas project, markets power from five hydropower generating facilities. For financial reporting, the Fryingpan-Arkansas project and Pick-Sloan's Western Division are separate. The power rates and financial statements for the Pick-Sloan Program reflect the costs and repayment requirements for both the Eastern and Western Divisions.

\*The Eastern and Western Divisions each market a portion of the power generated at the Yellowtail Dam in Montana.

## APPENDIX II

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**ALLOCATION OF REIMBURSABLE AND NONREIMBRUSABLE FEDERAL  
INVESTMENT BY PROGRAM PURPOSE, AS OF SEPTEMBER 30, 1994**

Dollars in thousands

<b>Program purpose</b>	<b>Federal investment</b>
<b>Reimbursable investment</b>	
Power	\$1,870,236 <sup>a</sup>
Irrigation	1,497,969 <sup>b</sup>
Municipal and industrial water supply	256,398
Subtotal	3,624,603
<b>Nonreimbursable investment</b>	
Flood control and navigation	529,839
Recreation	70,158
Fish and wildlife	80,298
Highway improvement	13,388
Safety of dams	28,263
Cultural resources	1,297
Other	115,647
Subtotal	833,890
<b>Total</b>	<b>\$4,458,493</b>

<sup>a</sup>This amount differs from the corresponding figure shown in app. III. Western and Bureau officials attribute the differences between the figures to variations in the manner in which the agencies report interest during construction and construction work in progress.

<sup>b</sup>This amount reflects the cumulative federal investment in constructing irrigation facilities. As shown in appendix III, the portion of these costs that is currently scheduled by Western for recovery through power revenues is \$643 million.

Source: Based on information provided by the Bureau.

## APPENDIX III

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**STATUS OF FEDERAL INVESTMENT REIMBURSABLE THROUGH POWER  
REVENUES, AS OF SEPTEMBER 30, 1994**

Dollars in thousands

<b>Reimbursable federal investment</b>	<b>Amount</b>
<b>Power</b>	<b>\$1,936,000*</b>
<b>Nonpower (irrigation assistance)</b>	<b>643,000*</b>
<b>Total reimbursable investment</b>	<b>2,579,000</b>
<b>Investment repaid</b>	<b>898,000</b>
<b>Unpaid investment</b>	<b>\$1,681,000</b>

\*This amount differs from the corresponding figures shown in app. II. Western and Bureau officials attribute the differences between the figures to variations in the manner in which the agencies report interest during construction and construction work in progress.

\*This amount is the portion of the overall federal investment in irrigation facilities that is recoverable through power revenues.

Source: Based on Western's 1994 Annual Report, Statistical Appendix.

**STATUS OF IRRIGATION PROJECTS IN THE PICK-SLOAN PROGRAM  
AS OF SEPTEMBER 30, 1994**

The following four tables provide information on the status of the Pick-Sloan Program's existing, planned, and reauthorized irrigation facilities as provided by the Bureau in its draft list. Table IV.1 summarizes all these facilities. Tables IV.2, IV.3, and IV.4 provide details on existing, planned, and reauthorized units, respectively. The benefit-cost ratios that appear in these tables reflect the Bureau's calculation of the feasibility of developing the irrigation facilities. The ratio for an individual facility results from dividing the benefits expected to be derived from developing a facility by the expected cost of constructing and operating that facility. The Bureau considers a ratio exceeding 1.0 to indicate feasibility and a ratio of less than 1.0 to reflect infeasibility. We did not assess the accuracy of the information in the tables or in the notes, which were also provided by the Bureau.

**Table IV.1: Summary of Irrigation Facilities**

Status of facility	Number of irrigation facilities	Acres to be fully irrigated*	Acres to be partially irrigated*	Capacity (kW)	Irrigation-related power investment	Irrigation-related reservoir investment	Total irrigation-related investment
Planned	95	838,400	243,629	122,269	\$84,210,328	\$74,894,665	\$159,104,993
Reauthorized	9	940,840	263,100	281,331	194,361,079	100,321,296	\$294,682,375
<b>Subtotal</b>	<b>104</b>	<b>1,779,240</b>	<b>506,729</b>	<b>403,600</b>	<b>\$278,571,407</b>	<b>\$175,215,961</b>	<b>\$453,787,368</b>
Existing	30	623,800	148,171	14,423	7,301,915	49,101,827	\$56,403,742
<b>Total</b>	<b>134</b>	<b>2,403,040</b>	<b>654,900</b>	<b>418,023</b>	<b>\$285,873,322</b>	<b>\$224,317,788</b>	<b>\$510,191,110</b>

\*Fully irrigated acres are those irrigated using only federal irrigation water.

\*Partially irrigated acres are those irrigated using federal water to supplement other sources.

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Table IV.2: Existing Irrigation Facilities

Existing facility	State	Year unit was placed in service	Fully irrigated acres <sup>a</sup>	Partially irrigated acres <sup>b</sup>	Capacity (kW)	Irrigation-related power investment	Irrigation-related storage reservoir investment	Benefit-cost ratio for irrigation and date of analysis
St. Francis (Armel) <sup>c</sup>	CO	1951	6,000		1,988	\$1,369,195		0.55, Jan. 1967
Almena	KS	1967	5,400					1.02, Dec. 1962
Cedar Bluff <sup>d</sup>	KS	1963	6,200					1.82, Oct. 1961
Glen Elder	KS	1970	21,000					1.26, Aug. 1958
Kirwin <sup>e</sup>	KS	1957	11,500					0.90, Jun. 1952
Webster	KS	1960	8,500					2.00, Dec. 1960
Crow Creek <sup>f</sup>	MT	1955	5,000		2,000	1,377,460	\$86,682	1.96, Aug. 1950
East Bench	MT	1965	21,800	28,000			222,992	1.47, Mar. 1956
Helena Valley	MT	1959	14,100	3,500			184,823	1.50, Dec. 1956
Lower Marias	MT	1979	127,000		3,435			1.80, July 1971
Savage	MT	1950	2,200		386		202,000	N/A <sup>g</sup>
Dickinson	ND	1954	400					1.20, Oct. 1947
Fort Clark	ND	1954	1,900		485	334,034	171,133	1.10, May 1949
Heart Butte	ND	1952	6,700		1,601	1,102,657		N/A
Ainsworth	NE	1965	34,000		160	110,197		2.34, Jan. 1964
Farwell	NE	1966	52,500		600	413,238		2.03, Sep. 1955
Frenchman-Cambridge	NE	1952	54,700	9,600				1.92, Oct. 1961
Glendo	NE	1958		23,500				1.40, Dec. 1952
Sargent	NE	1957	13,700					1.67, Mar. 1952
Bostwick	NEKS	1953	86,200		640	440,787	46,436,600	2.01, Dec. 1956
Angostura	SD	1953	12,100					1.22, Apr. 1956
Belle Fourche <sup>h</sup>	SD	1914						
Rapid Valley	SD	1948		8,900				1.66, Dec. 1952
Shadehill	SD	1976	9,000					1.23, Jan. 1964
Keyhole	SD/WY	1976		57,200				1.06, Oct. 1949
Glendo	WY	1958		4,371				N/A
Hanover-Bluff	WY	1957	7,000		2,002	1,378,637	1,379,854	1.44, Nov. 1953
Owl Creek	WY	1957		13,100	1,126	775,510	417,743	1.04, Jun. 1950
Riverton	WY	1925	64,300					
North Loup	NE	1989	52,600					1.30, Feb. 1971
<b>Total</b>			<b>623,800</b>	<b>148,171</b>	<b>14,423</b>	<b>\$7,301,915</b>	<b>\$49,101,827</b>	

<sup>a</sup>Fully irrigated acres are those irrigated using only federal irrigation water.

<sup>b</sup>Partially irrigated acres are those irrigated using federal water to supplement other sources.

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<sup>4</sup>In 1967, the benefit-cost ratio for this facility (0.55) indicated that the irrigation development was infeasible, and the irrigation storage in the Bonny Reservoir was sold to the state of Colorado for recreation purposes. The project was authorized for completion on the basis of all of its benefits.

<sup>5</sup>The Reclamation Projects Act deauthorized funding for irrigation at Cedar Bluff because of a lack of water. The irrigation district was relieved of its obligation, and the state of Kansas paid the costs of irrigation storage on a discounted present-value basis. The available water is used by the state for recreation, fish and wildlife, and supplemental municipal water supply.

<sup>6</sup>The Kirwin Unit Definite Plan Report (June 1952) showed a benefit-cost ratio of 0.9. Correspondence in September 1952 from the Acting Commissioner and the Regional Director, Lower Missouri Region, requested that intangible (indirect) benefits be included in the justification. Subsequent correspondence from the Regional Director provided the requested benefits that were included to justify the construction.

<sup>7</sup>The facility is part of the Three Forks Division, which has a total pumping demand of 3,199 kilowatts.

<sup>8</sup>N/A = not applicable.

<sup>9</sup>Since Boysen storage is designated for water service, irrigation assistance reflects the currently unassigned storage costs for the reservoir.

<sup>10</sup>This facility has been integrated as part of the Bureau's Rehabilitation and Betterment Program.

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Table IV.3: Planned Irrigation Facilities

Planned facility	State	Year facility was placed in service <sup>a</sup>	Acres to be fully irrigated <sup>b</sup>	Acres to be partially irrigated <sup>c</sup>	Capacity (kW)	Irrigation-related power investment	Irrigation-related reservoir investment	Irrigation benefit-cost ratio
North Republican	CO/NE		2,400	2,700				0.18
Wilson	KS		25,000					0.10
Aizada	MT		9,000					0.10
Battlefield	MT		1,200		94	\$64,741	\$2,603,800	0.05
Benteen Flat	MT		1,600				3,473,300	0.07
Bonanza	MT		800		58	39,946	72,056	0.33
Brush	MT		1,000		70	48,211	90,070	0.46
Cameron Bench	MT		4,000	3,100				0.07
Chestnut Valley	MT		4,600					0.05
Clarkston	MT		1,000		134	92,290		0.09
Cracker Box	MT		1,600		106	73,005		0.07
Crow	MT		1,200		69	47,522	2,603,800	0.05
Diamond Ranch	MT		900				81,063	0.39
Dunmore	MT		11,400				24,740,800	0.10
Elm Coulee	MT		2,000		445	306,485		0.18
Farmer Creek	MT		1,600		187	128,793	144,112	0.39
Gallatin	MT			59,100	3,064	2,110,269		0.79
Glasgow Bench	MT		59,400		15,300	10,537,569	5,350,158	0.37
Haley	MT		2,400		703	484,177		0.19
Hardin <sup>d</sup>	MT		42,600	1,000	13,300	9,160,109		0.08
Hardscrabble	MT		2,200		273	188,023	198,154	0.41
Hobson Unit	MT			6,000				0.02
Huntley extension <sup>e</sup>	MT		1,800		62	35,814		0.03
Jefferson	MT		47,400	15,200				0.06
Lewistown	MT		4,000					0.07
Madison	MT		12,600	13,600				0.08
Marsh	MT		2,800		716	493,131		0.03
Medicine Lake North	MT		14,700		7,440	5,124,151	1,324,029	0.13
Medicine Lake South	MT		24,700		10,130	6,976,835	2,224,729	0.15
Missouri Diversion	MT		92,800		28,720	19,780,328	8,358,496	0.17
N-Bar-N	MT		7,200		739	508,971	648,504	0.22
Newlan	MT		3,900					0.03
Nickwall	MT		2,800		245	168,739	252,196	0.29
Noble	MT		1,700		242	166,673	153,119	0.34
Rock Creek	MT		1,000	200				0.06
Ross Fork	MT		3,000					0.08

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Saco Divide	MT		3,400		1,800	1,239,714		0.10
Seven Mile-Sitting Bull	MT		6,500		941	648,095		0.08
Seven Sisters	MT		3,200		1,462	1,006,923		0.13
Shoestring	MT		1,200		109	75,072	108,084	0.27
Shotgun (privately developed)	MT							
Sidney	MT		1,000		266	183,202		0.12
Stipek	MT		2,900		1,211	834,052		0.12
Sun-Teton	MT		53,200	3,700	1,422	979,374		0.01
West Bench	MT			6,700				0.12
Whitehall	MT		6,700	3,900				0.07
Wyola	MT		3,600				7,816,100	0.09
Yellow Bluff	MT		1,300		118	81,270	117,091	0.35
Bismarck	ND		8,500		514	354,007	765,595	0.11
Broncho	ND		15,400					0.08
Burnt Creek	ND		1,300		64	44,079	117,091	0.12
Hancock Flats	ND		5,400		1,202	627,853	486,378	0.12
Horsehead Flats Unit	ND		6,500		1,494	1,028,963	585,455	0.07
Manley Unit	ND		1,200		47	32,370	108,084	0.21
Nesson Unit	ND		7,400		591	407,039	666,518	0.38
Oliver-Sanger Unit	ND		8,300		2,109	1,452,532	747,581	0.14
Painted Woods Unit	ND		2,800		601	413,927	252,196	0.11
Square Butte Unit	ND		1,900		94	64,741	171,133	0.09
Williston Unit	ND		8,500		1,689	1,163,265	765,595	0.33
Winona Unit	ND		4,500		686	472,469	405,315	0.08
Wogansport Unit	ND		1,600		172	118,462	144,112	0.09
Albion Division	NE		16,900	1,900	364	250,698		0.05
Cedars Rapids Division	NE		29,800		97	66,807		0.05
Little Blue Unit	NE		20,000					0.03
Mirage Flats Extension	NE		5,900					0.04
Belle Fourche	SD		5,000		290	199,732		0.06
Crazy Horse	SD		500		32	22,039	45,035	0.11
Cukdesac	SD		5,400		1,848	1,272,773	486,378	0.08
Fort Thompson	SD		7,500		1,841	1,267,952	675,525	0.19
Grass Rope	SD		4,300		1,366	940,805	387,301	0.09
Greenwood	SD		4,900		472	325,081	441,343	0.18
Iron Nation	SD		1,700		503	346,431	153,119	0.06
Joe Creek	SD		4,400		1,649	1,135,716	396,308	0.08
LaRoche	SD		1,800		551	379,490	162,126	0.03

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Pine Ridge	SD		12,700		1,695	1,167,397		0.02
Rousseau	SD		2,200		566	389,821	196,154	0.08
Tower	SD		2,000		100	68,873	180,140	0.29
Yankton	SD		1,100		58	39,946	99,077	0.05
Edgemont	SDWY		4,700					0.02
Bighorn	WY		1,700		426	293,399	374,054	0.15
Boysen <sup>1</sup>	WY							0.00
Buffalo	WY		3,000	7,100				0.09
Crazy Woman	WY		5,700	6,400	280	192,844		0.10
French Creek	WY		800	2,500				0.07
Glendo <sup>2</sup>	WY			9,729			1,417,865	1.75
Greybull Flat	WY		1,000		343	236,234	211,281	0.17
Hudson Bench	WY		5,700				513,399	0.16
Kaycee	WY		23,100	5,800	2,529	1,741,798		0.08
Little Wind	WY			34,000				1.09
Lower Powder	WY		58,500		4,290	2,954,652		0.23
Piney	WY		4,000	16,000	56	38,569		0.21
Sheridan	WY			38,100				0.20
Shoshoni	WY		16,800		2,210	1,522,093	3,578,846	0.31
Tongue Pumping	WY		26,100		1,800	1,239,714		0.12
Ucross	WY		2,800	7,100	224	154,276		0.04
<b>Total</b>			<b>838,400</b>	<b>243,829</b>	<b>122,269</b>	<b>84,210,328</b>	<b>\$74,894,865</b>	

<sup>1</sup>The on-line date is indeterminate pending a finding of feasibility and reauthorization or, in the case of reauthorized but suspended facilities, a determination of the facility's status or the disposition of the facility's construction appropriations.

<sup>2</sup>Fully irrigated acres are those irrigated using only federal irrigation water.

<sup>3</sup>Partially irrigated acres are those irrigated using federal water to supplement other sources.

<sup>4</sup>Under the latest plan, the facility would use a hydraulic turbine from the Yellowtail Dam instead of electric pumps for irrigation pumping.

<sup>5</sup>Unit 2 is infeasible.

<sup>6</sup>Since Boysen storage is designated for water service, the irrigation assistance reflects the currently unassigned storage costs for the reservoir.

<sup>7</sup>Storage assignment for unsold water out of Glendo. The sale of Glendo water is being impeded by unresolved environmental concerns.

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Table IV.4: Reauthorized Irrigation Facilities

Reauthorized facility <sup>a</sup>	State	Year facility was placed in service <sup>b</sup>	Acres to be fully irrigated <sup>c</sup>	Acres to be partially irrigated <sup>d</sup>	Capacity (kW)	Irrigation-related power investment	Irrigation-related reservoir investment	Benefit-cost analysis and date of analysis <sup>e</sup>
Pollock-Herried <sup>f</sup>	SD		15,000		6,060	\$4,173,704	\$1,351,050	1.70, Jan. 1966
Garrison Diversion <sup>f</sup>	ND		115,740		72,298	50,753,288	20,357,702	0.70, 1992
Lake Andes-Wagner <sup>f</sup>	SD		45,000		23,900	16,460,647	4,053,150	0.56 & 1.02, 1986
Shoshone Extension	WY		36,600	37,300	522		200,660	2.06, June 1967
Narrows	CO			225,800				1.62, Jan. 1967
Kanopolis <sup>f</sup>	KS		16,500				29,774,084	1.50, Dec. 1971
Nebraska-Mid State	NE		140,000		16,800	11,570,664		1.40, Jan. 1960
O'Neill	NE		77,000		4,515	3,109,616		1.53, Apr. 1971
Oahe	SD		495,000		157,236	108,293,150	44,584,650	1.70, Jan. 1966
<b>Total</b>			<b>940,840</b>	<b>263,100</b>	<b>281,331</b>	<b>\$194,361,069</b>	<b>\$100,321,296</b>	

<sup>a</sup>These facilities were individually reauthorized by acts of Congress.

<sup>b</sup>The date a facility will be placed in service is indeterminate pending a finding of feasibility and reauthorization or, in the case of reauthorized but suspended facilities, a determination of the facility's status or the disposition of the facility's construction appropriations.

<sup>c</sup>Fully irrigated acres are those irrigated using only federal irrigation water.

<sup>d</sup>Partially irrigated acres are those irrigated using federal water to supplement other sources.

<sup>e</sup>Applying the current benefit-cost methodology and new economic parameters would render the reauthorized units infeasible today. The benefit-cost ratios for the reauthorized facilities shown in table IV.4 were calculated using previous benefit-cost methodologies. These methodologies resulted in ratios that tended to be higher than those calculated using current methodologies because the previous methodologies (1) counted specialty crops, which are more lucrative as a benefit; (2) used historic prices, which are higher in real terms than the current ones; and (3) incorporated both direct and indirect benefits while current methodologies use only direct benefits (indirect benefits have a high multiplier of 1.7 or 1.8). In the early 1970s, the Water Resource Council (established under the Water Resources Planning Act of 1965) recommended the use of a benefit-cost methodology that would have resulted in ratios indicating infeasibility had it been applied to the Pick-Sloan reauthorized irrigation facilities. Specifically, the new methodology (1) used only direct benefits; (2) used more recent prices based on U.S. Department of Agriculture estimates; (3) excluded specialty crops; (4) incorporated recent, higher interest rates (7 or 8 percent now versus the 2 or 3 percent used during the 1950s and 1960s); and (5) discounted for inflation. These new "principles and standards" became effective in 1979. They were replaced by less rigid "principles and guidelines" (which allowed some exceptions; for example, the inclusion of specialty crops as benefits). The Bureau has not reassessed the benefit-cost ratios for the reauthorized facilities because some federal investment in irrigation equipment has already occurred at these facilities (the amounts invested are shown in the notes for the individual reauthorized units) and because the Congress specifically decided to reauthorize the facilities. This investment in these irrigation facilities requires a careful consideration of the decision to terminate or proceed and the manner in which these sunk costs will be handled.

## APPENDIX IV

## APPENDIX IV

<sup>1</sup>The appropriation was deauthorized by P.L. 100-516, which authorized the Mini-Wiconi Rural Water Supply Project. No studies were conducted to determine the facility's feasibility, but local interests suggested deauthorizing the irrigation development as a trade-off for developing a rural domestic water supply and distribution system to serve the needs of the Native American and non-Native American populations in the area. The power allocation for the facility was made available for the municipal and industrial system, and funding for irrigation was deauthorized. The irrigation facility was to remain as a planned facility of the Pick-Sloan Program. Approximately \$1.1 million in federal investment in irrigation-related equipment has been expended on this facility as of September 30, 1994. This investment is currently categorized as construction-work-in-progress.

<sup>2</sup>The acreage for the Garrison Diversion Unit was reduced from 1,000,007 acres to 130,940 acres by P.L. 99-294 and to 115,740 acres by P.L. 102-575. At the time of the reformulation in 1986, it was recognized that the reduced scope of the project would result in economic infeasibility because of the loss of economies of scale and other factors. The reformulation was a compromise. Subsequent to the reallocation of the project's costs, it was determined that the project was also financially infeasible because the annual operation and maintenance costs exceeded the irrigator's ability to pay. A team appointed by the Secretary of the Interior recommended a halt to further development of the project. Approximately \$132.9 million in federal investment in irrigation-related equipment had been expended on this facility as of September 30, 1994. This investment is currently categorized as construction-work-in-progress.

<sup>3</sup>The facility was reauthorized by the Lake-Andes/Marty II Unit Act of 1992 (P.L. 102-575). The benefit-cost ratio for this unit was based on post-1979 methodologies. The Bureau employed "customized procedures" in calculating the ratio that allowed the consideration of a specialty crop (potatoes) as a benefit. The Planning Report/Draft Environmental Impact Statement (1985) included a benefit-cost ratio, using strict principles and guidelines standards, of 0.56. Under the customized procedures that included specialty crops, livestock intensification, and alternative price normalization, the benefit-cost was calculated at 1.02. On this basis, the Congress reauthorized the project.

<sup>4</sup>Approximately \$3.7 million in federal investment in irrigation-related equipment has been expended on this facility as of September 30, 1994. This investment is currently categorized as construction-work-in-progress.

<sup>5</sup>Suspended; the assigned cost is for a Corps reservoir.

<sup>6</sup>Approximately \$3.0 million in federal investment in irrigation-related equipment had been expended on this facility as of September 30, 1994. This investment is currently categorized as construction-work-in-progress.

<sup>7</sup>Approximately \$7.1 million in federal investment in irrigation-related equipment had been expended on this facility as of September 30, 1994. This investment is currently categorized as construction-work-in-progress.

Source: Based on information from the Bureau of Reclamation, Great Plains Region, Billings, Montana.

STATEMENT OF  
MR. J. M. SHAFER,  
ADMINISTRATOR  
WESTERN AREA POWER ADMINISTRATION  
U. S. DEPARTMENT OF ENERGY  
BEFORE THE  
SUBCOMMITTEE ON WATER AND POWER RESOURCES  
COMMITTEE ON RESOURCES  
UNITED STATES HOUSE OF REPRESENTATIVES  
MAY 2, 1996

Mr. Chairman, thank you for inviting me to testify before your subcommittee today on the Western Area Power Administration's (Western's) role in the suballocation of Pick-Sloan Missouri Basin Program power investment, from the Department of Energy's (DOE's) perspective. My remarks on the applicable authorities and methods of operation of the Pick-Sloan are limited to DOE's interpretation of the appropriate authorities. I will begin by providing the Subcommittee some background on Western.

Western markets and transmits Federally produced power throughout a 1.3 million-square-mile geographic area in 15 central and western states to nearly 600 wholesale customers. Western operates and maintains 16,760 miles of transmission line, 257 substations, and other associated power facilities. Electric power marketed by Western is generated at 56 plants operated primarily by the Bureau of Reclamation and the U. S. Army Corps of Engineers.

The Pick-Sloan Missouri Basin Program is a comprehensive river basin development project located in the upper basin of the Missouri River. Authorized by section 9 of the Flood Control Act of 1944, Pick-Sloan was conceived as a multi-state project consisting of dams on the Missouri and its tributaries as well as approximately five million acres of irrigation development. The Pick-Sloan was authorized by Congress as an ultimate development project, which means that cost allocations and suballocations are based on conditions expected to exist at the time that future Pick-Sloan construction is ultimately completed.

All capital investments associated with Pick-Sloan have been allocated by the Bureau of Reclamation and U.S. Army Corps of Engineers among the various project purposes: navigation, irrigation, power, flood control, recreation, municipal and industrial water, and fish and wildlife. Western has no authority to allocate or reallocate these costs. Congress has directed that Pick-Sloan investments allocated to flood control, navigation, fish and wildlife, and recreation be nonreimbursable. Unless provided otherwise by law, power investment is repaid with interest through Western's rates. Transmission investment by Western is included in power investment.

Congress recognized that project beneficiaries would be unable to repay the total Federal investment in authorized irrigation facilities. As a result, power customers are to repay authorized irrigation investment that is deemed by the Bureau of Reclamation

to be beyond the ability of irrigators to repay. Pursuant to law, irrigation assistance does not bear interest.

A unique feature of Pick-Sloan is the suballocation of investment allocated to power. When the Pick-Sloan Program was authorized, Congress envisioned a need for reservation of pumping power associated with authorized irrigation projects to deliver water to farmers. Power investment used to pump irrigation water was to be repaid without interest over the same time period allowed for repayment of the benefitting irrigation facilities.

Since their authorization in 1944, the construction of hydroelectric power plants has progressed far more quickly than construction of Pick-Sloan irrigation features. For example, it is my understanding from the Bureau of Reclamation that the actual Pick-Sloan hydropower capacity completed is more than double the 1944 estimate, while only 11 percent of originally planned irrigation acreage has been completed. Notwithstanding the uneven pace of development, consistent with the concept of ultimate development, that portion of the power investment eventually envisioned for pumping of irrigation water continues to be suballocated to irrigation. The effect of this suballocation is that 15.8% of existing power investment bears no interest and its principal will not be repaid until the same future time period as the benefitting irrigation features. Delaying repayment of the suballocated power investment makes today's power rate lower than it would otherwise be. Power associated with the 15.8% suballocated to irrigation is not given away for "free". It is sold at the current firm power rate for Pick-Sloan power.

The suballocation of power investment to irrigation was an integral component in the original authorization of the Pick-Sloan Missouri Basin Program in the Flood Control Act of 1944. Congress has on several occasions confirmed the ultimate development approach in repayment, most recently in section 1122 of the Water Resources Development Act of 1986. I am advised by legal counsel that action by Congress is necessary to alter the ultimate development approach taken by Western for the Pick-Sloan Missouri Basin Program. Therefore, neither Western nor the generating agencies have the authority to modify the suballocation approach administratively:

The suballocation of power investment has been examined in various audit reports over time. Since 1968, the U.S. General Accounting Office and the Interior Department's Inspector General

Office have reported a total of eight times regarding Pick-Sloan cost allocation and repayment. These reports note that Congress would need to authorize a departure from the current suballocation practice.

Mr. Chairman, this concludes my remarks. If you or members of the Subcommittee have any questions, I would be pleased to answer them.

Honorable Patricia J. Beneke  
Assistant Secretary for Water and Science  
Department of the Interior

before the

House Subcommittee on Water and Power Resources  
May 2, 1996

Thank you for the invitation to appear before the Subcommittee. I appreciate the opportunity to discuss the status of irrigation projects authorized as part of the Pick-Sloan Missouri Basin Program, as well as repayment of Pick-Sloan facilities.

#### **HISTORICAL BACKGROUND**

To begin, I would like to provide a short historical background.

The Flood Control Act of 1944 authorized what was then called the Missouri River Basin Project as a comprehensive plan to manage the water and power resources of the Missouri River Basin. In 1970, the Congress changed the project's name to the Pick-Sloan Missouri Basin Program. The Program included the Pick Plan, developed by the U.S. Army Corps of Engineers primarily to control floods in the Lower Missouri River Basin, and the Sloan plan, developed by the Bureau of Reclamation primarily to irrigate lands in the Upper Missouri River Basin.

The Program envisioned a comprehensive system of flood control, navigation improvement, irrigation, municipal and industrial water supply, and hydroelectric power generation facilities for 10 states -- Montana, Wyoming, Colorado, Kansas, Nebraska, North Dakota, South Dakota, Minnesota, Iowa and Missouri. As planned, Pick-Sloan would have included 213 single and multi-purpose projects providing over 1.1 million kilowatts of hydroelectric power capacity, and irrigation water to more than five million acres of farmland, among other features.

The idea for the program was conceived at a time when there was a significant effort underway to encourage people to return to the Great Plains. The population had declined significantly during the dust bowl era of the 1930's and during World War II when people left the area to assist in the war effort. Also, intermittent years of flooding along the Missouri River and its tributaries was a major concern. In the Spring of 1943, a record flood on the Missouri River caused devastating damage from South Dakota through Missouri. It was thought that the Pick-Sloan program would provide economic stability and hydropower for a growing nation at the same time as it would contribute important flood control, navigation and irrigation benefits.

Three Federal agencies are involved in managing the Program today. The Army Corps of Engineers operates six multipurpose projects on the main stem of the Missouri River along with a number of smaller projects on the tributaries. The Corps administers the flood control and navigation aspects of Program projects. Reclamation has a large number of multipurpose projects primarily on the tributaries to the Missouri River. Both Corps and Reclamation projects provide hydropower. Reclamation was initially given the responsibility of operating the transmission lines and hydropower marketing, but when the Department of Energy was formed in 1977, this responsibility was transferred to the Western Area Power Administration.

The original authorization was based on plans and estimates that were of a preliminary nature. The authorization recognized that some elements would change as further investigations were completed and the plan was approved, "subject to such modifications and changes as may be indicated, from time to time, as the plan is effectuated." Indeed, the original plan overestimated irrigation and navigation development and underestimated hydropower and recreation. Following enactment, while the plans were being refined, new analytical tools for economic, financial, hydrologic and soils analyses were being developed and applied. As a result, by 1958 the original irrigation development had gone from a proposed 5.3 million acres of new and supplemental irrigation to 3.8 million and hydropower from 1.1 million kilowatts to 2.4 million kilowatts. All of these changes and developments were reflected in the Corps' and Bureau's 1958 Economic Analysis and cost allocations.

The current economic and environmental modeling that is used for project evaluation to determine where Federal investments are made has evolved significantly since the time when Pick-Sloan was authorized and the original cost allocations were determined. Currently, we use economic and environmental modeling, such as the Economic and Environmental Principles and Guidelines for Water and Related Land Resources Implementation Studies and other public planning processes such as that in the National Environmental Policy Act, to determine if projects merit Federal investment. These methods were not in use when Pick-Sloan was authorized. Not only has the method of evaluation changed, but also local and national needs and values have changed significantly since 1944. Given the way the Executive Branch and Congress has looked at potential Federal projects in recent years, Pick-Sloan probably would be quite different from what was enacted in 1944, if authorized today.

Although the Pick-Sloan program has not been carried out as initially envisioned, the Program has provided significant benefits, such as water supply, flood control, recreation, hydropower, and navigation. Most of the hydropower, flood control, and navigation facilities have been built, and in fact actual developed power capacity is more than double what was originally planned. Since the program was first authorized in 1944, the Program dams and levies have reduced flood damages significantly. Annual hydropower sales average \$200 million per year and navigation benefits are estimated to average about \$17.7 million per year. Irrigated lands produce crops with an annual gross value of \$158 million. The attached chart shows by state the annual recreation benefits provided in 1994 as a result of the mainstem dams and reservoirs constructed in the Pick-Sloan program.

## **IRRIGATION**

While much of the originally planned project development has occurred, the program has fallen far short of its stated goals for irrigation. Overall, only about 11 percent of the irrigation anticipated in the Pick-Sloan plan -- less than 600,000 acres-- has actually been Federally developed of the planned 5.3 million irrigated acres.

The attached table shows by state the amount of acres planned to be developed for irrigation, and the number of acres actually developed under the Pick-Sloan Missouri Basin Program.

A combination of factors explain why Pick-Sloan has not met its original expectation for irrigation. A limited growing season along with market conditions and soil characteristics, including drainage problems, have all played a role. For these and other reasons, some irrigation projects were not economic to build.

### **COST ALLOCATION**

In accordance with Reclamation law, costs for purposes that are deemed reimbursable are repaid by the beneficiaries and nonreimbursable costs are paid for by the taxpayers. For example, certain costs allocated for irrigation are to be repaid by those agricultural users, and costs for construction and maintenance of the facilities attributed to hydropower are allocated to be repaid by the power customers. Costs repaid by irrigation, including pumping power costs, are reimbursable without interest, and power costs are reimbursable with interest. Costs associated with flood control, recreation and environmental enhancement are generally non-reimbursable and are therefore borne by the taxpayers.

In 1958, Reclamation and the Army Corps of Engineers completed a report showing the cost allocations for the multipurpose projects in Pick-Sloan. Known as the Ultimate Development Plan, the report was based on the assumption that all program components would be fully developed as envisioned in 1958. This methodology distributed or allocated costs based on the benefits anticipated for each purpose identified in the Ultimate Development Plan.

Subsequently, in 1963, in response to concerns about the financial health of the Pick-Sloan program, the Interior Department provided Congress with the Report on Financial Position, Missouri River Basin Project. The 1963 report presented a financial plan to maintain the financial integrity of the Pick-Sloan program. The report re-affirmed the Ultimate Development Plan concept that storage and pumping power facilities were built largely for the ultimate benefit of the irrigation projects that had not yet been built, but were expected to be built in the future. In reality, the cost assumptions in the Ultimate

Development Plan have not panned out as planned.

In 1964, Congress adopted Public Law 88-442, the Missouri River Basin Appropriation Act, which required reauthorization of individual Program projects that were not under construction as of June 30, 1964. This meant that all facilities that were originally authorized to be built as part of the Pick-Sloan program, but which were not yet completed by this date, had to be reauthorized by Congress before construction activities could commence. Since June 30, 1964, nine facilities have been reauthorized, and construction activities have taken place on four of the projects. The others remain inactive.

We do not expect that the entire Pick-Sloan Program will be realized. Nonetheless, costs continue to be allocated to Program purposes based on the assumption that full Program development will occur. Reclamation is prohibited by law, including the 1977 Department of Energy Reorganization Act, from reallocating the costs of the Pick-Sloan Program without authorization from Congress. Given current economic and financial conditions, it is difficult to justify further irrigation. However, because under current law Reclamation is bound by the cost allocation of the Ultimate Development Plan, costs associated with irrigation-related pumping power and reservoir storage continue to be allocated to future irrigation development. As a result these costs are deferred at zero interest until they are assigned to a unit under construction. The total deferred cost is currently \$382 million, consisting of \$127 million in reservoir storage and \$255 million of pumping power costs. The deferring of these costs results in \$14 million annually lost to the Treasury, exclusive of interest.

At this point, Mr. Chairman, of the original \$6.6 billion investment, \$2.5 billion is considered reimbursable by irrigation, \$2.3 billion is reimbursable by power, and \$.9 billion is reimbursable by municipal and industrial users. To date, \$601 million or 27 percent of their obligation has been repaid by power users, \$63 million or 2.5 percent of their obligation has been repaid by irrigators, and \$20 million or 2.2 percent of their obligation has been repaid by municipal and industrial water users.

In 1993, the Department of the Interior's Inspector General (IG) conducted an audit of Pick-Sloan's cost allocations and repayment. In that review, the IG expressed concerns that "the present method of allocating costs did not adequately protect the government's investment." In response, Reclamation is undertaking an in-depth review of Program costs based on currently planned development, contemporary uses, and applying currently used project evaluation and economic analysis. We believe that as part of our efforts to balance the Federal budget, we are obligated to report to the Congress on the financial and economic impacts of changes in the Pick-Sloan Program. We intend to keep the Subcommittee apprised of our findings and will seek guidance and legislative authority needed to take the next step forward.

This concludes my prepared testimony. I would be happy to answer any questions you may have.

Attachment 1				
Pick-Sloan Missouri Basin Program - Irrigation Development				
Full Service Acres				
State		Planned	Developed	Percent
Montana		967,130	46,000	4.8
Wyoming		281,560	7,400	2.6
North Dakota		1,266,440	9,000	0.7
South Dakota		961,210	15,200	1.6
Colorado		101,280	0	0.0
Nebraska		989,445	229,500	23.2
Kansas		193,335	72,600	37.6
Total		4,760,400	379,700	8.0
Supplemental Service Acres				
State		Planned	Developed	Percent
Montana		346,800	28,000	8.1
Wyoming		167,400	25,200	15.1
North Dakota		0	0	--
South Dakota		11,300	8,900	78.8
Colorado		1,719	0	0.0
Nebraska		19,930	45,500	228.3
Kansas		155	0	0.0
Total		547,304	107,600	19.7

**1994 Recreation Benefits of the Pick Sloan Missouri Basin Program<sup>1</sup>**

State	Regional Benefits
North Dakota	\$68,000,000
South Dakota	\$124,000,000
Montana	\$10,000,000
Kansas	\$2,700,000
Iowa	\$14,100,000
Nebraska	\$54,000,000
Total	\$272,800,000

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<sup>1</sup>Source: Missouri River Master Manual, U.S. Army Corps of Engineers, July 1994.

**WRITTEN TESTIMONY OF WARD UGGERUD  
VICE PRESIDENT FOR OPERATIONS, OTTER TAIL POWER COMPANY  
HOUSE RESOURCES SUBCOMMITTEE ON WATER AND POWER RESOURCES  
MAY 2, 1996**

My name is Ward Uggerud and I am Vice President for Operations at Otter Tail Power Company. Otter Tail is an investor-owned utility headquartered in Fergus Falls, Minnesota. We serve over 123,000 customers in the states of Minnesota, North Dakota and South Dakota.

The purpose of my testimony is to provide the subcommittee with information and analysis concerning the Power Marketing Administrations (PMAs) in general and the Pick-Sloan Eastern Division of the Western Area Power Administration (WAPA) in particular.

While I had been aware that PMAs were providing below-market, subsidized power to preference customers, it was not until last summer that I was made aware of the greatest fraud: the PMAs were giving away free power to preference customers at the expense of the American taxpayers.

This fact was revealed during a secret meeting of preference customers that took place in Sioux Falls, South Dakota, on July 17, 1995, to which I was inadvertently invited.

I know that you will be as astonished as I was when you hear the details of this meeting. But first, allow me to provide some background information to put this story in context.

#### **A. Background**

Proposals to sell the nation's PMAs have been around since the Reagan Administration. The privatization of the PMAs makes economic sense and would provide substantial savings to the American taxpayers.

PMAs no longer carry out their historic mission of providing power to poor rural and farm areas that could not receive power through the market. Today, PMA power goes -- without regard to need or entitlement -- to any customers who, because of allocations made decades ago, happen to be served by a rural electric cooperative or municipal operation. Nothing in terms of geography or income level distinguishes the customers who receive preference power from those who do not. The truth is that PMA preference power goes to a broadly diversified mix of residential, commercial and industrial customers who are completely homogeneous with surrounding customers served by utilities who do not receive it.

As was discussed last year, PMAs are heavily subsidized by the taxpayer in a variety of ways:

**PMAs are subsidized with below-market interest rate loans and disproportionately long repayment schedules.**

- PMA's pick and choose which loans to repay, and when, leaving any shortfall with the American taxpayer to offset.
- PMA's and their preference customers are subsidized with preferential tax treatment.
- PMA rates are artificially low because they do not recover all costs of operation.

Thus, it is the taxpayer who pays the price for the discounted power that PMA preference customers receive.

As you might expect, there was significant, well orchestrated opposition to privatization efforts from PMA preference customers who have become used to their taxpayer subsidy. They continue to insist -- despite all evidence to the contrary -- that the PMA's:

- a. are well managed;
- b. recover all their costs;
- c. provide power only to truly needy and deserving customers; and,
- d. are a positive return to the U.S. treasury.

Finally, they continue to assert that privatization groups just want to raise rates for their own financial benefit.

So you can imagine my surprise when I received an invitation to the Mid-West Electric Consumers Association PMA Forum to discuss strategies to deal with privatization proposals for the PMA's.

#### **B. The Meeting**

The meeting took place in Sioux Falls, South Dakota on July 17, 1995. The primary speakers at the meeting were Alan Richardson of the American Public Power Association (APPA), Glen English of the National Rural Electric Cooperative Association (NRECA) and Jeff Nelson of the East River Power Cooperative. During the meeting I took copious notes, which are attached to my testimony as Exhibit A.

The focus of the meeting was the House-Senate Budget Resolution Conference Report, which proposed the sale of a few of the PMA's.

Alan Richardson began his comments by stressing that the collective and adamant opposition by PMA customers to any sale of PMA assets seemed to be working for now. He also stressed that there was considerable Senate opposition to any sale.

Richardson stated that the driving issue was the need for Congress to find revenue sources to help balance the budget and reduce the deficit, and that APPA and NRECA had to deal with the question of how to maintain political clout in this atmosphere. He said that most

observers believe that the status quo of maintaining government control of federal power projects cannot continue and that options that give existing customers some additional control of the projects should be explored.

Glen English echoed Richardson's comments and stated that several options should be considered, including opposing the sale of PMAs, having existing customers either lease or buy PMAs or arguing that some PMAs should be sold while others should not. English thought it would be harder to prevent the sale of PMAs in every succeeding year.

English also acknowledged the tax problem associated with PMAs, namely, that they do not pay any because of federal sovereignty. Because of this, he stated that a lease of PMA facilities may be the best option for preference customers. Under a lease, it may be possible to remain exempt from paying future taxes and there may be other benefits owing to government ownership that could be maintained.

Jeff Nelson followed English and passed out a study done by the East River Cooperative Power on the financial aspects of selling the Pick-Sloan portion of WAPA. Nelson began by stating that the Pick-Sloan power rates were the lowest in WAPA.

Then Nelson dropped the "free power" (his words, not mine) bomb. Nelson said that \$204 million of Pick-Sloan's costs were not being recovered because irrigation projects are not being built and the portion of generation construction costs allocated to these future irrigation projects is not being charged to existing power customers. Since these costs are not being recovered, the electricity production to be used for those future irrigation projects is being used now at no cost to existing PMA customers! (Exhibit A, p.6)

At first I thought that Nelson may have misspoke. But then he said it again later in the meeting. In response to a question about irrigation revenue, Nelson said the biggest issue was how to deal with the costs that are presently allocated to future irrigation projects which will never be built. He went on to say that PMA customers were getting the free use of that generation now and may not be able to get this portion for free if the PMAs are sold. (Exhibit A, p.11)

Following Nelson's presentation, a question and answer period ensued. If Congress and the American taxpayer are not surprised enough by the disclosure of the free power issue, the following statements by the preference customers indicate that they are willing to do and say anything to perpetuate their fraud on the public:

- In discussing a proposal to buy the PMAs, Richardson stated that if you can buy the PMAs for \$2.6 billion (the budget reduction figure), that is 50 percent of their net present value and it would be "a steal." (Exhibit A, p.10)

- English followed up on this point by saying that a deal for \$2.6 billion and a guarantee of no rate increases is a deal to get it for "less than it's worth" and "that's what we want." (Exhibit A, p.10)
- Richardson went on to say that \$2.6 billion is a difficult price to support politically, but "(i)t's a damn good deal if you can get it through." (Exhibit A, p.14)
- Another preference customer said that the best deal would be to buy the assets for \$2.6 billion and sell them back to the investor-owned utilities for \$9-14 billion. (Exhibit A, p.17)
- Echoing the statements of others at the meeting, another executive said that his group believes that rates can go down if the PMAs are sold because the PMAs can be more efficiently operated than they presently are. (Exhibit A, p.9)

By the end of the meeting there was general agreement that the "just say no" approach to PMA sales was not sustainable and that the group was still searching for a new, unifying position.

The Sioux Falls meeting confirmed what many already believed: that PMA customers were receiving subsidized power. More importantly, it revealed for the first time that the power was not only being subsidized, it was being sent to preference customers free of charge. The meeting also revealed a potential shift of strategy for preference customers -- from fighting to maintain the free power status quo to pursuing a sweetheart deal for the purchase of PMA assets. Either way, the preference customers remain committed to ripping-off the taxpayers.

As a result of the meeting, considerable local and national press has been aimed at this issue. Articles in The Wall Street Journal (Exhibit B) and The Fargo Forum (Exhibit C) confirmed the major aspects of what was discussed at the meeting.

Perhaps most importantly, reports of the meeting led this subcommittee to ask the General Accounting Office (GAO) to investigate the PMAs and the free power issue. The GAO has confirmed the free power scam and quantified its depth in Pick-Sloan -- over a half a billion dollars.

### C. The Disclosure Issue

While the admission by public power executives that they are receiving free power is significant, it is doubly disconcerting because any information about the transaction is missing from WAPA's financial statements. In other words, this is a phantom transaction that would not otherwise be known if not for it inadvertent disclosure at the meeting in Sioux Falls. The over half billion dollars is not captured on the documents that are supposed to keep all Americans aware of their investment -- The WAPA Annual Report and accompanying Statistical Appendix.

It is interesting to note that the PMAs are not subject to the same disclosure standards as a normal business. Thus, the two statutes that were enacted to correct the abuses that led to the stock market crash of 1929 and the financial collapse of the U.S. economy and Great Depression of the 1930's, do not apply to the PMAs. Ironically, the 1933 Securities Act and the 1934 Securities and Exchange Act were directed at protecting small, local investors by establishing a program of full and fair disclosure. Under this program, "bright sunshine" would be the prescription for curing the ills of waste and abuse wrought by those who were benefitting from such activities.

Absent full disclosure by the PMAs, many small communities who are supposed to be the beneficiaries of the PMAs did not even know they were being taken for ride -- like the investors who lost it all in 1929.

#### **D. KMPG Peat Marwick Independent Auditor's Report for WAPA**

The importance of full disclosure is highlighted by what is disclosed on WAPA's Independent Auditors Report conducted by the public accounting firm KMPG Peat Marwick.

While KMPG Peat Marwick has provided unqualified opinions on WAPA's financial statements for fiscal years 1993 through 1995, their reports on WAPA's internal control structure and on compliance with laws and regulations expose a variety of questionable practices that could have a material effect on WAPA's financial statements in the future.

The 1993 through 1995 audits showed that at various times WAPA had:

- Delivered power to customers who were no longer under contract with WAPA; and,
- Failed to test and calibrate all meters yearly, in accordance with WAPA policy, possibly resulting in the incorrect metering of electrical power charged to customers.

KMPG Peat Marwick first reported these problems in 1993 and 1994, respectively. As of KMPG Peat Marwick's 1995 audit, the problems still existed. It seems elementary that a power company should only provide services subject to an existing contract and that the meters that measure the amount of power provided should be accurate.

Continued failure by WAPA to fully address the reportable conditions could lead to an adverse independent auditors report. For a publicly traded company, an adverse report spells disaster. The Securities and Exchange Commission (SEC) would halt trading on the company's securities and the company's directors could be subject to a shareholder liability suit.

For WAPA an adverse report would obviously not have the same effect, but it would certainly undermine management credibility and call into question the viability of WAPA to manage federal assets. Of course, Otter Tail firmly believes that exposure of the free

powerscam and the stated intent of some public power executives to seek a substantially below-market deal for PMA assets already indicates that the time is right for privatization.

**E. The PMA's Are Unregulated Monopolies that are Pursuing Monopoly Practices in the Marketplace**

Would the issue of free power have escaped public scrutiny for as long as it did if the PMA assets had been owned by private regulated entities? The answer is emphatically no.

Since the inception of modern electric utility regulation, the states and the Federal government and Congress have known that the generation, transmission and distribution of electricity was a monopoly practice. As a result, private electric utilities are the most heavily regulated industry in the United States. Private electric utilities are subject to regulation over its corporate structure and business activities by the SEC through the Public Utility Holding Company Act of 1935. They are also regulated as to the rates, terms and conditions of wholesale sales and transmission access by Federal Power Act as administered by the Federal Energy Regulatory Commission. Private electric utilities are also regulated as to the rates charged to retail customers in the states in which they provide service by state public utility commissions. Finally, private electric utilities are subject to the information, disclosure and accounting requirements of federal securities laws. Such requirements provide that the disclosure of material information be fairly presented so that the American public can easily discern the activities of the business.

Multi-tiered regulation as applied to private utilities was directed at eliminating the abuses inherent in the monopoly of generating, transmitting and distributing power. Those abuses included: pricing power so low as to limit competition; disclosing only selected information associated with respect to operations so as to mislead the public at large; and obtaining services from certain corporate departments at costs that are not in line with the market.

Ironically, the PMA's are **NOT** subject to the vast majority of these laws. Indeed, the **only** law that tangentially applies is the Federal Power Act (FPA). However, under the FPA PMA's are not regulated as to the rates, terms and conditions of wholesale sales like a private utility nor are they subject to transmission regulation to the same extent as private utilities.

**1. Rate Regulation**

In 1978, the Secretary of Energy issued Delegation Order 0204-33 vesting the ratemaking authority she possessed under the various statutes described above in the PMA administrators and providing for limited FERC review.<sup>1</sup> Subsequent to initial Delegation Order 0204-33, the Secretary expanded and clarified what the PMA administrators would be required to perform and

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<sup>1</sup> 43 Fed. Reg. 60,636 (Dec. 28, 1978).

what FERC's actual review process would be in Delegation Order 0204-108.<sup>2</sup> Under Delegation Order 0204-108, each PMA administrator has the authority to develop power and transmission rates for their respective PMAs. These rates are required to be certified by the PMA administrator as consistent with "applicable law" and at the "lowest possible rate to customers consistent with sound business principles." Interim rates prior to the final FERC review are established by the Deputy Secretary of DOE. The Bonneville Power Administration is governed by a different standard.<sup>3</sup>

As noted, Delegation Order 0204-108 also empowered FERC to confirm, approve and place in effect rates developed by each PMA administrator. However, FERC's review of the rates is extremely limited and cannot replace the PMA administrator's actions.

FERC may not look "behind the numbers" in determining the extent to which the PMA administrator is in compliance with the above criteria. As FERC Chair Moler stated this past year in testimony provided to the House Resources Committee on PMAs, "[s]ignificantly, the Commission can only approve, disapprove or remand a PMA's proposed rates. Unlike our regulation of public utility rates, the Commission cannot modify a PMA's proposed rates."<sup>4</sup> Indeed, Delegation Order 0204-108 notes, "[t]he Commission shall not review policy judgments and interpretations of laws and regulations made by power generating agencies."

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<sup>2</sup> 48 Fed. Reg. 55,664 (Dec. 14, 1983).

<sup>3</sup> FERC has particular statutory authority over Bonneville's rates. Pursuant to the Pacific Northwest Electric Power Planning and Conservation Act ("Northwest Power Act"), the Commission must confirm and approve, on an interim and final basis, Bonneville's rates. Under section 7(a)(2) of the Northwest Power Act, the Commission evaluates Bonneville's rates for sales within the Pacific Northwest region to ensure the rates: (a) are sufficient to repay the Federal investment in the Federal Columbia River Power System over a reasonable number of years after first meeting Bonneville's other costs; (b) are based on Bonneville's total system costs; and (c) insofar as transmission rates are concerned, equitably allocate the costs of the Federal transmission system between all users of the system, Federal and non-Federal.

FERC also has significant authority relative to Bonneville's sales outside of the region. Under section 7(k) of the Northwest Power Act, the Commission evaluates Bonneville's rates for sales outside the Pacific Northwest region to ensure the rates are established: (a) having regard to the recovery of the cost of generation and transmission of such energy; (b) so as to encourage the most widespread use of Bonneville power; (c) to provide the lowest possible rates consistent with sound business principles; and (d) in a manner which protects the interests of the United States in amortizing its investments in the projects within a reasonable period.

<sup>4</sup> Statement of the Honorable Elizabeth Moler, Chair of the Federal Energy Regulatory Commission before the House Resources Committee on the Potential Transfer of the Power Marketing Administrations Out of Federal Ownership, May 18, 1995, Serial No. 104-28, p. 91.

In sum, rate regulation applied to public utilities under sections 205 and 206 of the Federal Power Act is not applicable to the PMAs. The 205 and 206 standard, which requires that a utilities' rates be just, reasonable and nondiscriminatory, has no bearing on the establishment of PMA rates. Because PMA power and transmission rates are not subject to evaluation under the 205 and 206 standard, the PMA administrators, oftentimes in conjunction with the preference customers, are able to establish gross assumptions for repayment and cost recovery, thereby grossly undercharging for this power. Because FERC cannot look behind the numbers, and must take the assumptions they are provided from DOE as fact, the PMAs are able to evade rate regulation.

2. PMA Transmission Facilities are Not Regulated Like Other Private Utilities

Similarly, FERC does not have the same jurisdiction over PMA transmission facilities that it does with respect to private utilities. In this respect, on April 24, 1996 FERC issued its final rule requiring jurisdictional utilities to provide open access, thereby eliminating potential transmission monopoly abuses. The rule requires that all public utilities subject to FERC jurisdiction offer transmission services that are comparable to the services they provide themselves when they use their own transmission systems to make wholesale sales or purchases of electric energy. FERC issued the Mega-NOPR in order to effectuate a competitive wholesale power market. As Chairman Moler noted in testimony last year before the House Resources Committee:

We believe that open access is necessary to eliminate existing utility practices that are unduly discriminatory and to have competitive bulk power markets in which all wholesale sellers can reach all wholesale buyers. We concluded that ordering transmission service on a case-by-case basis under section 211 of the Federal Power Act, by itself, is not sufficient to remedy undue discrimination. This is because section 211 service is not a substitute for open access, i.e., service on request. Many competitive opportunities will be lost if customers have to go through the procedural requirements of a case-by-case request.

Under existing law, FERC does not have the authority to order open access transmission by non-public utilities, e.g., the PMAs, municipal electric systems and electric cooperatives. Accordingly, PMA transmission facilities along with those owned by municipal electric systems

and electric cooperatives are not subject to FERC's comparability standard, and are effectively beyond the reach of the agency's deregulation efforts.<sup>51</sup>

The impact of this problem has been evidenced today by the disclosure of the free power issue. It is also evidenced by virtue of the fact that WAPA has begun soliciting new retail customers in the Pick Sloan region. These customers are currently customers of private utilities. It's clear from WAPA's solicitation that private utilities cannot compete with an unregulated monopoly who can price electricity far below the market.

#### **F. Conclusion**

The uncontroverted statements of public power and rural co-op company executives reporting by the media and now the GAO all confirm the undeniable fact that the PMAs are giving away free power to preference customers and the American taxpayer is paying for it.

The disclosure of this outrageous fact has been obfuscated by those who seek to perpetuate this waste and abuse on the U.S. government and upon unsuspecting local entities that may otherwise need this money for a variety of natural resource management issues. The full extent of this abuse, which may have yet to be determined criminal implications, is not altogether known. Hopefully, pending GAO reports on the other PMAs will provide more information.

What is known is that consumption of free power by certain entities is hurting local communities with viable natural resource issues that could be addressed with proper funding. By providing free power to a select few, revenues that could be benefitting state and local water resource support is being syphoned off for the exclusive benefit of others who seek to maintain the status quo.

The best way to put an end to the free power scam is to put an end to the PMAs. The PMAs no longer operate according to their historical charter or in the best interests of the nation. Privatization offers a positive fiscal result for the American taxpayer, and current customer services will continue under new, private ownership.

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<sup>51</sup>The PMA's are subject to FERC's § 211 authority, and reciprocity provision. However, as noted above FERC does not believe that § 211 is adequate to resolve monopoly abuse. As to reciprocity, this requirement is only triggered if the PMA's were to seek access over another private utilities transmission system.

**PMA Forum  
Sioux Falls, South Dakota  
July 17, 1995**

Primary speakers at the forum were:

Alan Richardson - APPA

Glen English - NRECA

Jeff Nelson - East River Power Cooperative

A special PMA Hotline has been set up for PMA customers to provide up-to-date information on the status of this issue. The number to call for this information is: **303-296-2122**.

Introductory Comment:

The Conference Report which requires a \$2.6 billion budget reduction provides the basic framework under which a resolution of the PMA issue must be developed.

**Comments by Alan Richardson - APPA**

1. One of the questions that should be posed to Congress is why should revenue producing assets be sold.
2. The House Resources Committee, chaired by Rep Doolittle (Ca.) has introduced legislation which has two separate mechanisms contained in it.
  - A. It has been proposed that the assets of the SEPA should be sold at auction to receive a market determined price.
  - B. The Central Valley Project in California, however, is proposed to be sold at a price reflecting the remaining value of the debt to existing customers. This proposed treatment of the Central Valley Project by Chairman Doolittle gives an indication that there is sympathy for giving preferential treatment to existing customers. If further suggests that Congressmen are continuing to show preference for their own constituencies.
3. The Senate hearings which were held last week went well and there was little introduced which gave cause for concern as to how the sale will be handled.
4. Senator Murkowski, chair of the Senate Energy Committee, has proposed an option which would add a 5 mill surcharge to existing rates which would raise an additional \$2.6 billion in annual revenue. The current sentiment in the Senate is to not sell the PMAs.

5. The collective and adamant opposition expressed by PMA customers against the sale has been working. The Baucus - Pressler Amendment is an indication that the Senate has heard the arguments of opponents to the sale and is currently inclined to not sell the PMAs.
6. TVA is currently fully funded by customers except for \$140,000,000 which is appropriated for irrigation components of the TVA project.
7. Scott Klug offered an amendment to strip that \$140,000,000 from the appropriations bill. A vote on the Klug proposal was defeated 184 to 284 which gives further indication that Congress is willing to consider continued preferential treatment to existing PMA customers.
8. The driving issue is the need for Congress to find revenue sources to help balance the budget and reduce the deficit.
9. One of the important questions to deal with is how do we propose to hold onto the political clout that we presently have.
10. Dollars will become more and more important as Congress tries to deal with the deficits and balanced budget requirements and this will make continued favorable treatment for PMA customers more difficult..
11. The PMAs may become more important targets later as financial considerations become more predominant and the options for additional revenue become stickier.
12. Most people believe that the status quo of maintaining government ownership of the federal power projects can't continue in the long term.
13. PMA customers want more local control of the PMAs.
14. We should look for options that give existing customers some additional control of the projects.

Comments by Glen English - NRECA

1. The original observation in Washington that the sale of the PMAs was a done deal. Democratic president had proposed the sale to a Republican Congress and the Republican party has advocated the sale for years under previous Republican administrations.
2. Originally the biggest concern was how to prevent an auction to the highest bidder in an auction process and how to keep the PMAs for existing customers.
3. This issue is one that has come up once a decade.
4. Now we believe that we have reached the point where there is little of auctioning the PMAs to IOU's at market prices. The present feeling by most in Congress is that the PMAs should be sold to existing customers and net present value.
5. Opportunities have been created in this debate which have therefore opened new doors.
6. It is like a dog, however, that chases a car. What do you do when you catch it?
7. The options that now exist include:
  - a. Oppose the sale of the PMAs
  - b. Have existing customers purchase the PMAs
  - c. Have existing customers lease the PMAs
  - d. Argue that some PMAs should be sold while some should not.
8. The Senate is friendly to the PMAs.
9. The House may be intimidated by Senate votes which have expressed opposition to the sale of the PMAs.
10. Senator Murkowski says the PMAs will be sold, but maybe not this year.
11. We could maybe succeed in blocking the sale this year. The question is - can you fight this fight every year?
12. It will become harder to prevent sale in every succeeding year.
13. The PMAs may need to provide a greater sum of money the next time this issue comes up.

14. IOU offers will become more attractive to Congress in the future as Congress looks for more and more ways to bring in more and more money.
15. Abolishing the DOE will hurt the proponents of maintaining the PMAs as is.
16. Approximately 1/3 of the DOE employees work directly with the PMAs. There are substantial savings available to Congress in eliminating these employees from the federal payroll. Loss of these DOE employees will reduce number of people in the government opposed to sale and elimination of these jobs will reduce the number of people arguing our case in front of Congress.
17. Even if Congress doesn't move to sell the PMAs, it may ask to raise electric rates and derive more revenue from the sale of electricity.
18. Arguing to oppose the sale of the PMAs at this time won't end the struggle.
19. Proposals to divide up the PMAs and sell them on a project by project basis would be disastrous. Unity and support for a common proposal among all customers must be maintained.
20. The strategy must be to keep PMAs intact.
21. Water management is at risk if PMAs are bought by preference customers as the decisions for water management will then be made by entities who have less of an interest in the electric operations of the PMA facilities.
22. The key strategy is to convince Congress that there shouldn't be any rate increases associated with the sale of the PMAs.
23. The question of taxes will be a problem. Presently the PMAs pay no taxes because of federal sovereignty. If the PMAs are sold, this sovereignty will be lost and taxes will likely have to be paid.
24. A lease of the PMA facilities may be the most attractive option. Under a lease, it may be possible to remain exempt from paying future taxes and their may be other benefits owing to government ownership that may be maintained.
25. A lease now may not prevent a sale in the future.
26. Leasing the PMAs may make funding for maintenance a problem.

27. It is possible that some PMAs may be sold.
28. Congress realizes WAPA is unique because of the complexity of its contracts that are in place as compared to those at other PMAs.
29. We should ask, does WAPA become more vulnerable if other PMAs are sold?
30. We must look for the options that are the most acceptable and attractive.
31. The decision on what to do must be made quickly and there will be no turning back once the decision is made.
32. Congress will decide what to do on this issue after Labor Day. We must work hard in August to develop a recommended proposal.
33. We must find a champion in Congress to propose our recommended option.
34. We must accept the fact the you can always expect the unexpected in Congress.

**Comments by Jeff Nelson - East River Power Cooperative study**

**Note:** Jeff passed out a study done on the financial aspects of selling the Pick-Sloan portion of WAPA. This handout is attached to these notes from the forum.

1. The Pick - Sloan project is the most complex of all the WAPA projects.
2. The Pick - Sloan rates are the lowest in WAPA.
3. Basin Electric Power Cooperative has prepared a valuation study of the Pick-Sloan Project.
4. The valuation study calculates a purchase price that is based on establishing a price that would yield the government an initial amount of revenue equal to the revenue stream of the generation at current rates.
5. The Dakota Conservancy District believes generation revenues should pay for irrigation projects. This isn't currently happening and could cause rates to rise if this were required.
6. \$204 Million of costs are not now being recovered because the irrigation projects aren't built and the portion of the generation construction costs allocated to these future irrigation projects is not being charged to the existing power customers. Since these costs aren't being recovered, the electricity production to be used for those future irrigation projects is being used now at no cost by existing PMA electric customers.
7. Even if the PMAs are sold, it may be possible to avoid paying Federal taxes. If the PMAs are sold, it is unlikely that state taxes can be avoided and this additional tax liability could amount to perhaps \$45 million per year.
8. Operational priorities will become a problem if the PMAs are sold.
9. Another threat for continued preference to PMA customers is that Native Americans are asking for 100% of their power from Federal resources.
10. Another threat to the continued allocations for existing customers is that State and Federal customers who serve a public purpose (schools, state and federal offices, etc.) are asking that their power come from the federal power projects as all of their operating expenses are supported by general tax revenues and are paid for by all citizens.

11. If the PMAs are sold, existing customers would lose their walk away privilege which allows them to leave without any residual obligations. Under a purchase, they will have to be some continuing liability on someone's part. Perhaps a lease could reduce the amount of liability that would be created under a purchase.
12. Selling the PMAs would result in the loss of Federal sovereignty and it would likely cause additional tax liabilities.

**Questions and Comments:****1. Tom Heller - MBMPA**

1. MBMPA provides supplemental power to 58 municipal preference customers.
2. The allocation of this preference power is made to the municipals and not to MBMPA as a separate entity.
3. MBMPA urges everyone to stay together and be unified in this issue.
4. 60% of the electricity consumed by the MBMPA customers comes from WAPA allocations.
5. We should rely on APPA and NRECA to develop our positions and argue them for us in Washington.
7. Our primary focus should be to protect consumers from any rate increases.
8. MBMPA believes that the Federal Government won't continue to be in the power supply business and that some change is imminent.
9. The question we have is how can we reduce our risks in this matter?
10. We cant just say no anymore. The sentiment to sell the PMAs is too strong and the strategy of just plain opposing the sale isn't likely to work forever.
11. MBMPA's position is to let APPA argue the issue on our behalf.

**2. Mark Glaess - MN Rural Electric Association**

1. BPA rates have gone up. In part this has come about because of additional costs associated with environmental law, particularly the Endangered Species Act.
2. What effect will the Endangered Species Act have on our WAPA rates? A transfer of ownership won't effect that liability. We will be no worse or no better off than we would otherwise be.
3. Glen English responded by saying that liability for endangered species costs should go to all citizens and not just to those who get power from the PMAs.

**3. Debbie Levine - California**

1. Debbie represents the Desert Southwest Group.
2. Debbie supports acquiring the assets by purchasing them outright.
3. The Desert Southwest Group is currently having some disputes with WAPA.
4. The Desert Southwest Group wants more local control.
5. If we don't buy the PMAs now under favorable terms and conditions, the option of doing that may be taken away in the future.
6. If we don't have agreement in this group on how to proceed, the Desert Southwest Group will move on its own.

**4. Mark Mitchell - Ex. Dir. of Arizona Power Authority**

1. Our biggest strength is to move forward together and support a common proposal.
2. We definitely have an opportunity now to gain control of the PMA assets.
3. The Hoover Group is working on a purchase option.
4. We would prefer a lease over a purchase as a way to provide more insulation from the liabilities we would incur if we purchased the PMAs.
5. We think that we could seek preferential terms in a lease and then guarantee that those rights continue for a possible future purchase.
6. A lease now, instead of a purchase, could avoid future liabilities.
7. The Arizona Power Authority believes that rates can go down because the PMAs can be operated more efficiently than they presently are.
8. Under a lease, it may be possible to avoid paying both state and federal taxes as is presently the case.

**Reply by Glen English**

1. The biggest decision to make is not whether to lease or buy but rather do you want to do one or the other of these as contrasted to just categorically opposing a sale.
2. You can't break the PMAs into pieces. If you divide them up you will have all sorts of problems.

**Reply by Jeff Nelson**

1. East River holds the largest WAPA allocation in the Pick-Sloan Project.
2. We feel that we absolutely need assurance of having no rate increases regardless of what happens.
3. The discussions in Congress, however, only talk about protection on the amount of rate increases and they don't deal with a prohibition on any rate increase.

**Reply by Alan Richardson**

1. It is the IOU's that are talking about providing the protection of limiting rate increases. We should be arguing that there should be no rate increases at all.
2. If you can buy the PMAs at \$2.6 billion, that is 50% of their net present value, that's a steal.
3. If you pay anything more than that, there will have to be a rate increase.
4. We're faced with a very tough situation. The Federal Government needs money.
5. Just saying no has been our rallying cry in the past.

**Reply by Glen English**

1. The issue of what represents a zero rate increase is for APPA and NRECA to define.
2. Requiring that there be no rate increase is the argument we can use against the IOU proposals.
2. When we argue to get it at \$2.6 billion and for no rate increase, we're arguing to get it for less than it's worth. That's what we want.

**6. Dale Van Erter - Mayor of Sioux City Iowa**

1. Sioux City is a MBMPA customer.
2. Question: "Is there any revenue available from irrigation?"

Answer: Jeff Nelson: "Irrigation revenue would be based on ability to pay. 85% of irrigation cost must come from power sales. Irrigation can't be counted on to raise revenue."

**Reply by Jeff Nelson**

1. The bigger issue here is how to deal with the costs that are presently allocated to future irrigation projects which will never be built. We are getting the free use of that generation now and may not be able to get this portion free if the PMAs are sold.
2. A lease option may be a way to minimize the liability of picking up those costs which are now deferred to future and uncertain irrigation projects.

**7. Walt Canney - General Manager, Lincoln Electric System (Nebraska)**

1. Question: "What concept of governance would be contemplated?"

Answer: Glen English: "This will be a tough issue. I envision that it will involve equal representation from coops and municipals and that it will not be based on current allocations. I won't accept governance based on allocation amounts."

**8. Frank Knudson - Tri State G&T**

1. I am concerned about the amount of past rate increases from WAPA.
2. Customers need to get control of PMA assets to prevent future rate increases.
3. We better move quickly to get a good deal while we can.

**9. Gill Hanson - KEMA (Kansas)**

1. There are 39 cities on the KEMA system.
2. We should develop a strategy to keep unity among us.
3. KEMA doesn't want to make a decision now on whether to buy or lease.
4. If we make a decision today to buy or sell, that is an irreversible decision and could cause us regrets in the future.

**Reply by Glen English**

1. If you want to preserve your options till a later day, you may lose your flexibility and it may winding up costing you more. There's no looking back after September 1. If you don't want to move forward with a purchase or a lease then you have also chosen an irreversible position.

**Reply by Gill Hanson to Glen English**

1. How can you make a decision if you don't know what it will cost?

**10. Greg Sherman - Marshall, Minnesota**

1. Question: "Wouldn't the IOU's have the same environmental risk if they were to purchase the PMAs?"

Answer: "Yes they would, but the IOU's will just pass those environmental costs on to their customers."

2. The purchase price in the future will be much higher than what we might be able to get now.

**11. Howard Johl - Kimbleton (MBMPA Customer)**

1. The PMAs will likely be sold sometime and the cost will go up later so we might as well buy them now.
2. Together we can win this thing, if we're separated we fall.

**12. Harold Skybahl - Sioux City Iowa (President of MBMPA)**

1. We have a window of opportunity now to get a good deal.
2. If the IOU's buy the PMAs, they will charge us 3-4¢/kwhr for the power.

**13. Bob Martin - Rushmore Electric, Rapid City**

1. Question: "Are we talking about buying WAPA or are we talking about buying all the PMAs?"

Answer: Alan Richardson: "There must be unity among all of the PMAs as to what approach to use. We likely can't do one thing for one PMA and something different for another."

Answer: Glen English: SEPA and SWPA are already very unified.

**14. Bryan Jobson - Sacramento Municipal Utilities District**

1. SMUD is the largest WAPA customer of all.
2. We would be more comfortable if we had a written proposal to look at.
3. We are concerned about the economic and political risk if we make a decision to buy now.
4. The risks in buying the PMAs must be quantified.
5. Each project must be treated separately.
6. We need to begin by discussing these proposals with Congress and the Administration.
7. We have been taking the high ground of protecting our customers from any rate increase. That strategy that will be lost if we make an offer to buy the PMAs only to have the IOU's bid it up.
8. SMUD definitely wants a project by project treatment.
9. We insist that this not be a one size fits all proposal. We want more local control than we now have.

**Reply by Glen English**

1. It would be nice to be able to lay a specific proposal on the table but the problem is politics don't allow this.
2. This thing will likely change as it moves along. You're going to have to trust us at APPA and NRECA to develop and advance this.
3. We will try to minimize risk by limiting liability.

4. The key to this must be to keep it as simple as possible.
5. We must argue that the IOU's will raise rates and that any rate increase is unacceptable.
6. This deal must be based on the premise that the status quo needs to be preserved.
7. The Pick-Sloan rates can't be changed without legislation.

**15. LeRoy Neubauer - Valley City**

1. Valley city is one of the ND Municipals and is very dependant on the WAPA preference power to maintain low rates.
2. The rates for Valley City could double under a sale at market based prices.
3. We must buy WAPA now to preserve our low prices.

**16. Harris Davis - Sioux Valley Electric, Sioux Falls**

1. Question: "Will the sale of the Alaska Power Authority give us any guidelines on how the sale of other PMAs might go?"

Answer: "No. In Alaska the state is involved in the purchase and there are no IOUs that have been involved in any way. The Alaskan Power Authority sale has taken over 10 years to put together. We won't have that much time and this deal will be much more complex."

**17. Jeff Nelson - East River**

1. Question: "Can we really expect to be able to buy the PMAs for \$2.6 billion?"

Answer: Glen English: "There are a lot of Pigs in the Poke on this one. That is to say that there are a lot of things that could come up that we don't know about now."

Answer: Alan Richardson: "I don't think the \$2.6 billion price will hold. \$2.6 billion is a difficult price to support politically. It's a damn good deal if you can get it though."

## 18. Jeff Genser - law firm - Duncan Weinberg Keller

1. There are no guarantees in any of this.
2. Congress is very budget driven right now and they are likely to look for any sources of revenue that they can find.
3. KISS (Keep it Simple Stupid) may or may not work. There are other things that may come in to play here.
4. Senator Murkowski has said that the sale is not likely to happen this year.
5. Bob Nordhaus has presented testimony that has stated that the sale of the PMAs should yield \$4.47 billion.
6. Scott Klug will insist, at a minimum, on at least getting the amount that Nordhaus has testified to.
7. Representative Schaefer, Colorado, will propose withdrawing the sale of petroleum from the federal petroleum reserves. If this happens, one of the other revenue options will be removed and Congress could look to the PMAs for even more money.
8. The final budget recommendations will be budget driven and some of these other issues may be difficult to argue.
9. The only thing we know is that Congress needs to raise a lot of money.
10. Proposing a sale is risky because once you agree to the sale, you won't be able to control the issue anymore and you may get others wanting a chance to buy it.
11. Watch closely what happens to sale of petroleum reserves, that could be an indication of how badly Congress may need to get money out of the PMAs.
12. Opening up the ANWR is an alternative to PMA sale, but Clinton would likely veto it. If ANWR were opened, though, that could raise a lot of money and maybe there would be less pressure to sell the PMAs.
13. You have to give your national associations wide latitude in developing this issue.
14. You have to stay unified or you will lose much of your political force.

**Reply by Glen English to Jeff Genser**

1. Don't get hung up on the numbers, whether it's \$2.6 billion or not, or how feasible it is.
2. The question isn't so much the number as it is "Do you want to buy the PMAs or do you want to continue saying, Hell no, we don't want them sold. Where do you want to go?"
3. As to price, if the price goes above \$2.6 billion, then the horse is out of the barn and you won't be able to preserve the sale for the existing customers. You have to argue that \$2.6 billion is the absolute highest price because anything more will result in a rate increase and any rate increase must be resisted.
4. Our strategy should be to argue for a quick sale at \$2.6 billion and get the President's support by providing him the an opportunity to declare a victory. He can say that he proposed selling the PMAs and that he has accomplished it and has gotten the government out of the power business. Everybody should be happy.
5. The price will get settled politically and we should develop a moral high ground position to insist on a sale to current customers at a price that will result in no rate increases. That number is \$2.6 billion and we have to justify the rightness of the number on the philosophical reasons, not the financial details.

**19. Leslie James - Manager Contracts, Salt River Project**

1. The SRP owns the Navajo contract - Not the U.S.
2. Navajo is not for sale because Salt River has it tied up. Regardless of what you may hear to the contrary, the Navajo project is not a part of any of these discussions.

**20. Craig Osbrock - Brookings, South Dakota**

1. We have to yield to our national organizations and let them represent us.
2. This country seems to have a love affair with deregulation. Deregulation is being promoted by big business interests and not by the customers or by customer interests.
3. We must argue that competition isn't necessarily good.
4. The IOU's will keep up the attack on us and we must try and keep them off our back.
5. We should argue for owning or leasing and we should drop our position of just being opposed to any sale.

**21. Denny Valentine - NPPD**

1. The best deal would be to buy the assets for \$2.6 billion and then sell them back to the IOU's for \$9-\$14 billion.
2. We would like to see the numbers associated with the options.
3. We would like to see a group to get together and develop numbers and a strategy.

**Reply to Denny Valentine by Glen English**

1. We don't have the time. This has to get put together in August. We need to know today what we should do.
2. Our options are the following:
  - a. Continue to say no and fight it to the death.
  - b. Offer to buy the PMAs.
  - c. Put together a lease proposal.

**22. Dennis Hill - North Dakota Association of Rural Electric**

1. We started out in the beginning by just saying, "Hell no."
2. What has happened? Have we lost ground? We didn't used to talk about anything except flat out opposition to a sale.
3. Byron Dorgan has said, "Hell no, it won't go." He has led the fight for us in Washington and has done a good job of keeping up the opposition to a sale of any kind. We can't let Dorgan down and turn around now and say "OK, I guess we have decided to buy it." It's a matter of principle. Until we're convinced there are no other options except a purchase, we can't decide to go ahead and do this.

**Response from Glen English to Dennis Hill**

1. Either we support Doolittle's proposal or offer an alternative.

**23. Gerald Oberg - McClain Electric**

1. 40% of our power comes from WAPA.
2. We're opposed to throwing in the towel. We'd like to continue to oppose the sale.
3. Does anybody know what the remaining life of dams is?

**24. Dan Boyce - East Grand Forks, Minnesota**

1. 60% our power comes from WAPA..

**25. Al Crowser - Alexandria, Minnesota**

1. 50% of our power comes from WAPA.
2. We need more local input in developing alternatives.

**26. Bryan Jobson - Sacramento Municipal Utilities District**

1. Maybe we should be ready to buy - but we shouldn't offer to do so until we know more.

**27. Steve Brevig - NIPCO - Iowa**

1. Should this group meet again if necessary?

**28. Dennis Hill - North Dakota Association of Rural Electric**

1. Our direction can't change based on this meeting.
2. I don't have the authority from my board to make any decision here and none of the others has the authority to speak for their organizations

**29. Ron Mortenson - OPPD**

1. Only 5% of our power comes from WAPA.
2. We can't just sit on our hands, we have to do something.

**MID-WEST ELECTRIC CONSUMERS ASSOCIATION****PMA FORUM***Water and Power Marketing Committee Report***Issues**

- System Value
- Customer Acquisition-Financing
- Suballocated/Joint Costs
- Ultimate Development
- Unfinished Irrigation
- Taxes

**System Valuation Studies [Pick-Sloan]****•Assumptions**

- Purchase occurs at 12/31/98
- “Drought” deficits at \$28 million (Currently \$175 million)
- No suballocated costs
- No incomplete irrigation costs
- No “ultimate development”
- PRS replacement/additions through 1998
- PV includes principle, interest and “booked” aid to irrigation

**•Results @ PV of:**

- 6% — \$1.343 bil
- 7% — \$1.217 bil
- 8% — \$1.112 bil
- 9% — \$1.023 bil
- 10%— \$0.948 bil

**System Rate Impact—Financing****•Assumptions**

- 85% debt/15% equity financing
- Acquisition cost \$1.112 bil (8% PV)
- Interest on debt: 7.225%
- Equity value: 6.5%
- 30 year repayment
- O&M same as PRS

**•Results**

- Decrease of \$8 million/year or -0.8 mills/kwh

### Suballocated/Joint Costs

•Power investments “set-aside” (suballocated) in anticipation of future federal irrigation development along with “sunk” (existing) investments in common facilities now allocated to irrigation (joint costs)

- Suballocated costs — \$300 million
- Joint irrigation costs—\$120 million
- Total — \$420 (@0% interest)
- 350 MW (currently marketed as firm)
- Potential Rate Impact
  - 0-3.8\* mills/kwh (0 to \$38 million/year)
  - \*25 years @ 7.8% interest

### Ultimate Development

- Commitment of power revenues to aid in federal irrigation project repayment
  - Current: \$725 million
  - Future: \$5.9 billion
- Potential rate impact
  - 0 to ?
  - Political vs. economic issue

### Unfinished Irrigation

- Funds appropriated for the uncompleted Garrison Irrigation Project which is currently “outside” repayment obligation—\$133 million plus \$71 million in several other unfinished projects
  - \$204 million
- Potential rate impact (Garrison)
  - 0 to 1.3 mills/kwh (0 to \$13 million/year)

### Taxes

- Depending on the form of ownership federal taxes may be applied and state property taxes will be applied
- Potential rate impact
  - Assuming a \$1.5 billion “taxable” base and equivalent of 3% property tax rate:
    - \$45 million/year
    - 4.5 mills/kwh
  - Federal taxes: ?

### Summary of Financial Issues

	Annual Impact	
	\$(millions)	Rates(mills /kwh)
Financing	(\$8)	(.8)
Suballocated/ Joint Costs	0—\$38	0—3.8
Ultimate development	0—?	0—?
Unfinished irrigation	0—\$13	0—1.3
Taxes	\$45	4.5
Total	\$(8)—\$96	(.8)—9.6

**Other Key Issues**

- Competing operational priorities
- Native Americans
- State/Federal customers
- Insurance/liability
- Loss of current “walk-away”
- Federal Sovereignty

## Mid-West Electric Consumers Association

Paul Neal  
President

Eric Slong  
Vice President

Dwain Zinke  
Secretary-Treasurer

June 20, 1995

Thomas P. Graves  
Executive Director

Dear Pick-Sloan Customer:

The United States Congress continues to consider whether or not to sell the Western Area Power Administration and other federal Power Marketing Administrations. Both the Senate and the House Budget Resolutions call for sale of the PMAs; but the Senate also included an amendment opposing sale of the PMAs. Conferees are meeting to resolve differences between the two versions. The authorizing committees are just beginning to consider issues associated with sale of these valuable federal assets. Numerous bills have been introduced calling for the sale of the federal Power Marketing Administrations.

On July 17 at 1:00 p.m. in Sioux Falls, the Mid-West Electric Consumers Association will be convening a special meeting of all Pick-Sloan consumer-owned electric utilities to discuss and consider actions in Congress relating to the PMA's. The meeting will be convened at the Howard Johnson Hotel at 3309 West Russell. We will adjourn that afternoon. For those needing room reservations, the number at Howard Johnson's is 605-336-9000.

The purpose of the meeting is to provide a forum for Pick-Sloan customers. We will be updating you on the status of PMA activities in Congress, and the prospects and process for congressional action. We will be devoting a good deal of time to discussions so that we may better address the concerns and perspectives of Pick-Sloan customers. We have invited our national associations, APPA and NRECA, to attend as well.

Everyone has too many meetings these days, but it is important for you to attend this session. If we are to succeed in protecting our interests, we must maintain the unity that has served the Missouri River basin so well for so many years. To maintain that unity we must work together in understanding the nature of the issues confronting us and deciding upon a course of action that is in the best interest of all.

If you will be attending this Pick-Sloan forum, please return the enclosed response for as soon as possible so that we can finish planning the logistics for this meeting. We look forward to seeing you in Sioux Falls.

Sincerely,



Thomas P. Graves  
Executive Director

## Electric Co-Ops and Municipal Utilities Seek to Buy U.S. Assets at Bargain Price

By BENJAMIN A. HOLDEN

Staff Reporter of THE WALL STREET JOURNAL  
Groups representing member-owned electric cooperatives and municipal utilities have devised a plan to buy federal power assets for less than one-third of their market value, which studies put at \$9 billion or more, according to an executive familiar with the plan.

At a July meeting in Sioux Falls, S.D., executives of the American Public Power Association and the National Rural Electric Cooperative Association outlined a \$2.6 billion bid for three of the five Power Marketing Administrations operated by the Department of Energy, says a utility executive who attended. The five agencies own hydroelectric dams and transmission lines that crisscross the country and generate 6% of the nation's power.

In the spring, the Clinton administration announced as part of its 1996 budget a plan to sell three of the power agencies for \$3.7 billion. The power associations oppose selling the assets to anyone but the customers of the agencies, namely their organizations' members. They argue that investor-owned utilities, if permitted to buy the agencies, will raise rates to recoup their investments. Investor-owned utilities support selling the agencies, but argue the government can realize the full value of the assets only through competitive bidding.

The government hasn't decided what form the sales will take. But the associations' idea of a so-called preference sale carries weight because their members buy the bulk of the agencies' power. The associations argue they thus have a quasi-ownership interest in the power assets. Indeed, a fourth agency in Alaska appears to be on the verge of being sold, without bidding, to its customers.

The National Rural association criticized the Clinton plan as "an open invitation to investor-owned utilities to raise the

electric rates of America," and in a recent policy paper on the matter, the American Public association said it "strongly opposes" the sale of the agencies to anyone other than the existing customers. Neither group returned repeated phone calls seeking comment on the matter.

"Their argument is 'We've paid for them, therefore we own them,'" says Rep. Scott L. Klug (R., Wis.), head of the House Privatization Task Force. "But when I pay my bill at Wisconsin Power & Light, they don't send me shares of stock and say thanks for buying our electricity."

Opponents of preference sales were less kind upon hearing of the proposed bid. "This is outrageous," said Tom Kuhn, president of the Edison Electric Institute, the investor-owned utilities' trade group. "They're asking for a raid on the American treasury."

The investor-owned utilities press this argument by pointing to about 10 competing studies on the value of the assets put together by various Washington government and lobbying groups. The studies value the assets at \$9 billion to \$14 billion.

"I think \$2.6 billion is off by a factor of four," said Ward L. Uggerud, a vice president at Otter Tail Power Co., based in Fergus Falls, Minn. "It's a fire sale."

Otter Tail is among the handful of investor-owned utilities that have attempted to demonstrate the money-raising potential of the power agencies by lobbying in actual bids. Earlier this year, Tucson Electric Power Co. offered about \$550 million for the Arizona-based assets of one of the agencies.

Rep. Klug said the pending \$77 million sale of the Alaska Power Administration, is "a done deal" and should be completed soon. The tentative no-bid deal was reached last month with the city of Anchorage and the agency's customers.

Rep. Klug says he favors competitive

sales in some cases. "Each [power agency] may be treated differently," he said. "Some should be leased, some sold to preference customers, some to investor-owned utilities. But to say we're going to put them in a bloc and sell them to preferential customers at fire-sale prices is absolutely nuts."

But no matter how they are done, the sales must go ahead, says Rep. Klug. "Twenty-eight percent of the DOE does nothing more than run" the power agencies, he said. "If you're going to do any [dismantling of] the Department of Energy, the [agencies] have got to go."

Exhibit C.

# The Forum

SUNDAY, MARCH 17, 1996

FARGO-MOORHEAD

## Cheap hydropower vs. big water development?

**What is WAPA?**  
The Western Area Power Administration sells and transmits federal electric power in 15 western states. It is one of five federal power marketing administrations, or PMAs, under the Department of Energy.

In WAPA's Missouri Basin Eastern division, eight hydroelectric dams generate 5.9 million megawatt hours of electricity a year. It provides power for 190 municipalities and 24 umbrella rural electric cooperatives in North Dakota, South Dakota, Minnesota, Iowa and Nebraska.

**What is Otter Tail Power Co. proposing?**

- ▶ Otter Tail wants to take over management of WAPA's Eastern Missouri Basin system for five years for a pilot study to establish guidelines for the eventual sale of the five PMAs to private investors. It would receive \$10 million yearly for the study.
- ▶ Otter Tail advocates raising rates for municipal and rural electric cooperatives receiving public hydropower — an average of 25 to 30 percent for municipal customers, 5 percent for rural electric customers.
- ▶ Rates would decrease for farmers, American Indians and government customers.
- ▶ The higher rates would generate added revenues of \$102 million a year. North Dakota would have a claim on \$20 million a year to pay for water development for irrigation projects never built.

## HE JZZ



**Bruce Furness, Fargo Mayor:**  
"We're interested in anything we can do to solve our water problems in the future."

**Sen. Byron Dorgan, D-N.D.:**  
"This is a utility company that wants to raise electrical rates for people."

**Ward Ugerud, Otter Tail Power:**  
"Washington doesn't have \$500 million to give away for water projects."

**Ben. Kent Conrad, D-N.D.:**  
"If they did get that money lined up there'd be a lot of people there to snatch it."

Sources: WAPA, Otter Tail Power Co. DAWN BREHM / The Forum

# Untapped potential?

Otter Tail Power says hydropower savings could end N.D.'s water problems

Making people pay for 'free power' key, says power company

By Patrick Springer  
The Forum

North Dakota's dream of piping Missouri River water to the Red River Valley has failed to materialize for many reasons that largely boil down to one big reason: lack of money. Otter Tail Power Co. is floating a proposal it says would raise \$20 million a year for water development in North Dakota without raising taxes. The catch: Thousands of electricity customers — primarily municipal power consumers — in a six-state region would pay more for public hydropower generated by Missouri River dams.

Much more, in some cases.

Rates would jump 27 percent in Moorhead, for example, and 35 percent in Valley City, N.D., under the Otter Tail proposal for managing federal hydropower in a region including North Dakota, South Dakota and western Minnesota.

Overall, however, the rate increase would be about 5 percent, Otter Tail says. And rates for farmers and American Indians would not go up.

The utility argues that boosting public hydropower rates is a more realistic funding source for water development than asking money from a Congress struggling with deficits.

"The plain and simple fact is Washington doesn't have \$500 million to give away," says Ward Uggerud, Otter Tail's vice president of operations.

"One of the reasons there's a water problem is nobody has been able to figure out how to fund it," Uggerud says. Taxpayer subsidies hold hydropower costs well below market rates, Otter Tail and others argue.

"We're not the only ones who are saying that," Uggerud says. "The Inspector General says the same thing."

The Inspector General for the Department of Interior determined in 1993 that one quarter of the investment for power features of the Missouri Basin system was allocated to irrigation projects that never will be built, including Garrison Diversion.

Until the costs are made the responsibility of the electricity rate payers, taxpayers will continue paying \$2 million annually for operation and maintenance costs. Taxpayers pay another \$30 million annually in interest to finance \$382 million in costs, the Inspector General concluded.

## Debt disagreement

Two-thirds of the \$2.6 billion it cost to build the Pick-Sloan Missouri Basin Project remains unpaid, 47 years after the power system went into service, Otter Tail says. Hydropower customers disagree; they say 40 percent of the debt has been paid.

On average, Western Area Power Administration's (WAPA) Missouri Basin has paid annual interest rates of just 1.6 percent, Otter Tail maintains. At that rate it would take 150 years to retire the project's debt, Uggerud says.

"There are no unrecovered costs," says Tom Heller, general manager of Missouri Basin Municipal Power Agency in Sioux Falls, S.D., which sells hydropower to 58 municipalities, including Moorhead and Valley City. "The interest rate is actually higher than they have indicated."

In essence, Otter Tail says its plan would end subsidies for abandoned irrigation power, requiring customers to pay the true costs — and generating additional revenues of \$102 million a year for the federal treasury.

## Payoff for N.D.

North Dakota would have a legitimate claim to one-fifth of that amount, Otter Tail says. That's because the state was slated to receive one-fifth of promised irrigation acres from water projects never built, Uggerud says.

That's not a good swap, Sen. Byron Dorgan, D-N.D., says.

# WAPA customers

## NORTH DAKOTA

### Municipal Customers

- Cavalier
- Grafton
- Hillsboro
- Hope
- Lakota
- Maddock
- Northwood
- Park River
- Riverdale
- Sharon
- Valley City

### Cooperative Customers

- Basin Electric Power Cooperative
- Capital Electric Cooperative
- Central Power Electric Cooperative (Includes allocation for MAFB)
- KEM Electric Cooperative
- Minnesota Power Cooperative (Includes allocation for GFAB)
- Moor-Gran-Sou Electric Cooperative
- Oliver-Mercer Electric Cooperative (Includes allocation for Stanton Municipal)

### State of North Dakota

- Grafton State School
- McLean-Sheridan
- N.D. Mill & Elevator Assn.
- N.D. State School for the Deaf
- N.D. State School of Science
- N.D. State Hospital-Jamesstown
- N.D. State University-Bottineau
- N.D. State Water Commission
- University of North Dakota-Grand Forks

Source: WAPA

"This is a utility company that wants to raise electrical rates for people," he says. "I guess that's the business they're in."

Dorgan was a leader in a fight last year in Congress to block proposals to sell the federal power systems, including WAPA, which includes the Missouri Basin projects.

Otter Tail wants to manage WAPA's Missouri Basin power system during a five-year pilot project. It would study ways to ease the transition of selling the federal power systems to private investors, an idea Congress rejected last year.

"This is just a masquerade costume," Dorgan says. "What they've done is put a new costume on a proposal that's tired and worn out and long buried and trotted it out again."

The Otter Tail proposal faces formidable challenges, says Sen. Kent Conrad, D-N.D.

"We've not had a chance to evaluate the full implications, but I've got to say to you that I think it is highly unlikely that what they've proposed here would ever come to pass," Conrad says.

"They would be taking on so many constituencies in so many parts of the country that any objective view is that it's unlikely to happen," he says. "And if they did get that money freed up there'd be a lot of people there to snatch it."

## MINNESOTA

### Municipal Customers

- 17 cities including:
  - Ada
  - Alexandria
  - Barnesville
  - Brackengen
  - Detroit Lakes
  - Halstad
  - Hawley
  - Moorhead
  - Ortonville
  - Wadena

### Cooperative Customers

- 28 co-ops including:
  - Beltrami
  - Clearwater-Polk
  - Isasca-Mantrap
  - Lake Region
  - Red Lake
  - Red River
  - Todd-Wadena
  - Wild Rice
- State of Minnesota
  - ergus Falls State Hospital
  - Southwest Minnesota
  - State University
  - Winemar Regional Treatment Center

## FEDERAL GOVERNMENT

- U.S. Bureau of Indian Affairs-Beycourt & Ft. Totten
- Minot Air Force Base
- Grand Forks Air Force Base

DAWN BREHM / The Forum

## Money makes allies

But officials representing Fargo — which does not receive low-cost hydropower — are interested in the Otter Tail proposal as a means of raising money for water development.

"We're interested in anything we can do to solve our water problems in the future," says Fargo Mayor Bruce Furness. "It could benefit Fargo but it could hurt a lot of people around Fargo. We want to be sensitive to that."

Jon Lindgren, who represents Cass County on the Garrison Diversion Conservancy District and preceded Furness as mayor, believes Otter Tail's proposal has more merit than simply asking Congress for more federal tax money.

"It seems very apparent that the power rates are too low," Lindgren says. "If they're too low they need to be increased. There would be a lot of money if they were. Some of it could go to water development in North Dakota."

Proponents of North Dakota's Garrison Diversion Project, which would carry Missouri River water to the east, last fall outlined a plan seeking \$400 million in additional federal payments to finish the water project, and \$75 million in state support.

The plan by the Garrison Diversion Conservancy District does not propose raising hydropower rates, but lays claim to money for hydropower allocated for irrigation features never built.

Garrison Diversion's plan seeks to get money from the irrigation allocation to the project — valued at \$800 million — without raising electric rates. It hasn't worked out how. The board has not taken a stand on Otter Tail's proposal.

"I don't think it would be an issue of the district to appraise that proposal," says Garrison Diversion Manager Warren Jamison. "It's a power issue."

## Rates would jump

Under Otter Tail's plan, rates would increase more sharply for municipal power customers than rural electric customers because a much higher proportion of municipal power is low-cost public hydropower.

Municipal hydropower customers would pay electric bills averaging 25 to 30 percent more under the Otter Tail plan. "But their rates would still be far below the state average," Uggerud says.

For instance, Moorhead Public Service, which receives 65 percent of its electricity from low-cost public hydropower, would face a 27 percent increase. That translates into \$120 a year for a typical residential user.

"That's a good hit on your electricity bill," says Bill Schwandt, general manager of Moorhead Public Service. The non-profit utility should not be penalized for holding its rates down and making a wise decision 40 years ago to buy public hydropower, he says.

Even with a 27-percent rate increase, Moorhead power rates still would be 20 percent below rates paid by Northern States Power Co. customers in Fargo, Uggerud says. The Moorhead increase would raise \$5 million a year, Uggerud says.

"It's a no-brainer," he says. "What Moorhead gets paid in subsidies pays for the Devils Lake solution in two years." A solution for flooding at North Dakota's Devils Lake would cost an estimated \$8 million.

Schwandt's response: "So he'd like Moorhead to pay for Devils Lake's problem?"

## Price hikes vs. efficiency

Rural electric and municipal power customers argue that Otter Tail, a private utility, is trying to force its public power competitors to charge higher rates. A new era is coming in the power industry, where large customers especially will be able to choose their power supplier.

A subcommittee of the House Resources Committee has requested a study of the hydropower allocations by the General Accounting Office, the investigative arm of Congress, based on Uggerud's notes and other information. Uggerud expects to be subpoenaed.

Dorgan stepped in with a request of his own. He wrote a letter Feb. 7 asking the GAO to study unanticipated flood control and navigation benefits to states downstream from the Missouri River dams. "Take a look at the other half as well so we can see the whole map," he says.

Sen. Kent Conrad, D-N.D., says the power allocation issue is worth studying, but doubts Otter Tail's proposed privatization study ever will pass Congress.

Fargo Mayor Bruce Furness wrote the North Dakota congressional delegation asking them to support the allocation study. "We think this is something that should be investigated and determined," he says. Fargo, which does not receive the low-cost hydropower, is interested in a funding source for future water needs.

The "free power" does not go to distinct customers. It gets blended with public hydroelectric transmissions going to scores of rural electric co-ops and municipal power companies in WAPA's eastern Missouri Basin region.

The financial bottom line, according to Uggerud: customers of public power in effect get a 15-percent discount for their electricity, because their rates pay only 85 percent of capital costs associated with irrigation power.

Rural electric and municipal power administrators note, however, that about 15 percent of WAPA's eastern Missouri Basin power goes to private utilities, although Otter Tail is not one of them.

Instead of becoming more efficient, "They're approaching it from another direction," says Heller, who managed Moorhead Public Service before heading Missouri Basin Municipal Power Agency. "They're trying to get everybody else to pay more. That's how they're trying to compete."

Otter Tail's return for its proposed hydropower management study: a fee of roughly \$10 million a year, to pay administration and research costs, which would include identifying farmers and American Indians who would receive reduced-rate power. It will recommend guidelines for private ownership of the hydropower system and a gradual schedule to avoid "rate shock" for customers.

The company insists it has no plans to bid for any public hydropower assets, a position Dorgan, among others, regards as dubious. Instead, Uggerud says, Otter Tail is offering a viable means of raising money for significant water development, vital for North Dakota's economic future.

"We walk away at the end of five years," Uggerud says, "and Congress will have a very valuable study."

## Uggerud a potential witness in probe of hydropower abuses

By Patrick Springer  
The Forum

Ward Uggerud had an invitation in hand but kept a low profile at a strategy meeting last July in Sioux Falls, S.D., of executives

for municipal and rural electric agencies that sell public hydropower.

As a vice president of investor-owned Otter Tail Power Co., the inadvertently invited Uggerud was an unwelcome

guest at the conference of his arch-rival public power administrators.

They spoke candidly. Uggerud kept quiet and took notes.

What he heard startled him: the agencies' electricity customers received a bonanza of free power — unbilled capital costs of \$200 million, maybe \$420 million, maybe more — from electricity originally slated for federal irrigation projects never built.

Otter Tail, based in Fergus Falls, Minn., claims the full implications of the "free power" effectively have been kept secret from the general public for years, buried in dense bureaucratic language in obscure reports.

"That's not their power," Uggerud says. "That's government power."

Now Uggerud finds himself a potential key witness in a congressional investigation of possible public hydropower abuses — and the target of allegations he engaged in "corporate espionage."

Otter Tail is pushing a proposal to study privatizing hydropower generated by the eastern Missouri Basin power system of the federal Western Area Power Administration, which serves rural electric and municipal power customers in North Dakota, South Dakota, Nebraska, western Minnesota and western Iowa.

Rural electric and municipal power agencies hotly deny acting improperly or hiding secret subsidies. They say the power allocations follow laws passed years ago by Congress.

### Hydropower Catch-22

The controversy highlights a largely ignored bureaucratic Catch-22 stemming from a 1944 flood control act that authorized construction of Missouri River dams, including Garrison Dam in North Dakota.

*"That's not their power. That's government power."*

Ward Uggerud  
Otter Tail Power Co.

As compensation for massive flooding from the dams — roughly 500,000 inundated acres each in North Dakota and South Dakota — major irrigation projects were promised the states. Large allocations of low-cost hydropower from the dams were made to irrigation projects.

But customers were not to be charged for the irrigation power costs until irrigation was delivered — and, 50 years later, most of the projects have been abandoned, victims of environmental and budgetary battles.

Cheap power for irrigation flows throughout WAPA's eastern division; only 11 percent of WAPA irrigation projects were built.

Uggerud stumbled onto the Catch-22 at the July 17 meeting of the Mid-West Electric Consumers Association, held in Sioux Falls. The meeting, attended by around 150 municipal and rural electric executives, was called to discuss a plan by the public power agencies to buy the assets of WAPA and two other federal power marketing administrations.

### Buyout busted up

Their proposed price: \$2.6 billion, less than one-third of their market value, estimated at \$9 billion or more. The Wall Street Journal reported the scheme in September — based on Uggerud's notes and corroborated by other information — and the buyout by so-called preference customers fell apart.

The purchase, called "a steal" by one executive at the meeting, reversed the preference customers' vehement objection to privatization. They offered the bid as an alternative to a Clinton administration plan to sell the power agencies for \$3.7 billion, a plan killed last year in the Senate, in an attack in which Sen. Byron Dorgan, D-N.D., played a leading role.

Jeff Nelson, general manager of East River Electric Power Cooperative in Madison, S.D., said the irrigation power allocation subsidies associated with projects like North Dakota's uncompleted Garrison Diversion Project are widely known.

"It doesn't strike me as much of a secret that Garrison wasn't built," Nelson says. "Those numbers have always been available."

Not really, Uggerud maintains. Allocations were noted; free power was not spelled out.

The power for unbuilt irrigation projects is not disclosed in WAPA's annual reports. It is mentioned in obtuse phrases such as "suballocation" in public power documents.

A 1984 congressional report, "Taking From the Taxpayer: Public Subsidies for Natural Resource Development," notes a 1983 Inspector General's study that determined that one-fourth of the investment for WAPA's eastern Missouri Basin system was allocated to irrigation projects not likely to be built.

"There's no secrecy other than what the plan is here," Nelson says, referring to a copyright protecting Otter Tail's plan.

Uggerud's notes quote Nelson as saying \$204 million of eastern WAPA system costs are not being recovered, meaning that electricity is being used at no cost by customers. "We are getting the free use of that generation now and may not be able to get this portion free if the PMAs — power marketing administrations — are sold," Nelson told the Sioux Falls meeting.

Nelson says Otter Tail does not publicize its own subsidies: \$12.7 million in tax breaks in 1993 alone, totaling \$120 million over the years. Uggerud says the investment tax credits are available to any business and are not unique to private utilities.

### 'Corporate espionage'

Nelson does not deny the remarks, but says Uggerud's surreptitious notes were an act of "corporate espionage" aimed at forcing the sale of hydropower assets.

Uggerud says he is willing to testify under oath about his notes. "What they said was this is wrong but we kind of like it that way," he says.

Uggerud's notes and allegations have come to the attention of a congressional committee that is investigating whether WAPA and other federal power marketing administrations are selling some of their electricity at no cost.

TESTIMONY OF BRUCE C. DRIVER

REPRESENTING THE

LAND AND WATER FUND OF THE ROCKIES  
MIDWEST OFFICE OF THE IZAAK WALTON LEAGUE OF AMERICA  
NATURAL RESOURCES DEFENSE COUNCIL  
NATIONAL WILDLIFE FEDERATION

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

MAY 2, 1996

**Testimony of Bruce C. Driver**

Good morning, Mr. Chairman and Members of the Subcommittee, I am Bruce Driver. My business address is 2260 Baseline Road, Boulder, Colorado 80302. I am speaking today on behalf of the Land and Water Fund of the Rockies, the Midwest Office and South Dakota Division of the Izaak Walton League of America<sup>1</sup>, the Natural Resources Defense Council and the National Wildlife Federation. All are organizations with an interest in the impact of federal electric and water policy on the natural environment. An attachment to my testimony briefly describes each organization.

My testimony today addresses: (1) the allocation of the costs of the Pick-Sloan Missouri Basin Project and (2) the Otter Tail Power Company proposal to privatize the Billings Marketing Area of the Western Area Power Administration (WAPA).

**I. PICK-SLOAN COST ALLOCATION**

The "Audit Report No. 93-I-1641, Pick-Sloan Missouri Basin Program Cost Allocation, Bureau of Reclamation," authored by the U.S. Department of the Interior, Office of Inspector General, dated September, 1993, concludes that, absent cost reallocation, investment costs of \$382 million (nearly \$200 million in present value terms) in Pick-Sloan Missouri Basin Project (PSMBP) facilities may not be recovered from project users. This situation developed, the Audit Report describes, as a result of the

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<sup>1</sup> The League sponsors this testimony but does not necessarily support the positions of the testimony co-sponsors on PMA privatization made elsewhere.

allocation of certain reservoir storage and power facility costs to future irrigation development that is not likely to occur. Power users appear to benefit from the operation of these reservoir and power facility investments, but are not fully paying for them. It also appears that the reallocation of costs away from future irrigation projects to power users--the step necessary to rectify this situation--can be made only by Congress.

We do not collectively take a position on whether Congress should reallocate costs related to future irrigation projects that are unlikely to be built to power use. Whether such reallocation should take place raises issues of policy that go beyond the scope of my testimony.

We do believe, however, that, should Congress decide to reallocate these costs and thereby raise additional revenues from project power users, it should refrain from re-directing or allowing these revenues to flow towards unsound water projects. As this Subcommittee knows well, completion of water projects originally conceived as part of the PSMBP have been the subject of contentious disputes in Congress, some of them settled by Congress in the Garrison Reformulation Act of 1986. In our view, it makes little sense to create pressure to re-open these disputes by holding out the possibility that Congress might earmark or permit additional power revenues for use in the construction of water projects that have already been limited or defeated by Congress.

Our concerns in this regard have been heightened by the latest proposal being circulated by the Garrison Conservancy Subdistrict

of North Dakota. According to the National Wildlife Federation (NWF), a Garrison proposal dated February 7, 1996 asks for \$800 million in federal water and power funds to "finance irrigation projects to build what farmers had expected from the federal government over the past 51 years." The proposal, NWF indicates, requests an additional \$400 million in federal buy-out appropriations from Congress for a total of \$1.2 billion. NWF is concerned that the money that the District seeks for water projects for which Congress has already limited federal taxpayer support years ago may somehow be made available from higher PSMBP power rates.

## II. OTTER TAIL PRIVATIZATION PROPOSAL

Otter Tail Power Company has proposed a "pilot privatization" project for the Billings Marketing Area of the Pick Sloan Project (proposal). My understanding of the proposal is based on an eleven-page document published by Otter Tail in April 1995 and revised January 1996.<sup>2</sup>

### A. The Proposal

Otter Tail proposes to enter into a 5-year contract to "manage, operate and maintain the Billings Marketing Area of WAPA," also known as the Eastern Division of the Pick-Sloan Missouri Basin Project. (Proposal, page 1.) Otter Tail would "take over all power marketing activities and would implement strategies to transition rates to market levels." (Id.) Otter Tail would have

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<sup>2</sup> "Proposal for a pilot project to privatize the Billings Marketing Area of WAPA," Otter Tail Power Company, April 1995 (Revised January 1996).

"complete flexibility on all operational matters, including pricing." (Proposal, page 9.) However, Otter Tail believes that it can limit or avoid rate increases to "production agricultural customers of the rural cooperatives now receiving allocations of federal preference power..." and Native American residential customers. State and federal institutional customers would receive their full allocations of power for free. (Proposal, pp. 6-7.) Otter Tail would earn a management fee of one mill per kilowatt-hour for this service. (Proposal, p. 1) Revenues in excess of costs would be returned to the U.S. Treasury. (Id.)

**B. Issues raised by the Otter Tail proposal'**

**1. Absence of detail on key issues**

The proposal focuses on just one aspect of privatization--"transitioning" the price of Pick Sloan/Eastern Division power to market levels--but appears to ignore many other issues raised by privatization, such as the following:

a. WAPA's Eastern Division power sale contracts expire in 2000. In November, 1995, WAPA promulgated regulations (60 FR 54151) that would extend current Eastern Division contracts for 20 years. Would Otter Tail honor this regulation, or does it, under the rubric of "complete flexibility" seek authority to ignore it? Indeed, would any preference for tribes, municipalities and cooperatives still exist under the proposal?

Under the aforementioned regulations WAPA would also create a

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<sup>2</sup> In commenting on the Otter Tail proposal, we take no position regarding whether privatization of the Eastern Division of any other Power Marketing Administrations is or is not appropriate.

resource pool of up to 6% of the marketable resource, primarily to be made available to new customers, but possibly also to meet evolving water-related environmental needs within the Missouri River Basin. Does Otter Tail seek authority to ignore the resource pool? Otter Tail does not answer these important questions in the documentation I have seen.

b. At the same time that WAPA promulgated rules to guide the allocation of power to Eastern Division customers, it also implemented Integrated Resource Planning (IRP) rules for its customers. These rules were promulgated under the direction of Congress in Section 114 of the Energy Policy Act of 1992 (EPAct). The rules require WAPA customers, including its Eastern Division customers, to file IRP documentation for review by WAPA showing that they have evaluated the full range of demand- and supply-side alternatives for energy resources on their systems.

WAPA customers must file their Integrated Resource Plans (IRPs) or "small customer plans" within one year from the date of the promulgation of the IRP regulations (or 18 months thereafter if customers file joint IRPs) and again every five years thereafter. Western must review each of the filed IRPs or plans and, among other things, determine their reasonableness. Non-complying customers can lose a portion of their power allocation.

As of 1994 WAPA had 274 Eastern Division customers, all or most of whom will have to file IRPs, either singularly or as part of groups of customers. Does Otter Tail propose to take over the implementation of WAPA's IRP regulations? Its proposal is not

clear. Can it physically do so? Would it be appropriate to have Otter Tail, a potential competitor with utilities who file IRPs, reviewing their IRPs and passing judgment on them? If Otter Tail does not intend to take over WAPA's IRP responsibilities, will it implement the marketing penalty provisions of WAPA's IRP regulations for non-complying WAPA customers?

c. There are other aspects of national energy policy that WAPA is beginning to integrate into its power marketing decisions, including the integration of non-hydro renewable resources into its resource mix. Will Otter Tail implement these policies when it takes over the marketing of power from WAPA? Has Otter Tail even thought about how it will shoulder the energy and environmental policy burdens being integrated into WAPA's power marketing programs?

d. WAPA markets power from multi-purpose facilities that meet power, irrigation, recreational, fish, wildlife, navigational, municipal and industrial and other needs. An attempt is made to meet these needs in a balanced way after discussions between WAPA, the Bureau of Reclamation, the U.S. Army Corps of Engineers, Missouri Basin states and tribes. The U.S. Environmental Protection Agency, U.S. Fish and Wildlife Service, Bureau of Indian Affairs and other federal agencies also have interests in the operation of Pick-Sloan facilities as do non-governmental organizations, including environmental groups, irrigators, recreational users and many others. In short, operation of the Missouri River is a complex, contested and, sometimes, politicized

matter. Just what role does Otter Tail see for itself in operation of Missouri River facilities? Does Otter Tail expect to take on WAPA's role in participating in the governance of Missouri River facilities? Would this be appropriate?

2. The propriety of one stakeholder among many--Otter Tail--privatizing the Eastern Division

Having just one entity among the many who are stakeholders of the Eastern Division "privatize" the Division raises problems. Among them are:

- a. Should a utility be in the position of raising the rates of its utility competitors?

Competition is increasing in the electric industry. Otter Tail already must compete with WAPA's utility customers in wholesale electric markets. Within a matter of a few years, depending on the evolution of utility regulatory policy in the states in which Otter Tail operates, Otter Tail and WAPA customers may be competing for retail electric loads.

Otter Tail's proposal puts it in a position to manipulate the rates of other utilities with which it may compete in all markets within a few years. This would enable Otter Tail to stifle competition or to shape it to suit its needs. At a minimum, this aspect of the proposal is likely to breed skepticism among current WAPA utility customers regarding its fairness.

- b. Should one stakeholder, among many, privatize a multi-purpose system?

Subsection 1 of this section discusses some of the many issues raised by privatizing the Eastern Division, including issues of energy and environmental policy. Is it appropriate for just one of

the many stakeholders to take the lead in privatizing such a system? Does not any such privatization, assuming it would be appropriate at all, require the involvement of all affected publics and the balancing of policy objectives? Is Otter Tail the right entity to lead this effort? Should not any such effort be led or convened by federal agencies, who at least together should have a broader view of the issues than one lone utility? We think these questions raise considerable doubt regarding the propriety of giving the task of leading a privatization effort to Otter Tail.

- c. Assuming that one utility could lead a privatization effort, is Otter Tail the right utility?

Otter Tail is proposing to take on the marketing of power from 41 federal hydroelectric units with an installed capacity of 2800 megawatts. It is also asking to take on the burden of serving the partial loads of WAPA's 274 Eastern Division customers, including 47 municipalities in Iowa, 46 in Minnesota, 51 in Nebraska, 11 in North Dakota and 33 in South Dakota. Otter Tail would also have to meet the partial needs of 25 rural electric cooperatives, 4 federal agencies including Ellsworth Air Force base, 34 state agencies around the region, seven public utility districts, 3 irrigation districts and even 9 shareholder-owned utilities like Otter Tail. Is Otter Tail the proper entity to take on these tasks?

4. Where will revenues from higher power rates go?

As indicated above, in its published proposal Otter Tail promises to return revenues in excess of costs to the federal Treasury. Indeed, the proposal promises higher returns to

taxpayers if it is allowed to implement its proposal. However, Otter Tail is reported to be promising that at least a portion of the increased revenues it would raise from higher rates for WAPA power would flow to new water projects in North Dakota.

According to an article in the Fargo Forum by Patrick Springer, "Otter Tail Power Company is floating a proposal it says would raise \$20 million a year for water development in North Dakota without raising taxes." Otter Tail Vice-President Ward Uggerud was quoted in the same article as stating that "Otter Tail is offering a viable means of raising money for significant water development vital for North Dakota's economic future."

Which is it? Money for federal taxpayers or to pay for water development? Is it both? What about water development in other states that WAPA now serves with Eastern Division resources, like Nebraska, Wisconsin, Iowa, Minnesota or Montana? Is the proposal to siphon off power revenues into developments in these states, too? Will there be anything left for the federal taxpayer?

##### 5. The fee arrangement

Otter Tail seeks a fee for its management, operation and maintenance of WAPA's Eastern Division equal to 1 mill per kilowatt-hour of the Division's sales. In 1994 WAPA sold 10,309,106,000 kilowatt-hours of electricity to Eastern Division customers. Thus, in 1994 Otter Tail's fee would have been \$10.3 million. Over the five years of its pilot proposal, assuming 1994 sales levels, Otter Tail would earn over \$51,000,000 for its services. This sounds like a lot of money to implement a proposal

that may accomplish only one objective: To raise electric rates. Are there sufficient cost-savings or other benefits that make this deal worth entering into?

6. Relationship between cost reallocation and Otter Tail

Suppose that Congress determines to reallocate costs to power users as discussed in Section I, above. How close to market value would WAPA power be after reallocation? Put another way, how much additional revenue would be raised for federal taxpayers by Otter Tail's proposal above and beyond that already raised by cost reallocation?

7. Is Otter Tail's proposal a good experiment to shed light on national PMA privatization policy?

Otter Tail represents that "the experience [of implementing the Otter Tail proposal] will be helpful in establishing the ground rules for open and competitive sales as well as for additional leases or operating contracts or sales for western's other marketing areas and the other Power Marketing Administrations." (Proposal, page 1.) It is this representation that initially drew our attention to the Otter Tail proposal.

The concerns raised in my testimony cause me to conclude that the Otter Tail proposal would not lead to the establishment of ground rules to guide privatization of other WAPA marketing areas or other PMAs, assuming any such privatization is appropriate at all.

**Attachment: Identification of Testimony Sponsors**

The Land and Water Fund of the Rockies is a regional environmental law center serving the Rocky Mountain and Intermountain states of the American West. The LAW Fund's Energy Project was created to promote clean power technologies in this region of the country through interventions before state utility regulatory agencies and before federal agencies, such as the Western Area Power Administration (WAPA).

Incorporated in 1922, the Izaak Walton League of America, has about 50,000 member nationwide. The League pursues a broad range of national, regional and local conservation goals, including clean water, clean air, farm conservation and protection of natural areas. The Midwest Office of the League is located in Minneapolis, Minnesota, and serves the states of Minnesota, Iowa, Wisconsin and Illinois. Its priorities include the promotion of energy efficiency and renewable resources.

The Natural Resources Defense Council is a nationwide environmental organization with 250,000 members. Since 1970 NRDC has combined law, science and grass roots strength in defense of the environment. NRDC's Energy Project is active in the promotion of energy efficiency and renewable resources throughout the country.

The National Wildlife Federation, with about 6 million members, is the nation's largest conservation education organization. NWF's primary objective is to promote the wise use of natural resources through education programs, publications, research activities and cooperation with legislators, government agencies and private groups.



United States Department of the Interior

BUREAU OF RECLAMATION  
Great Plains Region  
P.O. Box 36900  
Billings, Montana 59107-6900

IN REPLY REFER TO:  
GP-2500

JUN 13 1996

Honorable John Doolittle  
Chairman  
House Subcommittee on Water and Power Resources  
Washington, D.C. 20515

Dear Mr. Chairman:

At your May 2, 1996, oversight hearing on Pick-Sloan Project Repayment Issues, Congressman Richard Pombo asked me to provide for the hearing record a report explaining how the Army Corps of Engineers calculated the recreation benefits associated with Pick Sloan. In response, I am providing a copy of Chapter 6 of the Corps' Draft Environmental Statement on the Review and Update of the Master Water Control Manual for the Missouri River, published July 1994. Prepared by the Corps' Missouri River Division in Omaha, Nebraska, the enclosed chapter is part of a several volume study evaluating whether the current water control plan sufficiently meets contemporary needs in the Missouri River Basin. The document analyzes benefits provided by the Corps' Missouri River Mainstem Reservoir System, but does not address benefits derived at Bureau of Reclamation and Corps tributary facilities. If you have additional questions, you may wish to call the Corps' Omaha office directly at (402) 697-2400.

In addition, I prepared the attached overview of recreation and other benefits provided by Pick-Sloan. If you have any questions, please contact me at (406) 247-7600.

A similar letter is being sent to Congressman Richard Pombo.

Sincerely,

Neil Stessman  
Regional Director

**Attachments**

Committee Note: These attachments were place in subcommittee files.  
cc: **Honorable Peter DeFazio**  
**House of Representatives**  
Washington, D.C. 20515  
(W/overview)

215 South Cascade Street  
PO Box 496  
Fergus Falls, Minnesota 56538-0496  
218 739-8200



May 9, 1996

John T. Doolittle  
Chairman, Subcommittee on Power and Resources  
US House of Representatives  
Washington, DC 20505

Dear Chairman Doolittle:

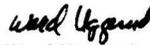
Thank you again for the opportunity which was afforded me to testify before the Power and Resources Subcommittee on the PMA issue. Fair and equitable treatment of the American taxpayer is certainly an issue of concern for all of us.

Just because the majority of Americans do not understand the issues involving PMAs does not mean the Congress should look the other way while billions of dollars of subsidies are being provided to "preference" customers each year. I commend you for your leadership in looking for truth and accountability. Our country would be in much better financial shape if all members of Congress exercised the degree of fiscal oversight that you have brought to your subcommittee. Our system of government would be imminently more respected if it operated as would a business using sound accounting principles.

During my testimony, I was asked questions about certain metering practices. Attached to this letter is a copy of our "Test Schedule" for revenue meters. Also attached is a copy of a letter written to the North Dakota Public Service Commission further explaining our meter testing policy.

Should you have additional questions, I would be most happy to answer them for you.

Sincerely,

  
Ward Uggerud  
Vice President, Operations

**OTTER TAIL POWER COMPANY****TEST SCHEDULE FOR INSTRUMENT RATED METERS  
USED ON RETAIL CUSTOMERS**

<b><u>Annual KWH Consumption</u></b>	<b><u>Meter ,Circuit, and Ratio Test</u></b>	<b><u>No. of Customers</u></b>
2,000,000 & Above	1 Year *	61
170,000 to 2,000,000	6 Years	1100
25,000 to 170,000	12 Years	3900
Less than 25,000	16 Years	<u>500</u>
	<b>TOTAL</b>	<b>5561</b>

\* Ratio Check can be taken every other year.

April 22, 1996

Ms. Illona A. Jeffcoat-Sacco  
Director, Public Utilities Division  
Public Service Commission of North Dakota  
600 E. Boulevard  
Bismarck, ND 58505-0480

Dear Ms. Jeffcoat-Sacco

In your January 9, 1996 letter to John Erickson you requested information about Otter Tail Power Company's standard procedures related to four areas. Dolores Simdorn will respond to three of the areas and requested that I respond to the Required Meter Tests area (69-09-02-26).

The following addresses each section of 69-09-02-26, Electricity Meter Testing.

1. Our central meter shop located in Fergus Falls has two watt-hour meter calibration boards. The accuracy of these boards is checked once each week with a solid state reference standard. Our three reference standards are returned to the manufacturer each June to have the calibration checked. This maintains the traceability of our watt-hour standards to the national standards.

When a meter is tested on the calibration board if it's "as found" accuracy is within our guidelines we do not adjust the meter. When the "as found test" is outside our guidelines the meter is adjusted and retested. This procedure ensures accuracy as close to 100 % as practical. All test data from our two boards is stored in our meter inventory system.

Instrument transformer rated meters tested in the field are compared to a solid state weather standard. These standards are checked against shop reference standards at least once a year.

2. All new demand meters and polyphase Kwh meters are tested in the central meter shop before initially placed in service. New single phase self-contained Kwh meters are sampled tested when they are received from the manufacturer to ensure acceptable accuracy. Any meters that are reconditioned in the meter shop are tested before they are sent to Divisions for installation.

Ms. Jeffcoat-Sacco

Page 2

Instrument transformer rated accounts are checked with a phase angle meter, ammeters and voltmeter to ensure proper connections were made by installer. These checks are done by M&C Technicians. Tests are completed within sixty days from the time sufficient load is connected to the service to ensure an accurate evaluation of metering. If current transformer or potential transformers need to be replaced this procedure is repeated. We also check these circuits whenever the premise is visited to update metering or as part of periodic test.

3. Our procedure requires a test at full load, light load and power factor which is the industry standard method. The full load and light load tests are done at unity power factor. Power factor test is done at fifty percent power factor.
4. Single phase Kwh meters are sample tested by groups. These groups are set up using manufacturer and age of the meters. Results the annual sample test help to determine which groups of meters should be put on the obsolete meter list. We presently are retiring a number of ball bearing meters each year since our previous sample tests have shown that this group of meters is starting to slow down. Information exchange with manufacturers and other utilities is used in designing the sample test and in choosing meters that should be retired.

Single phase self-contained demand meters and self-contained polyphase meters are on a sixteen year test schedule. We also retire a number of obsolete meters each year in this group before they reach the scheduled test period.

Premises with instrument rated meters are tested on a schedule which is based on annual Kwh consumption.

<u>Annual Kwh Consumption</u>	<u>Test Schedule</u>
2,000,000 and above	1 year
170,000 to 2,000,000	6 years
25,000 to 170,000	12 years
Less than 25,000	16 years

We continue to be active in national metering groups to keep abreast of the metering industry issues. Our purchase of a number of solid state meters in the past two years will require us to study this group of meters as they age to determine if test interval can be extended.

Ms. Jeffcoat-Sacco  
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5. Our customers request only a few special meter tests each year. (17 meters in 1995)  
Meters which our customers request to be tested are sent (UPS or hand delivered) to our central meter shop for testing. The results are mailed back to the Division office so that they can contact the customer to address their concern.
6. Since we have so few requests for tests, I am not aware of any cases where we have requested payment from our customer.

The information that I have provided is a quick overview of the activities related to meter testing. If you would like more details on any part of our processes, please let me know.

If your travels bring you to Fergus Falls please stop by for a short tour of our meter shop.

Brian Malchert, Manager  
Energy Measurement & Control  
218-739-8391

c: Mr. John Erickson  
Ms. Dolores Simdorn



STATEMENT BY CONGRESSMAN BOB FRANKS (R-MJ)  
CO-CHAIRMAN, NORTHEAST-MIDWEST CONGRESSIONAL COALITION  
HOUSE RESOURCES SUBCOMMITTEE ON WATER AND POWER RESOURCES  
MAY 2, 1996

Mr. Chairman, thank you very much for allowing me to make a statement before the Water and Power Subcommittee. As Co-Chairman of the Northeast-Midwest Congressional Coalition, I commend you and your colleagues for providing the needed oversight of the accounting practices of power marketing administrations.

I am very concerned that taxpayers in the Northeast and Midwest are subsidizing electricity for "preferred customers" in parts of the South and West, while being forced to pay some of the highest utility rates in the nation. In fact, the Northeast and Midwest are the only areas of the country without federally subsidized power. Not only is the subsidy given to the South and West unfair to consumers in our area, it places our region at a competitive disadvantage in attracting and keeping businesses. It's hard to convince energy-intensive businesses to stay in the Northeast or Midwest when they can pack up and move to the South or West and pay much lower energy bills. That is why I am particularly alarmed about the allegation that preference customers of the Western Area Power Administration (WAPA) have been receiving free electricity.

As I understand, the General Accounting Office will report at this hearing that federal taxpayers provided some one-half

billion dollars in subsidies to preferred customers such as municipalities and co-operatives in the WAPA service area. This is outrageous. Congress cannot rein in egregious government spending and balance the federal budget as long as federal subsidies like WAPA exist.

As you know, today there are five power marketing administrations covering most of the South and West. They operate 129 federally-owned generating plants. The largest of these, the Bonneville Power Administration, provides half of all the electric power used in the entire Pacific Northwest Region. With this committee's continued efforts, we may even find that other PMAs have similar subsidies.

In my home state of New Jersey, high energy costs are hindering job growth. In fact, many businesses that are now leaving the state identify high energy costs as one of the top reasons for their relocation. Indeed, one just has to look at the disparity in energy costs between a non-PMA state like New Jersey and PMA states such as Georgia or Texas. According to the New Jersey Board of Public Utilities, the industrial electric rate for New Jersey is 7.96 cents/kilowatt hour. However, Texas and Georgia businesses pay just 4.38 and 4.23 cents/kilowatt hour respectively. These high electric costs are inhibiting job growth and economic expansion in my state.

At a minimum, I believe Congress must recover the financial

resources lost because of the WAPA subsidy. Furthermore, Congress should privatise the PMAs as soon as possible and end the regional inequities they create. There is no justification for New Jersey taxpayers to pay some other state's electric bills. We must eliminate the hundreds of millions of dollars taxpayers now spend every year to operate PMA generating plants and take the federal government out of the power business.

Thank you.

**STATEMENT  
OF**

**Thomas Donnelly  
Executive Vice-President  
National Water Resources Association**

**before the  
Committee on Resources  
Subcommittee on Water and Power Resources**

**on**

**Pick-Sloan Repayment Issues**

**May 2, 1996**

**MR. CHAIRMAN AND MEMBERS OF THE SUBCOMMITTEE:**

I am Thomas F. Donnelly, Executive Vice President of the National Water Resources Association. The following testimony is presented to assist the Subcommittee in its oversight review of Pick Sloan Missouri River Basin Program.

The National Water Resources Association (NWRA) is a nonprofit federation of state associations and individuals dedicated to the conservation, enhancement, and efficient management of our Nation's most precious natural resource, water. The NWRA is the oldest and most active national association concerned with water resource policy and development. Its strength is a reflection of the tremendous "grassroots" participation it has generated on virtually every national issue affecting western water conservation, management, and development.

**BACKGROUND**

The Pick-Sloan Missouri Basin Program (PSMBP) was initially authorized by the Flood Control Act of December 22, 1944, which approved the general comprehensive plan for the conservation, control, navigation, irrigation of over 5 million acres, power generation from hydroelectric plants with a total installed capacity of about 2,500 megawatts, municipal and industrial water supplies, stream pollution abatement, sediment control, preservation and enhancement of fish and wildlife, and creation of recreation opportunities.

As part of the PSMBP, more the 1,000,000 acres of prime farmland in the Dakota's were permanently flooded by construction of the Garrison, Oahe, Big Bend, Fort Randall and Gavins Point Dams and additional acres of prime farmland were flooded with the construction of the Fort Peck Dam in Montana. These dams provide flood control, downstream navigation, hydroelectric power generation, recreation, rural, municipal and industrial water for the Missouri basin states.

In the 50 years since the passage of the Act, the flood control, power and navigation components have been essentially accomplished or completed. Development of water supplies for irrigation and domestic use as intended by the plan has not occurred. The PSMBP originally identified 137 irrigation units that would have provided water to nearly 5 million acres of land. Currently less than 10 percent of those land are receiving water service.

## PRESENT PICTURE

The upper Missouri River Basin Tribal Governments and the states of Montana, North Dakota, South Dakota, and Wyoming have made several attempts at receiving the benefits promised in the PSMBP, unfortunately the Federal government and Congress has turned a deaf ear to most of those proposals.

For example:

- The Subcommittee is well aware of the changes to the Garrison Unit in North Dakota which occurred in 1986. I will not dwell on that history other than to indicate the State has benefited from the municipal, rural and industrial program authorized under that legislation. I understand that the State is working on a detailed plan to have the promise of Missouri River water actually being delivered to Eastern and Central North Dakota. Hopefully this Subcommittee will address that specific issue sometime in the near future.
- When the Garrison Unit was undergoing reformulation in early 1980's, South Dakota was working on the CENDAK plan to deliver Missouri River water through the facilities partially constructed for the defunct Oahe Unit of the PSMBP, the development of the Lake Andes/ Wagner Unit and Gregory County Project, and the development of rural water systems to serve major areas east and west of the Missouri River. South Dakota has benefited from the authorization and development of three rural water systems. Authorization legislation for a fourth rural water system will be introduced later this year or early next year. While successful in the development of rural water, the State is waiting for the opportunity to complete the facilities that would deliver water for the purpose of irrigation as promised under PSMBP.
- Montana and Wyoming are waiting for the completion of water development promised under the Pick-Sloan Missouri Basin Plan.

As I have previously indicated, the PSMBP is a multi-purpose development program which has delivered various benefits to the PSMBP states of Colorado, Kansas, Montana, Nebraska, North Dakota, South Dakota and Wyoming. As well as, the states of Minnesota and Iowa as part of the project area for hydroelectric power marketing purposes.

The citizens of the upper Great Plains, an area represented by NWRA, have seen homesteads, farms and towns wither and disappear because the Federal government has failed to deliver the water development promised by the Flood Control Act of 1944. While individual water projects have been developed and Congress made new project adjustments and authorizations in the Omnibus Reclamation Authorization Act of 1992. There is still a need to address the overall water needs of all the citizens within the Upper Basin. It is important to understand however, there is still the expectation that the Federal Government will deliver on the water development promises that have yet to be met.

## SPECIFIC COMMENT

The PSMBP was authorized to bring rural economic benefits to the region through the multipurpose development of a major river basin. There are a couple of unique features of PSMBP which are a part of this hearing. They are the Ultimate development and suballocation concepts.

The Ultimate Development Concept, a method by which costs are allocated to the main project functions, is based on the ultimate development and completion of the project. For example, in the case of PSMBP, the ultimate benefits of flood control were realized as soon as the dams and reservoirs on the main stem of the Missouri river were completed. To date, the flood control benefits have been calculated at over \$2 billion dollars of flood damage prevented. The proposed ultimate development plan of the 1950's and 1960's was to have the entire PSMBP completed by the year 2000.

The ultimate development concept has been a very important part of the PSMBP development as it has allowed for the multipurpose development without major financial impacts. NWRA believes it is essential that the ultimate development concept be maintained if the remaining water development in the upper basin states has any chance of proceeding.

The other unique feature of the PSMBP program is the suballocation percentage. There are few people in the country that understand the arcane details of this issue, and I don't pretend to be one. What I do understand is that the basic plan for the PSMBP contemplated that capacity from the project hydroelectric power plants would be used for pumping irrigation water for the many units not capable of service by gravity flow. Accordingly, a portion of the cost of the power system can be said to be for the exclusive use of irrigation, and, in that sense, appropriately allocable to the purpose of irrigation which is the suballocation percentage.

As in all multi-purpose projects where irrigation is a function it has been the Federal policy that power revenues would be used to repay the costs of irrigation development that is beyond the ability of the water user to pay. As you know, this particular component is called irrigation aid. To date, there has not been a demonstration of commitment by the Federal Government to complete the irrigation components of the PSMBP. It is our hope that the irrigation aid component of the power revenues and pumping energy can be used for water development that would meet the contemporary water needs of the upper basin states.

The individual upper Missouri River basin states are developing innovative projects and plans that would allow each state to receive the economic benefits that were promised when the original project was authorized and the reservoirs created a permanent flood of prime farmland on the upper Missouri River. To accomplish this we think a strong water-power partnership and maintaining the principles of ultimate development in

the PSMBP is the only way to complete the water development and improve the economic conditions of the upper basin states.

The development of safe, affordable water supplies will translate into the research and development of diversified businesses, new products, marketing strategies and employment opportunities. Economic development opportunities on the Great Plains depend on the careful stewardship of all the natural resources. The pioneer spirit, rural values and heritage that have served as the foundation for the establishment of the current rural economy will guarantee the development of future opportunities.

## CONCLUSION

In summary NWRA asks that the Subcommittee consider the following points:

- that there is a compelling regional necessity and obligation to stay with an ultimate development concept for the Pick-Sloan Missouri Basin Program;
- that the upper Missouri River Basin States gave up over 1 million acres of prime agricultural land to satisfy Pick-Sloan Missouri River Basin Program needs on the federal promise of water development and the attending economic development, which to this day are unrealized,
- that the states of Montana, North Dakota, South Dakota and Wyoming are working on comprehensive proposals for the development of water resources as envisioned in the Flood Control Act of 1944. Each state has different needs and they should be allowed the opportunity to design a program that will fulfill the contemporary water development needs of their citizens. We urge the Subcommittee give these proposal serious consideration when they are completed and submitted for authorization.

Thank you for this opportunity to provide our view. NWRA looks forward to working with the Subcommittee as you move forward on these issues.



ISBN 0-16-052957-3



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