

Y 4
. In 8/14

1023

93-53
In 8/14
ep
93/4

93-53

REVIEW OF ELECTRIC POWER RATE INCREASES

GOVERNMENT

DOCUMENTS

Storage

FEB 10 1975

HEARINGS

THE LIBRARY
KANSAS STATE UNIVERSITY

BEFORE THE

SUBCOMMITTEE ON
WATER AND POWER RESOURCES

OF THE

COMMITTEE ON

INTERIOR AND INSULAR AFFAIRS

HOUSE OF REPRESENTATIVES

NINETY-THIRD CONGRESS

SECOND SESSION

ON

H.R. 14221

A BILL TO PROVIDE FOR THE REVIEW OF INCREASES
PROMULGATED BY THE SECRETARY OF THE INTERIOR
ON NOVEMBER 1, 1973, IN RATES FOR ELECTRIC POWER
SOLD AT FIVE BUREAU OF RECLAMATION PROJECTS, AND
FOR OTHER PURPOSES

HEARINGS HELD IN WASHINGTON, D.C.

MAY 17 AND 20, 1974

Serial No. 93-53

Printed for the use of the
Committee on Interior and Insular Affairs



U.S. GOVERNMENT PRINTING OFFICE

WASHINGTON : 1974

41-200

COMMITTEE ON INTERIOR AND INSULAR AFFAIRS

HOUSE OF REPRESENTATIVES

JAMES A. HALEY, Florida, *Chairman*

ROY A. TAYLOR, North Carolina
HAROLD T. JOHNSON, California
MORRIS K. UDALL, Arizona
PHILIP BURTON, California
THOMAS S. FOLEY, Washington
ROBERT W. KASTENMEIER, Wisconsin
JAMES G. O'HARA, Michigan
PATSY T. MINK, Hawaii
LLOYD MEEDS, Washington
ABRAHAM KAZEN, Jr., Texas
ROBERT G. STEPHENS, Jr., Georgia
JOSEPH P. VIGORITO, Pennsylvania
JOHN MELCHER, Montana
TENÓ RONCALIO, Wyoming
JONATHAN B. BINGHAM, New York
JOHN F. SEIBERLING, Ohio
HAROLD RUNNELS, New Mexico
YVONNE BRATHWAITE BURKE,
California
ANTONIO BORJA WON PAT, Guam
WAYNE OWENS, Utah
RON DE LUGO, Virgin Islands
JAMES R. JONES, Oklahoma

CRAIG HOSMER, California,
Ranking Minority Member
JOE SKUBITZ, Kansas
SAM STEIGER, Arizona
DON H. CLAUSEN, California
PHILIP E. RUPPE, Michigan
JOHN N. HAPPY CAMP, Oklahoma
MANUEL LUJAN, Jr., New Mexico
JOHN DELLENBACK, Oregon
KEITH G. SEBELIUS, Kansas
RALPH S. REGULA, Ohio
ALAN STEELMAN, Texas
DAVID TOWELL, Nevada
JAMES G. MARTIN, North Carolina
WILLIAM M. KETCHUM, California
PAUL W. CRONIN, Massachusetts
DON YOUNG, Alaska
ROBERT E. BAUMAN, Maryland
STEVEN D. SYMMS, Idaho

CHARLES CONKLIN, *Staff Director and Chief Clerk*

LEE McELVAIN, *Counsel*

CHARLES LEPPERT, Jr., *Minority Counsel*

SUBCOMMITTEE ON WATER AND POWER RESOURCES

HAROLD T. JOHNSON, California, *Chairman*

MORRIS K. UDALL, Arizona
THOMAS S. FOLEY, Washington
LLOYD MEEDS, Washington
ABRAHAM KAZEN, Jr., Texas
ROBERT G. STEPHENS, Jr., Georgia
TENÓ RONCALIO, Wyoming
HAROLD RUNNELS, New Mexico
YVONNE BRATHWAITE BURKE,
California
JAMES R. JONES, Oklahoma

MANUEL LUJAN, Jr., New Mexico
CRAIG HOSMER, California
DON H. CLAUSEN, California
JOHN N. HAPPY CAMP, Oklahoma
JOHN DELLENBACK, Oregon
ALAN STEELMAN, Texas
DAVID TOWELL, Nevada
WILLIAM M. KETCHUM, California
STEVEN D. SYMMS, Idaho

JIM T. CASEY, *Consultant on Water and Power Resources*

JACK DAUM, *Minority Consultant*

NOTE.—The Chairman of the Full Committee is an ex officio voting member of this subcommittee. The first listed minority member is counterpart to the subcommittee chairman.

CONTENTS

	Page
Hearings held:	
May 17, 1974.....	1
May 20, 1974.....	59
Text of H.R. 14221.....	1
Report of the Department of the Interior.....	3
Report of the Federal Power Commission.....	4
Report of the Comptroller General.....	4
Statements:	
Armstrong, Richard T., general manager, Plains Electric Generation and Transmission Cooperative, Inc.....	151
Dillon, Thomas, attorney, representing the Sacramento Municipal Utility District.....	85
Gillmore, Hon. Gary, Mayor, City of Santa Clara, Calif.....	98
Johnson, Hon. Harold (Bizz), a Representative in Congress from the State of California.....	25
Kuder, William B., assistant general counsel, Pacific Gas & Electric Co. (plus information for the record).....	125
Subcommittee on Conservation and Natural Resources, questions of Nov. 12, 1973 and P.G. & E. answers.....	126
Views and comments on General Accounting Office report B-125042 of Nov. 19, 1973.....	129
Bureau capacity disposition (table).....	129
Bureau energy disposition (table).....	130
Congressman McCloskey's questions of Feb. 25, 1974, and P.G. & E. answers.....	132
Subsidy received by Government owned and/or financed electric utilities.....	135
Revenue and tax data—investor-owned and Government-owned and/or financed electric power systems, 1967 (table).....	138
Table 2.—Net electric income and tax deficiency, Government-owned and/or financed electric utilities, 1967.....	139
Table 3.—Federal Government subsidy to Government-owned and/or financed electric power systems, 1967.....	140
Table 4.—State and local Government subsidy to Government-owned and/or financed electric power systems, 1967.....	143
Table 5.—Federal, State, and local government subsidy to Government-owned and/or financed electric power systems, 1967.....	144
Table 6.—Federal, State, and local government subsidy to Government-owned and/or financed electric power systems, projected to 1980.....	144
McDiarmid, Robert C., special counsel to the Northern California Power Agency.....	101
Moss, Hon. John E., a Representative in Congress from the State of California presented by Phineas Indritz.....	6
Northern California Power Agency, submitted by Herbert C. Westfall.....	117
Plains Electric Generation and Transmission Cooperative, Inc., position statement.....	152
Richter, Melvin, attorney, Arizona power Authority (plus attachments).....	59
Stamm, Hon. Gilbert G., Commissioner, Bureau of Reclamation.....	30
Westfall, Herbert C., for the Northern California Power Agency.....	117

IV

Letters:

Abdnor, Hon. James, Member of Congress, to Hon. Harold T. Johnson, dated May 28, 1974-----	Page 29
Horton, Hon. Jack, Assistant Secretary of the Interior, to Hon. James A. Haley, dated May 16, 1974 (report)-----	3
Johnson, Hon. Harold T. (Bizz), chairman, Subcommittee on Water and Power Resources, to Hon. Rogers C. B. Morton, dated Jan. 28, 1974-----	26
Johnson, Hon. Harold T. (Bizz), chairman, Subcommittee on Water and Power Resources, to Hon. Rogers C. B. Morton, dated March 22, 1974-----	25
Keller, R. F., acting Comptroller General of the United States, to Hon. James A. Haley, dated May 15, 1974 (report)-----	4
Kuder, William B., Pacific Gas and Electric Co., San Francisco, Calif., to Hon. Harold T. Johnson, dated June 26, 1974 (answer to rebuttal of Northern California Power Agency)-----	163
Nassikas, Hon. John N., Chairman, Federal Power Commission, to Hon. James A. Haley, dated May 16, 1974 (report)-----	4
Pelz, Richard K., Office of the Solicitor, Assistant Solicitor, Power, to Assistant Secretary, Land and Water Resources, dated Feb. 15, 1974 (memorandum)-----	37
Spiegel, George, special counsel to the Northern California Power Agency, to Hon. Harold T. Johnson, dated, June 6, 1974 (plus rebuttal to statement by William B. Kuder)-----	152
Additional information:	
Contract for electric service to the Sacramento Municipal Utility District, U.S. Department of the Interior, Bureau of Reclamation, Central Valley Project Calif-----	88
Coverage of projected annual expenses in Bureau of Reclamation power ratemaking studies-----	37
General power contract provisions, U.S. Department of the Interior, Bureau of Reclamation, dated effective June 10, 1952-----	93
Northern California Power Agency rebuttal to statement by William B. Kuder, assistant general counsel, Pacific Gas and Electric Co....	153
Pacific Gas and Electric Co. answer to rebuttal of Northern California Power Agency-----	163
Westfall, Herbert C., personal professional qualifications-----	124

REVIEW OF ELECTRIC POWER RATE INCREASES

FRIDAY, MAY 17, 1974

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON WATER AND POWER RESOURCES
OF THE COMMITTEE ON INTERIOR AND INSULAR AFFAIRS,
Washington, D.C.

The subcommittee met, pursuant to notice, at 10:15 a.m., in room 1324, Longworth House Office Building, Hon. Harold T. Johnson (chairman of the subcommittee) presiding.

Mr. JOHNSON. The Subcommittee on Water and Power will come to order. I am very sorry that I was late and caused a delay here for all of you people who are going to testify, but we had another very important matter like we get hung up with from time to time. We had to take care of it.

I apologize to my colleagues who were here on time.

The Subcommittee on Water and Power Resources will please come to order for the hearing of testimony on H.R. 14221—a bill to provide for the review of increases promulgated by the Secretary of the Interior on November 1, 1973, in rates for electric power sold at five Bureau of Reclamation projects, and for other purposes.

Unless there is objection, the bill will be entered in the record at this point.

Is there objection?

Hearing none, it is so ordered.

[The bill follows:]

[H.R. 14221, 93d Cong., 2d sess.]

A BILL to provide for the review of increases promulgated by the Secretary of the Interior on November 1, 1973, in rates for electric power sold at five Bureau of Reclamation projects, and for other purposes

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That Congress finds and declares that—

(a) the Secretary of the Interior, pursuant to section 9(c) of the Reclamation Project Act of 1939, as amended (43 U.S.C. 485h(c)), has established by contract rates for electric power sold to customers at five Bureau of Reclamation projects (Central Valley, Colorado River storage, Parker-Davis, eastern and western divisions of the Pick-Sloan Missouri River Basin, and Rio Grande) in fourteen States;

(b) the customers of these projects include municipalities, irrigation and utility districts, cooperatives, and State and Federal agencies;

(c) on January 27, 1973, the Secretary of the Interior announced his intention to increase such power rates effective January 1, 1974;

(d) on May 28, 1973, the Secretary of the Interior announced proposed rate increases higher than those estimated by him in January 1973;

(e) despite requests by customers and Members of Congress for adequate public hearings on such rate increases, the Interior Department held only informal one-day hearings for each project at which Reclamation Bureau officials stated that they would not answer questions during the hearings or allow examination of Bureau and other experts concerning the basis for such increases;

(f) on November 1, 1973, the Secretary of the Interior promulgated the proposed rate increases for each of the five projects, effective April 1, 1974;

(g) on November 19, 1973, the Comptroller General of the United States issued a report (B-125042) on the Central Valley project rate increase criticizing several of the principal criteria and procedures used by the Interior Department in establishing the Central Valley project rate increase, recommending that they be changed, and noting that such change "would tend to reduce substantially" the Central Valley project rate increase;

(h) many of the Comptroller General's findings are applicable to the rate increases for the other projects; and

(i) despite the Comptroller General's findings, the Secretary of the Interior made no substantial change in the criteria or procedures used in promulgating the rate increases.

SEC. 2. The Secretary of the Interior shall within thirty days after enactment of this Act transmit to the Federal Power Commission the rate schedules promulgated by him on November 1, 1973, for each of these five projects, and all pertinent documents, letters, memorandums, and other materials. Upon receipt of such schedules and materials, the Commission shall, with assistance of the Comptroller General, promptly conduct a thorough review of the promulgated schedules and the criteria and procedures followed by the Secretary in developing such schedules, for the purpose of determining their reasonableness and adequacy and their consistency with applicable requirements of law and regulations. Upon completion of such review, the Commission shall issue a decision as to each project, approving such schedules or recommending to the Secretary modifications thereof. Each such decision shall be made on the record after an opportunity for public hearing pursuant to sections 307 and 308 of the Federal Power Act, as amended (16 U.S.C. 825f and 825g). Nothing in this section shall be deemed to preclude the Secretary from reviewing any such rate schedule at the same time the Commission is reviewing it, and submitting to the Commission for approval any modification therein. All materials, documents, and other written matter related to the Commission's decision shall be available to the public.

SEC. 3. Each decision of the Federal Power Commission issued pursuant to section 2 of this Act shall be subject to rehearing and judicial review, in the United States Court of Appeals for the District of Columbia, in accordance with section 313 of the Federal Power Act, as amended (16 U.S.C. 825i). For the purpose of this Act, the term "person" in section 313 shall include the customers of the projects referred to in this Act.

SEC. 4. The rate schedules promulgated by the Secretary on November 1, 1973, for each of the five projects referred to in this Act shall continue in effect pending review thereof pursuant to this Act: *Provided*, That if the Federal Power Commission does not issue its decision concerning any such project on or before June 30, 1975, the Secretary of the Interior shall on July 1, 1975, suspend such rate schedule for such project and reinstate the rate schedule which was in effect for such project on March 31, 1974. Such reinstated schedule shall remain in effect until the Federal Power Commission has issued its decision for such project under section 2 of this Act.

SEC. 5. The Secretary of the Interior, upon receipt of any final decision by the Federal Power Commission recommending a modification in the rate schedule promulgated by him on November 1, 1973, for any project, shall promptly promulgate a new rate schedule in accordance with said decision. Such new rate schedule shall be effective as of April 1, 1974, as to all customers for which the rate schedule was validly promulgated on November 1, 1973. The Secretary shall also provide, as appropriate, for any refund, credit, or other adjustment in rates paid by any customer between April 1, 1974, and the date such new rate schedule is promulgated.

SEC. 6. The Secretary of the Interior shall promptly publish proposed regulations providing for opportunity for an adequate public hearing and written decision on the record concerning any electric power rate increase hereinafter proposed by the Secretary pursuant to section 9(c) of the Reclamation Project Act of 1939, as amended, and any contract or amendment thereto executed pursuant to such section, and public review and comment, during a period of not less than forty-five days prior to its execution, on every proposed contract or modification thereof hereinafter negotiated for the sale, exchange, or transmission of electric power at projects subject to said section 9(c). Such regulations shall be promulgated by the Secretary within one hundred and twenty days after enactment of this Act and shall apply to any such rate increase hereinafter proposed.

Mr. JOHNSON. Immediately following the bill there will be entered in the record the departmental reports, particularly the Department of Interior report dated May 16, 1974, wherein it is recommended in effect that the bill not be enacted. The report was signed by Assistant Secretary Jack Horton and was received by the committee on May 16.

Is there objection to it being placed in the record?

[The Department of Interior report follows:]

U.S. DEPARTMENT OF THE INTERIOR,

OFFICE OF THE SECRETARY,

Washington, D.C., May 16, 1974.

HON. JAMES A. HALEY,

Chairman, Committee on Interior and Insular Affairs, House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: This responds to your request for the views of this Department on H.R. 13867 and H.R. 14221, identical bills "To provide for the review of increases promulgated by the Secretary of the Interior on November 1, 1973, in rates for electric power sold at five Bureau of Reclamation projects, and for other purposes."

We recommend that the bills not be enacted.

The bills would require the Secretary of the Interior to transmit to the Federal Power Commission within thirty days after enactment the rates schedules promulgated by him on November 1, 1973 for five Bureau of Reclamation projects—Central Valley, Colorado River storage, Parker-Davis, eastern and western divisions of the Pick-Sloan Missouri River Basin and Rio Grande—together with related materials. The FPC, assisted by the Comptroller General, would review the schedules to determine "their reasonableness and adequacy and their consistency with applicable requirements of law and regulations." The FPC would then approve the rates or recommend modifications after a hearing on the record pursuant to sections 307 and 308 of the Federal Power Act. Provision is made for judicial review of each FPC decision. The rates would continue in effect pending review, provided that if the FPC's decision is not issued as to any of the projects by June 30, 1975, the Secretary shall suspend the rate schedule for such project and return to the March 31, 1974, rate schedule, which will remain in effect until the FPC issues its decision. The Secretary would be required to follow the FPC's decision in setting rates, which would be effective from April 1, 1974.

The bills would also require the Secretary of the Interior to publish regulations "providing for opportunity for an adequate public hearing and written decision on the record concerning any electric power rate increase hereinafter proposed by the Secretary pursuant to section 9(c) of the Reclamation Project Act of 1939, as amended." In addition, every contract or amendment executed pursuant to section 9(c) would be subject to a requirement that it be made available for public review and comment for not less than forty-five days prior to execution.

We oppose the bill's provisions relating to the rates promulgated on November 1, 1973. These rates were promulgated on the basis of extensive study and review by the Secretary and after public opportunity for comment. The rates are proper and in accordance with applicable law and legislation authorizing an *ex post facto* review of them is unjustified. We note incidentally that judicial review of our action is being sought.

We would not object to submission of future Reclamation power rates to the FPC for advisory review on the same basis as the rates promulgated by the Secretary for other Interior power agencies. Beyond this, existing law provides an adequate framework for the development of appropriate procedures, including public participation in rate setting, and we therefore oppose further modification of the law.

The Office of Management and Budget has advised that there is no objection to the presentation of this report from the standpoint of the Administration's program.

Sincerely yours,

JACK HORTON,

Assistant Secretary of the Interior.

Mr. JOHNSON. We also have received a report from the Federal Power Commission signed by the Chairman which is in opposition to the legislation. We also have a report from the Comptroller General recommending certain amendments to the legislation. If the legislation is amended he would have no objection.

That was signed by the Acting Comptroller General.

Is there objection to those other two reports going in the record?

Hearing none, so ordered.

[The Federal Power Commission report and the Comptroller General's report follow:]

COMPTROLLER GENERAL OF THE UNITED STATES,
Washington, D.C. May 15, 1974.

HON. JAMES A. HALEY,
Chairman, Committee on Interior and Insular Affairs, House of Representatives

DEAR MR. CHAIRMAN: By letter dated April 23, 1974, you requested our comments on H.R. 14221, a bill to provide for the review of increases promulgated by the Secretary of the Interior on November 1, 1973, in rates for electric power sold at five Bureau of Reclamation projects, and for other purposes.

Section 2 of the bill provides for the review of the rate schedules by the Federal Power Commission with assistance of the Comptroller General. The Federal Power Commission is the proper agency to review power rates. We believe that any form of direct participation by the Comptroller General in the Federal Power Commission's review would tend to compromise the General Accounting Office's independent role as a review arm of the Congress. Accordingly, we suggest that the bill be amended to delete that part of section 2 which provides for assistance by the Comptroller General.

Our Office would, of course, provide the Federal Power Commission with copies of any reports we have issued on the Federal power programs and would discuss any findings or observations included in such reports. Also, we would make reviews of the rate-making practices used in the Federal power programs as we deem appropriate or as might be requested by a committee on the Congress having jurisdiction over such programs.

Section 6 of the bill provides for the Secretary of the Interior to publish proposed regulations providing for public hearing and written decision on the record concerning, among other things, any electric power rate increase hereinafter proposed by the Secretary pursuant to section 9(c) of the Reclamation Project Act of 1939. Such public hearing and written decision on the record are not now required for rate schedules issued by the Secretary for Federal power marketed pursuant to section 5 of the Flood Control Act of 1944 (16 U.S.C. 825s), and to section 6 of the Bonneville Project Act, as amended (16 U.S.C. 832e). These latter two laws provide, however, that rate schedules become effective upon confirmation and approval by the Federal Power Commission.

We suggest that the Committee consider the need for establishing a uniform rate review and approval process for all power marketed by the Secretary of the Interior regardless of whether the Federal power is marketed pursuant to section 9(c) of the Reclamation Project Act of 1939, as amended; section 5 of the Flood Control Act of 1944; or section 6 of the Bonneville Project Act, as amended.

Sincerely yours,

R. F. KELLER,
Acting Comptroller General of the United States.

FEDERAL POWER COMMISSION,
Washington, D.C., May 16, 1974.

HON. JAMES A. HALEY,
Chairman, Committee on Interior and Insular Affairs, House of Representatives,
Washington, D.C.

DEAR MR. CHAIRMAN: This is in reply to your request of April 23, 1974, for the Commission's views on H.R. 14221. The Federal Power Commission does not favor the enactment of the bill.

Currently, the Congress has placed upon the Secretary of the Interior the proprietary responsibility for the marketing of hydroelectric power and energy and water for irrigation and municipal and industrial water supplies from the five projects as identified in the bill. Currently, there is accountability of the Secretary to the Congress under numerous pieces of legislation commencing in 1902, 32 Stat 388. The proposed bill would dilute that accountability by interjecting into the Secretary's responsibilities, the views and recommendations of this Commission, applying procedural and ratemaking concepts of the Federal Power Act, 16 U.S.C. 791(a) *et seq.* The Secretary's legal responsibilities and the statutory standards governing the marketing of power and water under the Reclamation laws are not the standards and procedures of the Federal Power Act.

Section 2 of the bill, while not specific in relation to defined terms, provides that rates for the subject five projects shall be determined as to " * * their reasonableness and adequacy and their consistency with applicable requirements of law and regulations." "Reasonable and adequate" are terms of art under the Federal Power Act and we assume that their use in the bill reflects this fact. The Bureau of Reclamation uses repayment studies as a major factual predicate for its ratemaking proposals. This Commission employs the tests of the Federal Power Act, just, reasonable and not unduly discriminatory or preferential 16 U.S.C. 824d. The bill appears to blend the two standards.

The bill mandates the application by the Commission of ratemaking procedures to the rate schedules previously promulgated by the Secretary of the Interior for the following Bureau of Reclamation projects: Central Valley, Colorado River Storage, Parker Davis, eastern and western divisions of the Pick-Solan Missouri River Basin, and Rio Grande, situated in 14 states. The net result of any Commission recommendations, as provided in the bill, would appear to change longstanding Congressionally imposed standards as to how Reclamation project services (power and water) are to be priced.

Procedurally, the bill would apply to federally-owned electric operations, the hearing and judicial review concepts which Congress has determined should be applicable to the non-federal utilities which the Commission regulates under the Federal Power Act. This means that Commission findings and recommendations and any implementing rates and charges of the Secretary under Section 5 of the bill, would be subjected to judicial review in the courts upon the basis of the substantial evidence rule and error of law test which govern this Commission, 16 U.S.C. 825f, but do not now govern actions of the Secretary in discharging his proprietary functions. Section 6 of the bill raises questions as to whether the Secretary would have to follow FPC review procedures in subsequent rate reviews.

The application of these types of procedures to proprietary functions of the Secretary may raise substantial administrative problems for the Secretary in the light of the Reclamation laws which he must administer. We do not administer those laws and the economic regulatory functions of the Federal Power Act are markedly different from the purposes of the reclamation laws.

Policy considerations aside, the Commission's staff has also assessed the factual ramifications and manpower requirements of the studies which would be necessary under the application of these concepts to the five projects. Their initial estimate is that 50 man-years would be required for Commission staff personnel. Salary costs alone would be in excess of \$1,000,000 annually. The bill contemplates that the studies would be completed by June 30, 1975. The staff does not believe that the studies could be completed within that time period. Current work schedules and budgetary requirements of this agency preclude the dedication of that type of effort, without specific Congressional funding authorization. If, notwithstanding the Commission's policy views, the Congress does apply the foregoing concepts to the Secretary and the five projects, this Commission could not undertake the hearings prior to Congressional action approving budgetary increases. There could be a recruitment problem since these studies would demand highly specialized accounting and engineering talents.

For the reasons stated above, the Commission does not favor enactment of this bill. The views expressed herein are those of the EPC and do not necessarily reflect the views of the Administration.

Sincerely,

JOHN N. NASSIKAS, *Chairman.*

Mr. JOHNSON. Our first witness that was scheduled this morning is the principal author of H.R. 14221, Hon. John E. Moss. He was called to Sacramento and is in California as of now. We have here his counsel from one of his subcommittees that he serves on, Mr. Phineas Indritz, who will be called to the witness stand and give us the statement of the Congressman at this time.

Mr. Indritz.

STATEMENT OF HON. JOHN E. MOSS, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF CALIFORNIA, AS GIVEN BY PHINEAS INDRTIZ, COUNSEL TO MR. MOSS

Mr. LUJAN. Mr. Chairman?

The CHAIRMAN. Yes.

Mr. LUJAN. Since we have used the extra time that we had to read the report which was submitted, perhaps Mr. Indritz could summarize it.

The CHAIRMAN. You know, I arrived late this morning and it would be easier for me to follow the reading of the report. I have not had time to read it yet.

I would like to have it read into the record. Mr. Moss wanted me to set the hearings over but I said that was impossible due to our schedule. But I did assure him that his statement would be read in full, for the record, by the person he designated.

Mr. INDRTIZ. Mr. Chairman, members of the subcommittee, Mr. Moss regrets that he is unable to be present. He asked me to thank you very much for the opportunity to testify in support of this bill, which he, and you, and 13 other Members have introduced.

I will now read the text of his statement as he had prepared it and approved it.

This bill would authorize and direct the Federal Power Commission to review the increases in electric power rates which the Secretary of the Interior promulgated on November 1, 1973, for electric power sold at five Bureau of Reclamation projects.¹

The Federal Power Commission now reviews rate schedules filed by numerous utilities for sale of wholesale power. It also reviews the rate schedules for electric power sold by three of the four power marketing agencies of the Interior Department, namely, the Bonneville Power Administration, the Southwestern Power Administration, and the Southeastern Power Administration. It has not heretofore reviewed the rates promulgated by the Department's fourth power marketing agency, the Bureau of Reclamation, except incidentally when the Commission reviews rate schedules filed by utilities which purchase power under contract with the Bureau of Reclamation.

This bill would not authorize the Federal Power Commission to review all Bureau of Reclamation rate schedules. Its purpose is much more limited. It provides for FPC review of only the rate schedules promulgated by the Secretary of the Interior on November 1, 1973, for the five specific projects I mentioned a moment ago.

The Bureau of Reclamation now sells electric energy from these projects to municipalities, irrigation and utility districts, cooperatives,

¹ The five projects are: Central Valley, Colorado River Storage, Parker-Davis, Eastern and Western Divisions of the Pick-Sloan Missouri River Basin Program, and Rio Grande.

and State and Federal agencies in 14 States. On January 27, 1973, the Interior Department announced its intention to increase the rates for power sold from these projects effective on January 1, 1974. In making that announcement, the Interior Department officials provided no data to support the proposed increases. Indeed, they admitted that they still had not "determined" the amount of the increases. They said only that "when the detailed computer studies" were completed the Bureau's officials would "explain" them to the customers at the Bureau's regional offices.

The Conservation and Natural Resources Subcommittee on which I serve believed that such meager procedures of public disclosure and review would be quite inadequate. Therefore, on February 2, 1973, Subcommittee Chairman Henry S. Reuss, Congressman Paul N. McCloskey, Jr., and I sent a joint letter to the Secretary of the Interior, requesting that the Department make available to the subcommittee and to the customers various studies, documents, and other memoranda pertinent to the rate increases. After considerable delay, the Department grudgingly made available some materials, principally those which were specifically requested. But if our subcommittee or a customer was not aware of a particular document and made no request for it, such document remained hidden in the files. In short, the Department forced Bureau customers to go on fishing expeditions to get information which the Interior Department and Bureau of Reclamation should have made available long earlier. Only through extensive searching and inquiry were they able to find many pertinent documents that Interior had not released to the public before its so-called public hearings were held.

In our February 2 letter to Interior, we also expressed concern about the Department's hearing procedures concerning the proposed rate increases. We said:

We are concerned about the adequacy of procedures announced in the press release to enable review and comment on the proposed rate increases and studies by Bureau customers.

The Bureau's power rates at the projects mentioned in the press release are not subject to the formal review procedures of the Federal Power Commission, unlike rate changes for power marketed by the Bonneville Power Administration and the Southwestern Power Administration. Thus, the Department must establish its own formal procedures for such review. But apparently this has not yet been done, nor does it appear to be contemplated. The Department's press release merely states 'that when the detailed [Bureau] computer studies are completed the results will be made available . . . for review by customer groups', and that knowledgeable Bureau personnel 'will explain the completed studies and results to preference customer groups'. This informal, limited, off-the-record, hit-or-miss procedure is not satisfactory.

We think the Bureau's customers, consumer groups, and other members of the public ought to have the opportunity to review, and if they disagree, to challenge the rate increases and the underlying studies through formal procedures, including public hearings with a record and opportunity for presenting and cross-examining witnesses. As the press release notes, the Bureau's 'power rates have been held constant' for a long time. A major change in rates after such a long 'constant' period deserves more and broader formal review procedures than those suggested in the press release.

* * * We therefore request that you advise us by February 28, 1973, what formal procedures will be afforded and in what time frame, to enable such review and challenge before the effective date of the proposed rate increases, not only by Bureau customers, but by all segments of the public.

But Interior did not adopt such procedures. Instead, in a March 9, 1973, letter to our subcommittee, the Department wrote that it planned only to hold "informal customer meetings" to explain these increases. The Department added that if there is enough "public interest following the open meetings with customers" the Department "will be pleased to entertain public hearings in order to provide full disclosure."

In that letter, the Department also promised a minimum of 6 months review "to obtain a thorough understanding and resolve reasonable difference." That promise was never kept. The review was shortened to less than 5 months and no effort was made to "resolve reasonable differences."

The Department never held the informal meetings. Instead, it provided only a 1-day hearing for each project, and specifically mandated in advance that "No questions should be answered" by Bureau officials. Thus, the customers were deprived of the opportunity to question Bureau experts on the record about the bases for the rate increases.

When our subcommittee protested this lack of any formal procedures, the Department, in a June 21, 1973, reply, stated that no public hearing "is required by law" and that:

We see no need for the expense, delay, and rigidities that formal proceedings, with such features as sworn testimony, cross-examination, rules of evidence, and written briefs would entail.

Mr. Chairman, our subcommittee disagrees with Interior. We are concerned, not with the negotiations of a new contract, but with the Government's proposal to modify existing contracts unilaterally. Interior argues that this involves the matter of fixing the price of the sale of electric power and energy produced at Federal dams, and that this is a form of Federal property, the disposal of which is governed by article IV, section 3 of the Constitution. Interior states that the authority given by the Constitution to Congress "to regulate the disposal of Federal property is exclusive and without limitation." But Interior, unlike Congress, is not cloaked with such unlimited authority concerning the disposal of Federal property. Whatever authority Interior has to modify existing contracts, it must be exercised fairly and in accordance with the due process clause of the constitution.

But Interior has not afforded the customers even the semblance of "due process." Its hearings were a sham. Under strict orders from Interior officials in Washington, the Regional Director of the Bureau opened the July 10 hearing in Sacramento on the Central Valley project increase by stating (p. 3 of transcript):

Let me stress again that we are here to receive your comments on the proposed power rate adjustment. No examination of witnesses will take place today, nor will the Bureau undertake the answering of question[s] during this hearing.

Moreover, Interior has not acted fairly in modifying the rate increase. The Interior Department's Assistant Solicitor for Power has repeatedly criticized the Department's rate proposal and described it as arbitrary.

First. In a May 23, 1973 memorandum to Deputy Assistant Secretary Wilson, Assistant Solicitor Richard Peiz noted that the Depart-

ment's draft brochure on the CVP showed that the proposed rate would result in a reserve of "\$361 million against unpredictables in project repayment." He wrote:

The amount of this reserve will be even higher if a higher rate is approved than the one used in this preliminary study. *A reserve of this magnitude will be severely criticized.*

The report should contain a more careful and believable explanation than simply that it is designed to cover "unpredictables." It may be that the reserve serves the function of allowing repayment of additional irrigation features which it is anticipated will be authorized in the future. If so, the report should explain this. *The law requires the Secretary to set the lowest possible rates to consumers consistent with sound business principles. It is consistent with sound business principles to have a reserve for contingencies but \$350 million or more seems excessive.* (Emphasis supplied.)

He also noted that the Department's "discussion of alternatives is incomplete." He said that one of the—

* * * key alternatives is not discussed, namely, whether the rates should be further increased from the level shown in the April study in order to avoid a deficit in meeting interest payments during a short period of about two years. *As I explained to you, in my opinion section 9(c) of the 1939 Reclamation Project Act does not require that interest costs be recovered in each and every year. A short-run deficit in recovering interest costs would be permissible. It is hard enough to justify the rate increase shown in the April 1973 study without going higher merely to cover interest expenses for a two or three-year period out of the sixty years in the study.* (Emphasis supplied.)

Second. On October 2, 1973, Assistant Solicitor Pelz wrote a memorandum (marked "Administratively Confidential") to Assistant Secretary Horton who has made all of the decisions on the rate increases. Assistant Solicitor Pelz starts off by giving the following, eminently sage, advice to the Assistant Secretary:

1. You may not be arbitrary, capricious, or abuse your discretion.
2. You may not exceed your statutory authority or act in violation thereof.
3. You must follow applicable regulations until they are changed.

He then proceeded to point out that the Assistant Secretary's decision of May 23, 1973, to double the rate increase for Central Valley project customers from 25 percent to 52 percent "was arbitrary from a legal point of view, and would be set aside in a court action." He said:

The arbitrariness arises because the Department is attempting to handle a unique and significant situation with a policy developed for ordinary circumstances. The clothes will not fit.

In the same memorandum, Mr. Pelz again returned to the reserve or surplus problem he referred to in his May 23 memorandum, saying:

The study published with the June brochure shows an 'earned-Surplus Cumulative' at the end of the payout period of \$496 million. A surplus of this magnitude creates a serious legal problem because the applicable power marketing statutes generally authorize you to set rates only at such levels that will recover costs, but not so high as to make a profit. It is important to demonstrate, therefore, first, that whatever surplus appears in the rate and repayment study finally decided on, this surplus is the *result* of the rate decisions taken for other grounds and not the *cause* of such decisions, except that a surplus to meet reasonably probable contingencies could be justified.

Second, even where the surplus is a result and not a cause, it is important that it not be unreasonably large. If it is too sizable, it has a feed-back effect; that is, it would influence the court to take a second look at the decisions which, in fact, did determine the rate, to see whether they really are in accordance with the statute if they have the result of producing such a large surplus.

Mr. Chairman, the Department has thus far failed to rid itself adequately of the deficiencies cited by Mr. Pelz. These deficiencies give added weight to the charge many customers and I make against these rate increases, namely, that the Department has acted in a high-handed and arbitrary manner and with total disregard for the public interest and its duties under the Constitution. This charge is further substantiated by our subcommittee's hearings of last January and by the Comptroller General's report to our subcommittee of November 19, 1973, which criticized several of the criteria and procedures used by the Department in its rate increase for Central Valley project customers.

Despite this, the Department, in cavalier fashion, promulgated the rate increases on November 1, 1973, effective April 1, 1974. Assistant Secretary Horton's action of splitting the increase for Central Valley project customers into two stages—the first effective on April 1, 1974, and the second on January 1, 1977—does not change the basic unfairness of the rate increase.

In a March 14, 1974, letter to our subcommittee, Mr. Morton said that as a result of its review of the Central Valley project rate increase following our subcommittee hearings, the Department is "now considering possible modification of the second step in 1977." But the Department has not withdrawn its promulgation of that second step. The customers must assume that it will be effective as promulgated last November. They must plan accordingly. This is an imposition. It is government by men, not laws. It cannot and should not be tolerated by Congress or the courts.

The setting of electric rates is, of course, a highly complex and technical process. Nevertheless, it is a process which has many well-established guidelines. In this country, we have come to accept the notion that the rates of public utilities for such essential commodities as electric power should be fair and reasonable and that they should be subject to review by public bodies such as the Federal Power Commission or public utility commissions. The history of the Department's inadequate procedures and departure from well-established rate making criteria certainly warrant applying this same principle of review to the rate increases which the Secretary of the Interior promulgated on November 1, 1973. H.R. 14221 will insure this. I urge its quick adoption.

I have several detailed comments on the technical provisions of the bill, as well as a suggested clarifying amendment.

Section 1 of the bill sets forth the highlights of the sordid history of the Interior Department's mishandling of the rate increases for customers of the five Bureau of Reclamation projects. I urge that this history be retained in the bill when it is reported so that all Members will be able to see for themselves why the legislation is so essential.

Section 2 directs that the Federal Power Commission shall, with the assistance of the Comptroller General, review the rates promulgated by the Secretary of the Interior on November 1, 1973, in order to determine their reasonableness and their consistency with law and regulations. After completing its review, the Commission shall either approve the schedules or recommend modifications thereto. The Commission's review shall be made on the record and after opportunity for public hearings pursuant to the provisions of the Federal Power Act, and shall be subject to judicial review.

H.R. 14221 simply provides a method for reviewing the Interior Department's rate increases at these five projects, and if they are found improper, for their modification. The rates will not be affected by this bill until the review is completed. There are some who suggest that the new rates should be suspended pending this review. However, since it appears that some increase may be needed, I think the taxpayers should not have to shoulder the cost of these power sales while we wait for the FPC to review the rate increase. I have therefore included adequate provision in the bill for Interior to give refunds or credits to the customers if the FPC recommends a rate reduction.

However, to avoid the possibility of undue delay in the review procedure, section 4 of the bill provides that if the FPC does not issue its decision prior to June 30, 1975, the rate schedule promulgated on November 1, 1973, will be suspended and be replaced by the schedule in effect on March 31, 1974, until the FPC issues its decision. If the FPC recommends a modification in the rate schedule, the Secretary will be required under section 5 of H.R. 14221 to abide by the Commission's decision retroactive to April 1, 1974, and, as I have said, to provide any refund, credit, or other adjustment to comply with the FPC decision.

This bill will apply to all customers affected by the Interior Department's rates promulgated on November 1, 1973. Some customers—namely, those represented by the Northern California Power Agency—have already filed suit against the Secretary of the Interior, challenging the Central Valley project rate increase on a variety of grounds. I am informed that the Sacramento Municipal Utility District contemplates seeking a judicial determination of its right under its present contract to be free from rate increases until May 25, 1978.

This bill is not intended to deprive any customer of its legal rights. Thus, section 5 specifically states that any new rate schedule resulting from the Federal Power Commission's decision shall be effective only as to those customers for which the rate schedule was "validly promulgated on November 1, 1973." If any rate schedule then promulgated was not valid as to any customer, whether because it violated any law or because it was contrary to any contract, this bill is intended to preserve the customer's right to challenge the application of the Secretary's rate schedule or the FPC's modification thereof.

It has been suggested to me that the first sentence of section 4—which states that the "rate schedules promulgated * * * on November 1, 1973 * * * shall continue in effect" pending FPC review—might be construed to deprive some of the customers of their right to test the validity of those rate schedules in court proceedings. It is certainly not my intention to deprive any customer of such right. Therefore, to avoid the possibility of any such erroneous interpretation, I recommend that the first sentence of section 4, preceding the Provided clause—that is, in lines 20-23 on page 4 of H.R. 14221—be revised to read as follows:

Sec. 4. The rate schedules promulgated by the Secretary on November 1, 1973, for each of the five projects referred to in this Act shall continue in effect—and at this point the following language will be added—"*as to all customers for which such rate schedules were validly promulgated on that date*". The sentence then continues, "pending review thereof pursuant to this Act * * *."

[The words italicized are to be added to the present language of the first sentence of section 4.]

Mr. Chairman, the basic problem that has arisen in connection with the Interior Department's rates of November 1, 1973, stems from the fact that the Secretary has failed to provide adequate opportunity for public hearings, review, and comment. It is a public agency responsible to the people. It should not be autocratic or arbitrary. It should give reasons for its decisions. It should give the public an opportunity to know what those reasons are and to comment upon them. I firmly believe that if the Department had complied with our February 1973 request, we would not be here today and our subcommittee and the General Accounting Office would not have had to spend long hours trying to ferret out the full details of these rate increases.

Our experience with the Department's procedures in connection with the rate increases it promulgated for these five Bureau of Reclamation projects demonstrates that the Department has failed to meet elemental standards of fairness. Accordingly, section 6 of H.R. 14221 would require the Secretary of the Interior to publish and adopt regulations applicable to future rate increases which will provide for opportunity for adequate public hearings and written decisions on the record concerning any electric power rate increases hereafter proposed by the Department pursuant to the Reclamation Project Act of 1939.

Mr. Chairman, I thank you for permitting me to present this statement. I hope your committee will report this bill favorably as early as possible, in order to expedite the Federal Power Commission's review of the Department's rates of November 1, 1973.

Mr. Chairman, this concludes Mr. Moss' statement. He has asked me to be available to you for any questions that you may have.

Mr. JOHNSON. I want to thank you, Mr. Indritz, for reading Congressman Moss' statement. It is a very complete résumé of what has taken place since the first notices of the rate increases were made known to us throughout the areas that are covered, including the Central Valley project of California where there are many preference customers that are affected.

I have followed the statement as you read it very closely. I am well aware of the hearings that were held in California by the Bureau people and the hearings that were held by the subcommittee of the Committee on Government Operations in Washington. I would say that Congressman Moss has brought to our attention some information that I did not hear anything about, either in the Sacramento hearings or in the hearings before the Government Operations Subcommittee, at least while I attended.

Now, you quote here from an assistant solicitor by the name of Pelz some very important information. Is this the first time that Congressman Moss has had this information available to him?

Mr. INDRITZ. The information became available to the subcommittee after the hearings. We have copies of the memorandums referred to, if you desire.

Mr. JOHNSON. It was not made a part of the subcommittee hearing record as I recall?

Mr. INDRITZ. That is correct.

Mr. JOHNSON. I did not see anything or hear anything about it at that time. Now, is that person still with the Department of Interior?

Mr. INDRITZ. It is my understanding that he is.

Mr. JOHNSON. I really have no questions to ask on the statement. I am fairly familiar with most everything that has been brought to light in the statement, with the exception of that particular information.

To the best of my knowledge, I have never heard of it before. I followed your reading concerning the information that was made available to the Government Operations Subcommittee. Was that made available to you by the Bureau of Reclamation?

Mr. INDRIITZ. The staff of the subcommittee has been continuing its examination into the subject matter of the hearings that our subcommittee held. We have continued to examine this matter and to request information from the Department of Interior. Those two memorandums were part of the information that became available to us.

Mr. JOHNSON. Submitted to you by the Bureau of Reclamation?

Mr. INDRIITZ. By the Department of the Interior.

Mr. JOHNSON. The gentleman from Georgia, Mr. Stephens.

Mr. STEPHENS. Thank you, Mr. Chairman. I have been listening to the statement and appreciate having that opportunity.

Also, I have read the accompanying report from the Comptroller General and from the Department of Interior.

The only question that I have and would like to satisfy my mind on is this, Mr. Chairman: the question of the rates seems to at the present time be contested in the courts?

Mr. INDRIITZ. Only with respect to the Central Valley project so far as I am aware. A lawsuit has been filed by the Northern California Power Agency and a number of municipalities and one rural electric cooperative in northern California. The Sacramento Municipal Utility District, which serves primarily the city of Sacramento, is contemplating getting its particular questions resolved through judicial action, but as far as I am aware, as of now no suit has been filed.

Mr. STEPHENS. Would the suit be in the form of an injunction to prevent the assessment of the new fee, or new rates?

Mr. INDRIITZ. There are apparently some technical questions as to the format of such a suit and it is my understanding that the general manager of the Sacramento Municipal Utility District has requested the Interior Department to file a suit instead of having the Sacramento Municipal Utility District do so. If the district files a suit, it would probably have to be in the court of claims which has jurisdiction only with respect to refund of money, or based on a contract, and would not have authority to issue any injunction or a declaratory judgment. And for that reason Sacramento Municipal Utility District believes that all of the issues could be better explored in the forum of a Federal district court. But that would require the institution of suit by the Government. As I understand the district's present proposal, the district would withhold the increased charges in a separate escrow fund and then have the Government sue for the higher rates.

I do not think that any decision has yet been reached as to whether that procedure would be followed.

Mr. STEPHENS. Would the court proceeding provide an adequate remedy for the people affected rather than the legislation?

What is the reason for thinking that legislation would provide a better remedy than the court proceedings?

Mr. INDRIITZ. The court proceeding, of course, would be limited. It would relate only to whether the rates were in violation of law or contract. It would not correct the deficiencies which have been disclosed thus far, in the opinion of the Conservation and Natural Resources Subcommittee, concerning the procedures of the Interior Department. For that reason, section 6 of the bill, which goes beyond simply these five projects, would prescribe a procedure for public review and comment in the future on all rate increases by the Interior Department. The first five sections are based on the assumption that the Department, as one of the parties, ought to have its rates reviewed by a public agency and not be the sole determinant of whether rates are to be increased without adequate opportunity for the customers to question the basis for the November 1, 1973, rate increases and to be able to examine the witnesses to find out what were the reasons for the rate increases and to present their comments. But, section 6 would apply beyond simply these five projects or the November 1, 1973, rate increase.

Now, your other question as to whether a court action would be an adequate remedy, rather than providing for a review by the Federal Power Commission—that is a question of judgment and I am not entirely prepared to say that a court decision would provide an adequate remedy. But, the principle underlying Mr. Moss' bill, as he explained it to me, was that the Federal Power Commission, an agency set up to review rates, has the technical proficiency. It is accustomed to doing it. It actually reviews the rates of four power marketing agencies of the Interior Department—the Bonneville Power, the Southwestern, the Southeastern, and the Alaska Power Administrations. This bill would simply require the Commission to review the rates of one more agency, namely, the Bureau of Reclamation. Such review, as stated in Mr. Moss' bill, would be in conformity with the current procedures under the Federal Power Act.

Mr. STEPHENS. And the only objection, as I understand it, they have to that is the fact that it would increase their staff and their budget? Not that they do not have the expertise to do it, but the fact that they do not have the staff to do it?

Mr. INDRIITZ. That is my understanding of the Federal Power Commission position.

Mr. STEPHENS. I mean, as far as it is not that they do not have the ability to do it, it is, insofar as their normal duties are concerned, that they just do not have the staff to do it?

Mr. INDRIITZ. That is correct, as I understand it.

Mr. STEPHENS. Thank you, Mr. Chairman.

Mr. JOHNSON. The gentleman from New Mexico, Mr. Lujan.

Mr. LUJAN. Thank you, Mr. Chairman.

I think that was an excellent statement and it sets out the case very well, or at least one side of the proposition. I gather that the real basis for this, although you used a lot of different adjectives to describe the action of the Department, is that it is a unilateral decision to increase rates by the Department without any input from any of those affected. That the Secretary or Undersecretary decided that they were going to triple, or quadruple, or whatever the rates and there was just no opportunity to combat that sort of thing?

That is basically it?

Mr. INDRIITZ. That is correct, Mr. Lujan. In this particular case, in relation to this rate increase, there was some opportunity for customers to make an input, but only after a great volume of protests, both by our subcommittee and by customers, and the expenditure of a considerable amount of time and effort by our subcommittee, the Comptroller General, and the customers. Because there is no procedure within the Department for any such review, the information that was initially made available was highly sketchy, quite inadequate. The rates had not been set or determined on the basis of the data they had. The data were incomplete and it was done entirely unilaterally. In that respect it is different than the negotiation of a contract where both parties have an opportunity to have their say. Here the rates, the rate changes, were made unilaterally. Unlike the authority exercised by a party to a contract, a Government agency should act in accordance with the Constitution. Due process may not be a requirement for the private contractor but it certainly is a requirement for a public agency. The position taken by our subcommittee was that fairness, that due process, had not been adequately provided for either by the procedures or the rate changes made in this case.

Mr. LUJAN. All right, the Federal Power Commission says that they do not want it because they do not have the manpower. How many other projects besides these are there that they would have to bring under the Federal Power Commission? We are talking about what here, four or five of them?

Mr. INDRIITZ. Five projects.

Mr. LUJAN. Five. How many others are there that would really accelerate that workload for them, increase their workload for them?

They say that we do not want to take over this responsibility, it is too much work.

Mr. INDRIITZ. The bill does not do that. The bill asks them to examine only the rates applicable to these five projects.

Mr. LUJAN. I understand that. But, if they apply to the five, it is only logical that we apply it to all of them. We cannot say just these five here—for the future now—talking about reviewing the five—that the rates were promulgated on, but for the future really what we ought to do is see that this thing does not happen again. So, my question is how many other of these generating projects are there that the FPC would have jurisdiction over?

Mr. INDRIITZ. Mr. Lujan, I do not know the precise number of the power generating projects of the Bureau of Reclamation. But, the Commissioner of Reclamation is here, and I am sure that he has that information at his fingertips.

Mr. LUJAN. I will ask him that when he is up.

Mr. INDRIITZ. I just do not happen to have that handy with me.

Mr. LUJAN. If the FPC does not want it then, do you have any other solution, like perhaps providing guidelines that the Department of Interior must follow in promulgating rates? Would that be acceptable to Mr. Moss, as far as you know?

Mr. INDRIITZ. On the basis of the conversations I have had with Mr. Moss, it is my understanding that it might be an alternative form of legislation to provide strict statutory guidelines for criteria for the Department to follow, in applying its review procedures with relation to the rate increases.

But, he would certainly want to study that in much more detail for the reason that putting such criteria into statutory form may not be a wise legislative decision. It may freeze the criteria. It may not be able to take into account other variables and he, therefore, laid aside that suggestion in favor of having the procedure which this bill sets forth, namely, a review of the criteria actually applied by the Department in relation to these five projects.

Mr. LUJAN. Thank you. Thank you, Mr. Chairman.

Mr. JOHNSON. The gentleman from Oregon, Mr. Dellenback.

Mr. DELLENBACK. Thank you, Mr. Chairman. This has been helpful testimony in setting forth Mr. Moss' view, and you have given it well.

May I ask a couple of questions which are based in part on the letter from the Federal Power Commission. The chairman has made a request that this be part of the record, and I do not gather, Mr. Chairman, that we have a witness from the FPC coming, do we?

Mr. JOHNSON. Not that I know of. The only Departmental witness would be Mr. Stamm, as far as we know.

Mr. DELLENBACK. All right. I appreciate knowing that.

I do not know whether you have had a chance to look at the May 16 letter from the Federal Power Commission in which they set forth their objections to the bill. Have you?

Mr. INDRIITZ. I have skimmed over it very rapidly.

Mr. DELLENBACK. Well, in addition to the concern that was expressed there by the FPC, and that Mr. Stephens referred to about the dollars, the 50 man years, and staff and personnel and the like, there were a couple of policy objections that I think you ought to have a chance to comment on. They say that the laws that exist provide for accountability of the Secretary to the Congress and they feel that the proposed bill would really dilute that accountability. That is on the first page, the first major paragraph on the first page. Notice that they say that the accountability of the Secretary to the Congress comes under numerous pieces of legislation and by interjecting into the Secretary's responsibility the FPC, that would, in their opinion, dilute the administrative line of responsibility. Then they go on further and make the point that the Secretary's legal responsibility and statutory standards governing the marketing of power and water under the reclamation laws are not the same as the standards and the procedures of the Federal Power Act.

Would you have any comment on that?

Mr. INDRIITZ. Yes, Mr. Dellenback. The paragraph that you referred to in the Federal Power Commission letter is really quite inconsistent with its own present practice. It now reviews the rates of the Southeastern Power Administration, the Southwestern Power Administration, the Bonneville Power Administration, and the Alaska Power Administration, all of which are under the Secretary of the Interior, all of which relate to the marketing of hydroelectric power and energy, and water for irrigation.

That is now under the Secretary. So, the FPC is actually now engaged in looking at rates that are administered by, made and administered by the Secretary of the Interior.

Mr. DELLENBACK. So you feel——

Mr. INDRITZ. So there is nothing new with respect to adding the Bureau of Reclamation for review purposes. Indeed, it is my understanding that the Interior Department witnesses are about to testify that they would have no objection to having the FPC review the Bureau of Reclamation rates. All they want to do, however, is have that review simply in the form of review for consultation purposes, but without the procedures for fairness and due process that are now present in the Federal Power Act. And a major purpose of this bill is to see to it that the procedures of the Interior Department, which were so woefully inadequate when the rate increases were first announced, are improved.

Mr. DELLENBACK. But, it is your feeling that, speaking to the first point of the FPC, that if it is valid, then it is also applicable to certain other procedures now being followed and that if it is all right under the present procedures, then it would not be made any worse by this particular bill?

Mr. INDRITZ. Yes, sir.

Mr. DELLENBACK. All right. They go on further and they indicate in their paragraph which is the third paragraph on the first page that the Bureau of Reclamation uses repayment studies as a major factual predicate for its ratemaking proposals.

The Commission employs the test of the Federal Power Act—just reasonable and not unduly discriminatory or preferential. Then, in their opinion, apparently this bill which is before us appears to blend those two standards. Would you have any comment that you would make for the record on that?

Mr. INDRITZ. I do not think that there is any inconsistency between the fact that the Bureau of Reclamation uses repayment schedules as a major factual predicate for its ratemaking proposals, and the standard under the Federal Power Act; namely, that the rates must be just, reasonable, and not unduly discriminatory or preferential.

Those are in no way inconsistent standards. The Bureau of Reclamation can continue to use repayment schedules as a major factual predicate.

But, those standards and the rates that result from them must come out to be just, reasonable, and not unduly discriminatory or preferential.

Now, I have not mentioned, because Mr. Moss' statement was limited solely to this bill, that there are elements of unfairness and undue discriminatory rates in at least certain areas of the Central Valley project. As a result of these rate increases, the same electric power—because it is impossible to distinguish between electrons and between kilowatts—is now being sold at two different rates, one rate to the preference customers and another rate to the Pacific Gas and Electric Co., all coming out of this same project's power.

Now, the excuse there, the rationale there, is that the difference in rate to the Pacific Gas and Electric Co. has been set by contract with respect to thermal power purchased from Centralia and blended into the Central Valley project.

At the hearing that our subcommittee had in January, the suggestion was made that an effort be made to eliminate that discrepancy, which can be done by suspending the rate increases until the rates

under the contract of the Pacific Gas and Electric Co. are reviewed in 1976. That suggestion was not followed by the Interior Department so that you now have different rates, one for the electricity going to the preference customers and the other for electricity going to the Pacific Gas and Electric Co.

What I am trying to say is that there is no inconsistency between the fact that the Bureau of Reclamation will use repayment studies as a factual predicate, and the requirement under the Power Act that the rates must be reasonable, just, and not unduly discriminatory.

And I might add that such criteria—just, reasonable, and not unduly discriminatory—are actually a constitutional requirement. As a matter of due process under the Constitution, no Government agency may act unjustly, unreasonably, or unduly discriminatorily.

Mr. DELLENBACK. Are you telling us that in your opinion the procedures used by the Bureau of Reclamation and the procedures under the Federal Power Act and the procedures under this bill are identical for determining rates?

Mr. INDRIITZ. At the present time?

Mr. DELLENBACK. My question is, are you telling me that the procedures used by the Bureau of Reclamation under its authorizing legislation to set rates and the procedures used in the Federal Power Act to determine rates, and the procedures of section 2 of this bill are identical?

Mr. INDRIITZ. No, they are not because—

Mr. DELLENBACK. Well, now, that is the point. As I read this letter, the letter says those procedures are different.

Mr. INDRIITZ. But that is precisely what this bill is intended to do—to correct that discrepancy.

Mr. DELLENBACK. Let me take a step back then. Are you indicating in your opinion, the procedures followed by the Bureau of Reclamation in setting rates and the procedures under the Federal Power Act are identical, or do they use different criteria for determination?

Mr. INDRIITZ. They are not identical. And as is indicated in the history of the past 2 years, and the hearings held thus far, the Bureau of Reclamation sets its rates on the basis of its own rate and repayment schedule without—

Mr. DELLENBACK. Excuse me just a moment. Don't snow me with words. Let me ask you a question and then you reply to it if you will.

Mr. INDRIITZ. I am trying to.

Mr. DELLENBACK. You are indicating to me that the procedures followed under the law that pertains to the Bureau of Reclamation for the setting of rates provides for one procedure for ratemaking?

Mr. INDRIITZ. Yes.

Mr. DELLENBACK. The procedure under the Federal Power Act, using the criteria of just, reasonable, and not unduly discriminatory or preferential is a different procedure, is that correct?

Mr. INDRIITZ. The procedures are quite different.

Mr. DELLENBACK. All right, they are different.

Mr. INDRIITZ. Yes. They are different.

Mr. DELLENBACK. They are different. Now, under this bill, under section 2, and not only the procedures are different but the criteria applied are different, is that correct?

Mr. INDRIITZ. The criteria are different and the procedures are different.

Mr. DELLENBACK. Under those two?

Mr. INDRLTZ. That is correct.

Mr. DELLENBACK. Now, under the procedures and criteria set forth in section 2, there is a third set of criteria. That is correct, is it not? Because the language of section 2 says "determining reasonableness and adequacy," and I don't find "adequacy" in either set of language, for either the Bureau of Reclamation or the Federal Power Act. And also in section 2, in line 24, page 3, it says "consistent with applicable requirements of law and regulation," and I do not find that in the law and I do not find that language anywhere in here. I am not arguing the point, I am just trying to understand it. And if I understand what the Federal Power Commission is saying, and I am not arguing their case for them, but I understand what they are saying is part of the confusion that would be brought about by this bill is, at the present time, the Bureau of Reclamation is supposed to walk a certain road. At the present time the Federal Power Act requires the FPC to walk a different road.

This bill comes along and sets up a third road. And they say that this makes for some additional confusion. And is that valid?

Mr. INDRLTZ. No, sir.

Mr. DELLENBACK. Well, I do not understand where it is not valid, because your reply to my first question was "Yes." My question is: Is the procedure followed under the Bureau of Reclamation and the criteria used different than that under the Federal Power Act?

Mr. INDRLTZ. The procedures—and I am speaking simply to the procedures—

Mr. DELLENBACK. Well, let me swing from procedures. I am not really talking procedures. Are the criteria used for determining rates the same? Are the criteria used for rate determination by the Bureau of Reclamation, set by act of Congress, the same criteria for rate determination provided for under the Federal Power Act? Are they different measures?

Mr. INDRLTZ. Well, when you are talking about criteria, when you are dealing with repayment of Federal facilities, the criteria that would be applicable to the Federal projects would be different simply because the statutes which created those Federal projects may have different requirements.

Mr. DELLENBACK. But, so the answer is they are different then because we have written two different statutes, I assume, I assume the Congress has written one statute—and I was not here at the time we set those procedures for the Bureau of Reclamation—but I assume that the statute that created the Bureau of Reclamation and set up a certain method, not only procedurally but by the application of certain criteria. Those are different measures than the Federal Power Commission uses under the Federal Power Act.

Mr. INDRLTZ. Mr. Dellenback, the situation is highly complex.

Mr. DELLENBACK. I understand that and I recognize I am not an expert in the field.

Mr. INDRLTZ. Under the Federal Power Act, there is a requirement that the accounting procedures of the Bureau of Reclamation must be in conformity with FPC requirements. The Federal Power Commission has never enforced that statute. We have asked the Federal Power Commission why it has not been enforcing that statute and the Commission has given us no adequate explanation. The fact is

that the Federal Power Act specifically refers to power generating entities that are Federal and, therefore, there is a congressional appreciation of the necessity for dovetailing FPC requirements and the ratemaking, accounting procedures, and the recordkeeping of the Bureau of Reclamation. Some of this accommodation has already taken place with respect, as I mentioned, to the four other power marketing agencies—Southwestern, Southeastern, Alaska, and Bonneville Power Administrations.

What this bill proposes is that the Bureau of Reclamation also be geared into the FPC review, and in conformity with hearing procedures which are embodied in the concept of due process of law. This concept ought to be, by virtue of the Constitution, implicit in the ratemaking procedures of the Interior Department, but which the Interior Department has not followed it.

Mr. DELLENBACK. I am trying to separate procedures from the criteria, because I am troubled by the procedural situation. But I am not sure because we are troubled by this that we are not being asked to do something which substantively gets more confusing. I am approaching it *de novo* and I have read these things and it seems to me that we are reaching out to straighten out something largely procedural which we do not know whether we are going to object to substantively, and the objection in Mr. Moss' testimony is largely one of procedure. Now, if we set procedure aside and say all right, if we require the FPC to move into the problem and start to do something, as the bill would provide, the FPC comes to us and says it would be a bad move.

Now I am trying to find out why they say it would be a bad move, because they do not have a witness here to give us anything more than is in their letter. And I am going to, on the particular point, and I concede again, you see, that this is not something on which I am an expert. I am just approaching this as a lawyer trying to balance these things off against each other to see if what they say is accurate. It could be a confusing thing. They say in effect that we are the wrong people because if you put us into this thing, we normally follow a certain test, we look to determine whether something is just, whether it is reasonable, whether it is not unduly discriminatory or preferential, and those are the principle criteria we use to measure. They say those are not the measurements you and the Congress wrote in the Bureau of Reclamation statute you set up.

Mr. INDRITZ. That is not so. The reason that I say that it is not so is because the Congress itself cannot write a law which is unconstitutional and when the Congress wrote a law which prescribed the functions of the Secretary of the Interior, implicit in that law is the requirement that the Government agency must act fairly, justly, and not unreasonably or unduly discriminatorily.

These are constitutional requirements which are inherent in the Interior Department's legislation. The complaint that Mr. Moss has set forth here is that the Department has failed to follow those constitutional requirements with respect to the procedures.

Mr. DELLENBACK. When I am done I will make a request relative to the FPC, Mr. Chairman. You are saying then that the statement of the FPC is in error on this particular point? Then they also go on, going on to that particular point, they say that the bill requires, in

looking into reasonableness and adequacy and consistency with applicable requirements of law and regulation, they say that is the test that neither the Bureau of Reclamation is required under statute to apply or the FPC is required to apply. Is that in error also?

Mr. INDRITZ. Mr. Dellenback, the phrase "consistent with applicable requirements of law and regulations" is obviously the kind of criteria that the Federal Power Commission has to follow in its review of the rates of the other power marketing agencies. They have to examine whether it is consistent with law and regulations. That is, in fact, the kind of requirement that any regulatory agency has got to follow.

Mr. DELLENBACK. Is the statement of the FPC in error or correct?

Mr. INDRITZ. The one question that I would like to review a little more carefully is about the word "adequacy" in this bill. Now, that, I would like to have the opportunity to study a little more. That possibly might be a little different or produce a difference.

But all of the other criteria in this bill, I respectfully submit to you, are requirements the FPC must either under the Constitution or as a requirement under law, and it is now being done with respect to other marketing agencies in the Interior Department.

Mr. DELLENBACK. So, you are telling us, in effect, that the statement of the FPC on this particular point is in error?

Mr. INDRITZ. I am not saying that they are in error, but what I am saying is that the conclusion to be derived from what they say does not follow.

Mr. DELLENBACK. Very well.

They go on also and they make on page 2 of their presentation the argument that procedurally the bill would apply to federally owned electric operations, the hearing and judicial review concepts which the Congress has determined should be applicable to the non-Federal utilities which the Commission regulates under the Federal Power Act. And then they raise at least some question about that. And they say section 6 is somewhat ambiguous as to whether the Secretary would have to follow FPC review procedures in subsequent rate reviews.

Mr. INDRITZ. I think that they are wrong on that. There is no ambiguity. Section 6 is very clear. It says that the Secretary would have to follow certain prescribed review procedures and they are set forth in section 6 in precise language.

Mr. DELLENBACK. OK. So, they are in error on that.

Then on the third principal policy question they raise, it is in the second full paragraph on page 2 of their letter where they say the application of these procedures to proprietary functions of the Secretary may raise substantial administrative problems for the Secretary in the light of the reclamation laws which he must administer. And they say at the FPC they do not administer those laws and the economic regulatory functions of the Federal Power Act are markedly different from the purposes of the reclamation laws.

Is there any validity to that point?

Mr. INDRITZ. I think that there is no validity to that paragraph. They are now reviewing the rates made by several agencies of the Interior Department. There are no administrative problems that the Secretary would incur, other than the requirement of setting up a review procedure which fully recognizes the rights of the customers, the States and the municipalities and the irrigation districts, and

Federal agencies. Also there were several Federal agencies that protested at our hearings in very bitter terms about the increase that was imposed upon them. The principal thrust of this bill is to cure the administrative defects within the Department's review procedures.

Mr. DELLENBACK. Before I have one last question, Mr. Chairman, may I make a request that we ask the FPC for a reply, after a copy of the transcript has been given to them, because there are three points now on which the witness has taken issue with the letter of the FPC, and I would be interested, as a member of the subcommittee, in knowing whether Chairman Nassikas stands with his statements in this regard or whether he concedes that the witness is correct and that Mr. Nassikas' statements are wrong on these three particular points.

I would request we make a copy of the testimony available to the Federal Power Commission and ask them to give us their concurrence therein or their refutation thereof.

Mr. JOHNSON. You have heard the request of the gentleman from Oregon.

Is there objection?

Hearing none, so ordered.

I am not so sure that you will not get back more confusion.

Mr. DELLENBACK. Yes, Mr. Chairman, and it is regretful that they do not have a person up here.

Mr. JOHNSON. Well, maybe they do.

Mr. DELLENBACK. It seems to me that certain of their points are valid and if they are not, I want them shot down.

Mr. JOHNSON. Is there anyone here representing the Federal Power Commission?

Mr. DELLENBACK. Well, they are not going to concede that now.

Mr. JOHNSON. I realize that.

Mr. DELLENBACK. And the other question, the last one, in order to be assured that I understand the question of whether or not what we are asking the FPC here to do is the same thing in the way of reviewing rate schedules that we are already asking them to under the other three marketing agencies of the Interior, that is, Bonneville and Southwestern and Southeastern.

Are we asking them to do the same thing relative to rate review under H.R. 14221 for the four elements that we are already asking them to do under those other three that I have referred to?

Mr. INDRITZ. No, sir.

Mr. DELLENBACK. We are asking them to do something different?

Mr. INDRITZ. Yes, sir.

Mr. DELLENBACK. Do I understand correctly that what we are asking them to do is to, in effect, not just give an advisory opinion, but to make a determination which will be followed on a mandatory basis, whereas that which we already do under the other three is advisory?

Mr. INDRITZ. Not quite. Not quite. Under the review that the FPC provides with respect to the other four power marketing agencies, the Commission can veto the rate increases or the rates. Then it goes back to the Interior Department for restructuring, and then the case has to come back again to the FPC for approval. It is a veto function.

This bill would authorize the FPC to modify the rates, to avoid this delay.

Mr. DELLENBACK. Is it not a fundamental change?

Mr. INDRIITZ. There is another major difference that I would like to explain, and that is that under the review procedure that the FPC provides for the other four agencies, it does not apply the procedures of the Federal Power Act which authorizes examination of witnesses, hearings, and so forth.

There are deficiencies in the current review that the FPC gives with respect to the rates of the Bonneville Power, Southwestern, and South-eastern. The Commission reviews the rates but does not allow customers to come in and ask questions. There is litigation now going on concerning that issue. The Government's motion to dismiss was denied in those cases. Although the cases are still in litigation, it may be even necessary to have legislative modification to assure that customers have an opportunity to ask questions and to present testimony on these increases which so substantially affect their pocketbook.

So, the procedures with respect to the other four agencies are not quite the same as under this bill. This bill would require that the rate increases of November 1, 1973, be reviewed under the procedures of the Federal Power Act with regard to hearings, for examination of witnesses and also judicial review. These procedures are now applied in the FPC's review of electric power rates if any of the Department's power marketing agencies, including the Bureau of Reclamation.

Mr. DELLENBACK. One minor technicality. You are referring to the other four. I thought Mr. Moss' testimony said that there was a total of four power marketing agencies, three of which are subject to rate review?

Mr. INDRIITZ. A typographical error. I am sorry, it should have added Alaska.

Mr. DELLENBACK. So there are really five?

Mr. INDRIITZ. Right. Yes.

Mr. DELLENBACK. And four are already covered?

Mr. INDRIITZ. Right.

Mr. DELLENBACK. So you are helping me with understanding this thing in saying that H.R. 14221 does not provide the same kind of review for this, for the Bureau of Reclamation that is already provided for the other four?

Mr. INDRIITZ. That is right.

Mr. DELLENBACK. The difference being that when you alluded to we now propose to go further and not give the Federal Power Commission a veto over rates, but actually the power to set the rate whereupon the Secretary must follow?

Mr. INDRIITZ. To modify the rates once they have been set by the Interior Department.

Mr. DELLENBACK. And having modified them, that which they modify to must be followed by the Interior?

Mr. INDRIITZ. In this particular case namely, as to the rate increases of November 1, 1973. The bill does not at this point—Mr. Moss has not proposed at this point that the Bureau of Reclamation have all of its rate increases made subject to FPC review.

Mr. DELLENBACK. So, this is a single shot operation to take care of this particular and, in effect, to give the FPC the power to move in and set the rates on this particular contention and take the power away from the Secretary?

Mr. INDRITZ. That is correct.

Mr. DELLENBACK. Thank you very much. Thank you, Mr. Chairman.

Mr. JOHNSON. We want to thank you, Mr. Indritz, for coming here and giving us the benefit of your reading of Congressman Moss' statement into the record and your responses to the questions that have been asked. We thank you.

And at this point I would like to ask general leave to have all co-authors to have the right to submit a statement in the record.

Do I hear objection?

Hearing no objection, so ordered.

I might say that I have followed this and happen to be a coauthor on this particular piece of legislation. In the Central Valley project we have five preference customers, four cities and a cooperative. Our preference customers from the Central Valley System are very much disturbed with the amount of the increase. We do not say that there should not be some increase. We all accept that. But, the methods that were used resulted in a suggested rate being levied against us now, amounting to some 28 percent, when it should be more like 14 percent or thereabouts.

That is our contention. Now, there is an argument between the Bureau and myself at the present time as to how they arrived at the criteria they use in coming up with the rate that they asked for.

They have agreed with us after all of the hearings and all of the interest that has been shown that they would forgoe the second step possibly. That will have further review and consideration.

Whether they levy it or not I do not know. But, as pointed out in Congressman Moss' statement, there is a cloud there on all of the preference customers where they have not been assured that this second step will not be invoked upon them at the proper time.

As a coauthor, I had no part in drafting the legislation as such, but our subcommittee has the responsibility of going into this further and trying to work out acceptable language that will bring the consideration to our preference customers which they would like to have in the way of a piece of legislation.

How this bill will read when we are through with it is something else. One problem is in the 1939 Reclamation Act in section 9c requiring that there will be no deficit year. This is something that has never been followed in any of the reclamation projects heretofore. When the Bureau witness comes before us today, I want to ask specifically for information on this. I think that would bring rates down to a much more reasonable and acceptable rate if previous interpretation were followed in applying the 1939 Reclamation Project Act. They are now demanding that they have no annual deficits. This has caused us a lot of concern as it represents about half of the rate increase being invoked now upon the preference customers.

I would ask unanimous consent that I have a right to submit a statement for the record, too.

Is there any objection?

Hearing none, so ordered.

[The statement of Hon. Harold T. Johnson, with accompanying letters and the statement of Hon. James Abdnor, Member of Congress from the State of South Dakota in letter to Chairman Johnson, dated May 28, 1974, follow:]

STATEMENT OF HON. HAROLD T. (BIZZ) JOHNSON, A REPRESENTATIVE IN CONGRESS
FROM THE STATE OF CALIFORNIA

Mr. Chairman, and Members of the Subcommittee on Water and Power Resources, this statement is in support of the objectives of H.R. 14221 which I was privileged to co-sponsor with Congressman Moss and others, to provide for the review of increases promulgated by the Secretary of the Interior on November 1, 1973, in rates for electric power sold at five Bureau of Reclamation projects, and for other purposes.

At the outset, let me say that I am fully aware that Congress has given the Secretary of the Interior authority to market wholesale power from federal projects and has conveyed upon him wide latitude and discretion for the establishment of rates for such sales. I believe that it is appropriate that the Secretary have a considerable degree of latitude and discretion in such matters—and under no circumstances would I hold that Congress undertake to tell the Secretary, in detail, about such matters.

In the case of the power rates promulgated in November, 1973, however, I believe the Department of the Interior has exceeded the limits of the discretion Congress intends the Secretary to exercise. This being the case, it appears that the Congress has no alternative available to them except that we require, by statute, that certain minimum procedures and criteria be followed. I am not sure that the Subcommittee can bring out a bill which will assure that due process is being followed and that the intent of the Congress is not being ignored.

I have devoted a great deal of my personal time and that of my staff in trying to understand the basis for the Secretary's rate increases. I furnished a statement to the Regional Director of the Bureau of Reclamation at the so-called Field Hearings at Sacramento on July 10, 1973. I further testified before the Subcommittee on Conservation and Natural Resources, of the House Committee on Government Operations, on January 22, of this year.

I have written a number of letters to the Secretary of the Interior expressing my concern with the rate increases and with the manner in which it was promulgated.

Two of the more relevant letters are those of January 28, 1974, and March 22, 1974, which I attach to, and make a part of, this statement.

The Members will note that these letters deal primarily with the Department's assumption that no deficits may be incurred in any year of the payout period of the federal reclamation power system. This is the most crucial aspect of the Central Valley project rate studies and is the most fertile field, in my opinion, for legislative action.

In conclusion, of these remarks I would say that I hope that never again will we be confronted with a situation in which the Department chooses to forge ahead in the setting of rates without following due process and without regard to the intent of this Committee and its policy announcements. Indeed, we should amend and enact H.R. 14221 to assure that such will never happen again.

COMMITTEE ON INTERIOR AND INSULAR AFFAIRS,
U.S. HOUSE OF REPRESENTATIVES,
Washington, D.C., March 22, 1974.

HON. ROGERS C. B. MORTON,
Secretary of the Interior,
Washington, D.C.

DEAR MR. SECRETARY: By letter dated February 25, 1974, Assistant Secretary Horton informed me of the Department's intention to effectuate an increase of approximately 25 percent in the wholesale rates for commercial power from the Central Valley Project, California, on April 1, 1974. This action is being taken despite the concerns which have been expressed by several Members of Congress—and despite the showing by the House Committee on Government Operations that increases in this magnitude are of dubious justification.

Accompanying Secretary Horton's letter were two studies ostensibly establishing that the April 1, 1974, increase is necessary and that a further increase in the capacity charge of \$0.50 per kilowatt month will be necessary in 1977. Taken together these studies show that a surplus of almost \$600,000,000 will be produced by the end of the statutory repayment period. Also, they illustrate that the repayment objectives of 50 years for all reimbursable costs will be met well ahead of time—even without the second increment of increase.

It is clear, from my analysis of these studies, that they rely for their validity on your Department's recently self-imposed assumption that there can be no operating deficits during any year of system operation. I must insist that there is no requirement in law for such an assumption and Mr. Horton's reference to Section 5 of the Flood Control Act of 1944 is totally without relevance to this case as that legislation deals exclusively with the marketing of power from Army dams.

I once again invite your attention to the clear and unequivocal language of the report of this Committee accompanying the bill to authorize the Third Powerplant—wherein it is stated that the only criterion for power system financial management obligatory upon your Department is the retirement of each block of reimbursable investment within 50 years.

It is, therefore, inconceivable to me that your Department can, with logic, adopt a contrary policy as being mandated by the Reclamation Project Act of 1939. Secretaries and solicitors of both parties have been operating under the Reclamation Project Act for 35 years without noting a prohibition against "no deficit" years. Your Department would evidently have me believe that a long procession of your honorable and distinguished predecessors have either been aware of their responsibility or have consciously avoided it.

In conclusion, I am fully aware that existing law authorizes you to market power and to set the rates for which it will be sold. This being the case, your judgment in these matters is supreme insofar as the Congress is concerned—unless we become forced to the drastic act of altering the law.

In the meantime I can only appeal to your sense of logic, equity and fairness—which appeal I now renew.

Sincerely yours,

HAROLD T. (BIZZ) JOHNSON,
Chairman, Subcommittee on Water and Power Resources.

COMMITTEE ON INTERIOR AND INSULAR AFFAIRS,
U.S. HOUSE OF REPRESENTATIVES,
Washington, D.C., January 28, 1974.

HON. ROGERS C. B. MORTON,
Secretary of the Interior,
Washington, D.C.

DEAR MR. SECRETARY: This letter deals with your Department's intentions to increase the wholesale rates for hydroelectric power from five multiple-purpose projects of the Bureau of Reclamation, with particular emphasis on the Central Valley Project, California. This matter first came to my attention in January 1973 when an Interior Department press release announced that increases were necessary in the case of all five power systems.

On January 31, 1973, I sent a letter to then Assistant Secretary James R. Smith asking that a rate increase for the Central Valley Project not be promulgated until there had been an opportunity for all concerned to review and analyze the studies on which any such increase was to be based. That letter was acknowledged by then Acting Commissioner Stamm under date of February 22, 1973. Mr. Stamm forwarded certain inconclusive and tentative information and also committed the Department to provide a period of six months after availability of refined studies for review and discussion with customer groups.

On May 27, 1973, another Departmental press release was issued in which the results of "detailed computer studies . . . which demonstrate that rate adjustments are necessary" were announced. The rate adjustment for the Central Valley project was an effective 52 percent increase, approximately twice the amount estimated in the January press release. This release was followed in a short period of time by an informational brochure purporting to contain the justification for the then proposed increase in rates.

Within a few weeks following receipt of the brochures, and after a review of the materials by me and my staff, I arranged an informal meeting at which the preference customer groups, and your key staff, were afforded an opportunity to set forth their respective views concerning the validity of the increase proposed by the May 1973 release. As this meeting progressed it became increasingly evident to me that the criteria for the Central Valley Project rate study were excessively severe and, by comparison with the criteria for at least one of the other four systems, apparently designed to maximize the require-

ment for a rate increase. I might add that your representatives displayed a most cooperative and open-minded attitude at this meeting. They agreed readily to open the files of the Department, at all levels, to representatives of the preference customers and to consider carefully our suggestions concerning certain of the analytical criteria that were brought to their attention as being inappropriate. As a consequence of this meeting and other representations by the preference customers, your Department agreed to leave the record open until August 31, 1973, during which time additional comments would be received from interested persons.

The proposed rate increases next surfaced in a third press release in November 1973 which announced, with seeming finality, the promulgation of a two-step rate increase for the Central Valley Project. The first step to become effective on April 1, 1974, would be in the amount of about 28 percent. A subsequent increase for January 1977 was also announced; this to result in an overall increase approaching the 52 percent figure first proposed in May 1973. Despite Commissioner Stamm's commitment of February 22, 1973, we have not yet received the study which supports this latest announcement.

On January 22 and 23, 1974, the Subcommittee on Conservation and Natural Resources, of the House Committee on Government Operations, conducted Hearings into the matter of the announced increase in Central Valley Project wholesale power rates. I testified at this Hearing and attended the proceeding for the first day. I was represented for the entire Hearing by Committee staff. Testimony was taken from preference customer representatives, Departmental witnesses and counsel for Pacific Gas and Electric Company, the franchised public utility serving the Central Valley Project marketing area. During this Hearing, I first learned of the alleged changes that had been made in the rate studies between the May 1973 proposal and November 1973 formal promulgation. Let me here say that nothing which was brought out at these Hearings detracted from my impression that a rate increase was first determined administratively and that the Bureau of Reclamation has been working diligently ever since to find a set of criteria that would support such determination.

Specifically, we have previously noted several areas in the analysis, furnished to us subsequent to the May 1973 release, that are either incorrect or inappropriate for use in the studies. These points were presented orally to your staff at the above-cited informal meetings and were also set out in my testimony on January 22, 1974, to the Subcommittee on Conservation and Natural Resources. The extent that they have been considered and reflected in the latest rate study is, of course, unknown since that study has never been furnished to me. Incidentally, the validity of most, if not all, of my concerns has been endorsed by the General Accounting Office in its report to the Subcommittee on Conservation and Natural Resources.

The points at issue are, briefly, as follows:

1. ESTIMATES OF HYDROELECTRIC POWER PRODUCTION

The amount of power available for marketing is determined in major part by the water available for storage in project reservoirs. Projections in this area are customarily predicated on historic hydrologic records. Despite the availability of a longer and more favorable period of record, the May 1973 studies made use of a limited period. I have been informed, orally, that use of the more extensive hydrologic record in projections of future power production would increase saleable power by an amount ranging from 6 to 10 percent. This may or may not have been reflected in the studies supporting the November announcement.

2. NO DEFICIT-YEAR CONCEPT

The assumption concerning whether annual deficits in operation, maintenance and interest expense may be capitalized into the plant accounts for subsequent return with interest is a most crucial one. The study supporting the rate increase proposed in the May 1973 press release assumed that there could be no deficit in any year of the repayment period. In order to eliminate a projected deficit in fiscal year 1982 (when large interest payments would be required on new investment associated with not-yet-completed Auburn Unit, New Melones Project and Marysville Project) substantial immediate increase in annual revenues were indicated. Rate increases dictated by this assumption, when allowed to persist throughout the repayment period (50 years following FY 1981—the date all presently authorized investment is assumed to be completed) result in large surplus amounts that have no legitimate purpose in being.

The record and origin of this criterion is murky at best as it is clear that it has never, heretofore, been invoked in Power System Rate and Repayment Studies by the Bureau of Reclamation. Assistant Secretary Jack O. Horton testified, on January 22, 1974, that the procedure was required by Section 9(c) of the Reclamation Project Act of 1939—an interpretation of the law which has escaped the Department's Solicitors for almost 35 years. It is also an interpretation that is in direct conflict with the understanding of the subject presented to the House Committee on Interior and Insular Affairs by the Secretary of the Interior during testimony on legislation to authorize the Third Powerplant, Columbia Basin Project, Washington. Relying on Secretary Udall's explanation (which has never been rescinded or changed insofar as I am aware) the Committee on Interior and Insular Affairs took explicit note of the fact that repayment of each block of investment within the period required by law (50 years) was the sole criterion of compliance with the requirements of the law concerning repayment.

Despite Secretary Horton's reliance on this questionable interpretation of Section 9(c) of the Reclamation Project Act of 1939, your representatives subsequently testified that the study supporting the rate increase announced in November 1973 did, in fact, provide for capitalization of interest in at least two years of the repayment period. The extent to which this is accurate is unknown to me inasmuch as I have not yet been furnished this study.

3. REQUIREMENTS FOR SURPLUS FUNDS

The study supporting the May 1973 proposed increase envisioned a substantial surplus and sought to justify its necessity as a source of financial assistance to cover future irrigation investment beyond the capacity of the water users to repay. This concept has its roots in Reclamation law and tradition and it is not my purpose here to question it. I do question the realism, however, of imposing rate increases at this point in time to help repay any unit of the Central Valley Project not yet authorized. The entire revenue producing capability of the Central Valley Project after FY 2031 will be available for this purpose and it is inconceivable to me that any investment not yet authorized will, in fact, be developed in a time frame which requires financial assistance on or before 2031.

I illustrate this assertion by pointing out that your Administration has not recommended the authorization of any additional development whatsoever in the Central Valley—despite the most persistent urging of this Member and others in the California Delegation. Moreover, I can find no basis for optimism that this situation is about to change. In fact, every inquiry on this point is met with the explanation that all previously completed feasibility investigations must be converted to the Administration's new analytical system—which, so far as I can determine has not yet been installed at the working level of the Bureau of Reclamation. It is, therefore, clear that several years will likely elapse before we may reasonably expect recommendations, authorizing legislation, preconstruction planning and construction funding to eventually come out on any not yet authorized addition to the Central Valley Project—to say nothing of the large backlog and the Executive Branch reluctance to fund, at an adequate level, the work already in progress. Only the most sanguine would anticipate a major requirement for financial assistance before 2050 considering that irrigation is customarily allowed 50 years, plus a development period of not to exceed 10 years, within which to be repaid.

4. CAPITALIZATION OF MAJOR REPLACEMENTS

While not a major item, it is clear from testimony of your witnesses on January 22 and 23 that the Department's policy permitting capitalization of replacements in lieu of "expensing" them on an annual basis has not been followed. This failure to reflect your own internal policies, when accompanied by the subjective handling of the "no-deficit year assumption" and the "surplus" question, simply adds additional doubt to the legitimate need for major rate increases.

In this letter I have not addressed myself to the impact of existing contracts on revenue needs. Whether these relationships—with Pacific Gas and Electric Company on the one hand and the Centralia Washington people on the other—were prudent at the time of their execution and whether they are indeed be-

ing properly administered is a question for competent legal authority to resolve. It is not necessary for me to extrapolate the effect of speculative changes in these instruments to arrive at a judgment that your Department has not made its case for any level of rate increase, much less that set forth in your most recent press announcement.

In fact, it is my considered opinion that the rate increase announced for April 1, 1974, for the sale of wholesale power from the Central Valley Project should be indefinitely deferred and so I urge you to take such action.

Sincerely yours,

HAROLD T. (BIZZ) JOHNSON,
Chairman, Subcommittee on Water and Power Resources.

CONGRESS OF THE UNITED STATES,
HOUSE OF REPRESENTATIVES,
Washington, D.C., May 28, 1974.

HON. HAROLD T. JOHNSON,
Chairman, Subcommittee on Water and Power Resources, Committee on Interior and Insular Affairs, U.S. House of Representatives, Washington, D.C.

DEAR BIZZ: I want to commend you on your rapid action in holding hearings on H.R. 14221, which I have co-sponsored, to direct a review of the Bureau of Reclamation's recently promulgated power rate increases and penalty provisions. As you know, the Bureau's preference customers, as well as their Congressional representatives, have been something less than pleased with the Bureau's handling of these matters. It was in reference to my own personal disgust and in deference to the wisdom of the other co-sponsors in this regard, that I expressed my desire to co-sponsor H.R. 14221 and would now like to comment for the hearing record.

Any rate increase to the Bureau's preference customers in my Congressional District is disturbing to them because they are truly dedicated to providing service to their customers at the lowest possible cost. They know that such rate increases can only be passed on to their customers. This rate increase was particularly upsetting to them for a number of reasons, including the following:

1. They had been assured shortly before the increase was announced that payout in the Missouri River Basin was well ahead of schedule. This tended to negate the Bureau's later contention that the increase was required to meet inflation and unforeseen costs, and the Bureau has never properly resolved the apparent conflict.
2. The rate increase and so-called "five-times" and "60% load factor" penalties are not only contrary to the long established Bureau policy of encouraging the use of electric power, but they were effected in an arbitrary and capricious manner. These policy changes have, therefore, come to appear punitive in nature rather than necessitated by the need to maintain the financial integrity of the power projects.
3. The preference customers were not given adequate opportunity to become informed of the justifications for the rate changes much less to interact with the Bureau in determining if the justifications are in fact just.

Government officials in service to all the people of our great country are often placed in the position of having to make certain decisions in spite of the wishes of a few. It is when these officials pay no heed whatsoever to the wishes of a few, however, that they do a disservice to the entire country and the system under which we live. Truly few are those who will not accept a decision in the best interest of the country as a whole, but I believe that it is that very governmental unresponsiveness typified by the Bureau of Reclamation's actions on this matter which is at the root of the great sense of disillusionment being felt today.

I believe, therefore, that consideration of legislation such as H.R. 14221, which would direct the Federal Power Commission to review the Bureau of Reclamation's rate changes, is well justified. In reflecting upon this legislation since its introduction, however, I have come to the conclusion that it is not precisely what is needed—as a matter of fact, it seems to me that its passage could very well aggravate the primary problem of governmental unresponsiveness by involving another layer of bureaucracy in the process.

Although I cannot agree with Commissioner Stamm's contention before the Subcommittee on May 17 that the Bureau's customers were given adequate notice and opportunity to suggest alterations in proposed rate changes, I must concur

with his assertion that: "Rate making for Reclamation projects is not a mere technical exercise, but involves a number of policy determinations which go to the heart of the responsibility for planning and administering the repayment of water projects as well as the power operations. Under Reclamation law, power is a so-called paying partner for irrigation costs. The matter of the proper accounting and cost allocation among the various project purposes, the administration of required project repayment, and the planning for future project construction are matters basic to the water activities of the Reclamation program. They involve important policy judgments as well as technical expertise. The FPC has no experience in these important aspects of water project operations, planning, and administration. We believe that unnecessary confusion, inefficiency, and uncertainty would result if the Federal Power Commission were authorized to substitute its judgment for that of the Secretary (of the Department of the Interior) in matters as important to the future activities of these five Reclamation projects as are involved in these rate matters."

Taking into account the factors I have mentioned, I am drawn to the conclusion that enactment of H.R. 14221 would not be in the best interest of the electric power consumers of my Congressional District. I believe that a formal, institutionalized process by which the Bureau can receive and consider comments on proposed rate changes is needed, but I do not believe that involving the FPC would accomplish this end in an efficient and effective manner.

I stand by my co-sponsorship of H.R. 14221 as a means to call the Bureau to account for their handling of these matters, and I am gratified by your speedy action in this regard. It may be that alternative legislation is still required to formalize a rational rate making procedure for the Bureau, but I would hope that it would be accomplished by means other than those in H.R. 14221 as currently written. I understand that the Bureau is also considering formalizing procedures for rate making under their present administrative authorities. If this is so, perhaps the Bureau has come to see the error of its ways and our intentions in introducing H.R. 14221 can be achieved without legislation.

In any event, I am certain that the informed oversight of Congress will continue to be required. Your continued excellent leadership will be invaluable, and I look forward to the Subcommittee's recommendations.

With kindest personal regards, I am

Sincerely,

JAMES ABDNOR,
Member of Congress.

Mr. DELLENBACK. Mr. Chairman?

Mr. JOHNSON. Now, our next witness this morning will be Mr. Gilbert Stamm, Commission of the Bureau of Reclamation. He has a number of Bureau people with him. You may bring all of your people up here with you because there are probably going to be questions that might be asked that some of them can answer.

We are glad to have you here, Commissioner. And I am sorry we have gotten around to this at 11:30. We figured you would be on about 10:30 but we were about half an hour late in starting.

STATEMENT OF GILBERT G. STAMM, COMMISSIONER, BUREAU OF RECLAMATION, ACCOMPANIED BY WILLIAM GRAHAM, CHIEF, POWER DIVISION, WASHINGTON OFFICE; RICHARD PELZ, ASSISTANT SOLICITOR FOR POWER; AND ROBERT BARTA, REGIONAL SUPERVISOR OF POWER, MID-PACIFIC REGION, SACRAMENTO, CALIF.

Mr. STAMM. Mr. Chairman, I do have with me on my immediate left Mr. William Graham, who is chief of the power division in the Washington office. On my right is Mr. Richard Pelz, assistant solicitor for power, and second on my left is Mr. Robert Barta, regional supervisor of power, from the mid-Pacific region in Sacramento, Calif.

We are appearing today to present our views on H.R. 13867 and H.R. 14221, identical bills requiring the Secretary of the Interior to transmit the recently promulgated power rate increases on five reclamation projects to the Federal Power Commission for review and recommendation or approval. The Comptroller General is to assist in the review. In addition the Secretary would be required to publish proposed regulations providing for public hearings and written decision on the record concerning any future power rate increase, and public review on proposed contracts or amendments, for 45 days prior to execution, for the sale, exchange, or transmission of electric power at projects subject to section 9(c) of the Reclamation Project Act of 1939.

We oppose enactment of the proposed bill.

Section 9(c) of the Reclamation Project Act of 1939 authorizes the Secretary of the Interior to sell power and energy from any reclamation project—

—at such rates as in his judgment will produce power revenues at least sufficient to cover an appropriate share of the annual operation and maintenance costs, interest on an appropriate share of the construction investment at not less than 3 per centum per annum, and such other fixed charges as the Secretary deems proper. * * *

Authorizing acts subsequent to 1939, in some cases, have refined some of the guidelines under which the Secretary may determine power rates for specific projects. But basically, they have been patterned after the 1939 act. The availability of power revenues to aid irrigation has, in one form or another, been a part of general reclamation law almost since its beginning.

The general plan for electric power rate increases for the five projects was announced January 27, 1973. Rate adjustments were found to be necessary to cover increases in annual costs of operation and maintenance, increased interest costs, and increasing costs associated with power system reliability and environmental factors. Even the increasing costs of fuel experienced by utility thermal powerplants affects reclamation power rates, because we must purchase additional energy during years when water supply is below average.

The financial position of each project is determined by rate and repayment studies. These are long-term studies which include historical data and projected estimates of future annual revenues and repayment requirements. The long-range estimates are periodically adjusted on the basis of significant changes in historical data and economic trends associated with costs and revenues.

The detailed studies that are made to determine the required rates are complex. Each project provides several classes of service, each having its own rate. Furthermore, each power rate has two components, one for power—kilowatt—and one for energy—kilowatthour. It is necessary to weigh the potential revenue from each class of service and each component of the rates in relation to current and expected future costs on the projects. The use of power revenues to aid in irrigation development must also be considered.

After the January 1973 announcement regarding the proposed power rate increases, the necessary detailed studies were made. In May 1973 public hearings were announced. Brochures explaining the studies and indicating the required rates were mailed to interested

parties in June 1973. Hearings were held in July 1973, and were followed by numerous meetings and extensive correspondence with all interested parties. The criteria for project repayment were discussed, customer questions regarding the studies were answered, and the needs for the power rate increases were explained. Over 60 meetings were held with various groups.

The information obtained from the hearings and from the subsequent meetings and correspondence was given full consideration before the specific power rate increases were announced on November 1, 1973. Several adjustments in the proposed rates were made as a result of the review, including a delay from January 1, 1974, to April 1, 1974, for implementation, and a two-step increase for Central Valley project, with the second step delayed until January 1, 1977.

Two additional actions were taken after the November 1973 announcement. The application of the five-times penalty provision relating to unauthorized contract overruns was delayed for a year. We also advised this committee, in a letter dated February 25, 1974, that before implementing the second step of the Central Valley project rate increase in 1977, we would make a complete review of our procedures and policies. We stated the review would be carried out with full disclosure and consultation with interested parties.

The specific procedure, Mr. Chairman, to carry that out is being prepared now and will occupy approximately a 2-year period for implementation.

In our opinion, we have afforded the customers and other interested parties ample opportunity to review and comment on the proposed rates. We also believe we were responsive in making appropriate adjustments where they were justified.

As indicated previously, we oppose enactment of H.R. 13867 and H.R. 14221. Although our views are summarized in the Department's recent letter reporting on the bills, we wish to take this opportunity to comment in more detail.

In our opinion, certain of the declarations contained in section 1 are erroneous or leave an erroneous impression. For example, paragraph (a) on lines 6 and 7 of page 1, indicates that the rates promulgated in November 1973 were established by contract. This is not the case; rather, they were established by a separate action of the Secretary. Paragraph (d) leaves the erroneous impression that all of the proposed rate increases announced on May 28, 1973, were higher than those estimated in January 1973. This is not true, since in four out of the five cases the rates were essentially the same or lower.

Paragraph (e) erroneously implies that the 1-day hearings were the only opportunity afforded for public information and comment; actually, as discussed previously, there were numerous meetings and extensive correspondence with the interested parties subsequent to the 1-day hearings. We repeatedly announced our willingness to meet with any and all customers who requested meetings.

Paragraphs (g), (h), and (i) refer to the Comptroller General's report on the Central Valley project rate increase. Although his report was not issued until after the rate increases had been promulgated on November 1, 1973, the points covered by the Comptroller General had already been considered by the Secretary in establishing the rates. The report indicated that 4 of the 11 contentions by opponents of the

rate increase had merit. One of the four related to the updating of hydrology, for which an adjustment already had been made in the rate determination. Another contention related to the treatment of replacements, but the Comptroller General's report indicated this would have little effect on the rate increase. The other two contentions related to the so-called no-deficit-year policy and to financial surpluses at the end of the repayment period. These were of importance only in the case of the Central Valley project and had been considered by the Secretary. The impact of the no-deficit-year policy on the Central Valley project rates was deferred by the decision to adopt a two-step rate increase, with the effective date for the second step being deferred until January 1, 1977.

Sections 2 through 5 of these bills would empower the Federal Power Commission to conduct hearings on the record and to substitute its judgment for that of the Secretary as to the rate increases which have now gone into effect. We have a number of objections to these provisions. The role of the Federal Power Commission would not be limited to a review of the adequacy of the justification for the Secretary's action.

Instead, the Commission would be empowered to make an independent judgment as to what the rates should be and the Secretary would be required to comply with its conclusion.

Ratemaking for reclamation projects is not a mere technical exercise, but involves a number of policy determinations which go to the heart of the responsibility for planning and administering the repayment of water projects as well as the power operations. Under reclamation law, power is a so-called paying partner for irrigation costs. The matter of the proper accounting and cost allocation among the various project purposes, the administration of required project repayment, and the planning for future project construction are matters basic to the water activities of the reclamation program. They involve important policy judgments as well as technical expertise. The FPC has no experience in these important aspects of water project operations, planning, and administration. We believe that unnecessary confusion, inefficiency, and uncertainty would result if the Federal Power Commission were authorized to substitute its judgment for that of the Secretary in matters as important to the future activities of these five reclamation projects as are involved in these rate matters.

In addition to our substantive objections to sections 2 through 5 of the two bills, a number of provisions present problems on technical grounds. Lines 13 to 17 of section 2 on page 3 would require us to transmit to the FPC all pertinent documents, letters, memoranda, and other material. The described documents are voluminous. It would be difficult for the bureau to carry on its regular operations without the availability of these documents. The normal procedures would be for the FPC to review the basic documents supplied by the Secretary and to identify the copies of additional material they might require.

Section 4 contains the novel provision that if the FPC does not complete its review by July 1, the rate increases should be suspended. This could reward delay. The adverse financial effect upon reclamation projects would be significant.

Section 5 ignores the possibility that FPC might conclude that the rate increases were too low and would recommend that they be fur-

ther increased. This raises the question as to whether any retroactive application of such increase would be permitted. Moreover, the further question is presented as to whether the FPC should consider updated cost data in connection with review. The rate increases were based on actual or historical data through the end of fiscal year 1972. Costs have continued to rise since that time, and if the studies are made on the basis of fiscal year 1973 or fiscal year 1974 data, they could well lead to a higher figure than those promulgated.

Section 6 of the proposed bill would require the Secretary to publish regulations providing for public hearings and written decision on the record concerning future power rate increases and would also require public review of any contracts or amendments relating to the sale, exchange, or transmission of power. We object to the proposal that all power contracts be subject to mandatory public review. We have about 500 power sales contracts. As many as one-half may be modified in some manner in a given year. Most of these contracts and contract changes are of interest only to the parties involved. All of our contracts are available for anyone to see who cares to, but to try to establish procedures for public hearings on every contract and every amendment would impose an administrative burden that would be so large, costly, and time consuming as to be almost unworkable and would accomplish very little in the public interest.

Possible future power rate increases admittedly are of more general interest and importance. The rate increases promulgated on November 1, 1973, were the first such increases in many years. In view of current inflationary trends, it appears probable that future rate adjustments may become necessary more frequently. In our opinion formal evidentiary hearings are not an appropriate procedure for establishing the price at which Government power is sold, because the subject is complex and of necessity involves the exercise of broad judgment and discretion on the part of the Secretary. However, we agree there should be a procedure for interested parties to become informed and to comment on rate changes before they are established.

This can and will be done within our present administrative authority. As mentioned before, we are, in fact, now in the process of developing systematic procedures. We further agree that it might be appropriate to provide a procedure for an independent review of the rates before they are made effective.

The Department would not object to a requirement that reclamation rate changes be subject to confirmation and approval by the FPC, thus placing reclamation rates on the same basis vis-a-vis the FPC as the rates of the Bonneville Power Administration, the Southeastern Power Administration, the Southwestern Power Administration, and the Alaska Power Administration. Under those statutes, the Commission does not set Interior's rates but does have, in effect, a veto power over rates proposed by the Secretary. The FPC review affords the public an opportunity for further comment on the Secretary's proposals and affords the public and the Congress the benefit of further review and comment by an independent expert body. This system has worked well in the past and affords acceptable balance between the needs of the Secretary to conduct his responsibilities relating to the reclamation program and the needs of the public for protection against arbitrary or capricious rate decisions.

Thank you, Mr. Chairman.

Mr. JOHNSON. Thank you, Mr. Stamm, for a very well-stated position as far as the Bureau of Reclamation is concerned on the legislation that is pending today. Do any of your other people want to make any further comment at this time?

Mr. STAMM. No, sir. They are here to answer questions that may be put to us.

Mr. JOHNSON. Well, I might say, you have pretty well stated the Bureau's position on this bill. Concerning the no-deficit-year position that has been taken by the Secretary in arriving at the present rate increase, what is your knowledge of where that is being used at the present time, and has it ever been used on this type of project before?

Mr. STAMM. I think the first case, Mr. Chairman, where this became an issue was in connection with the Central Valley project.

And as indicated by the quotations from internal correspondence made by the previous witness, it is obvious that there was some difference of opinion within the Department. That is the reason primarily that the rate was divided into two parts. The no-deficit-year policy is being thoroughly reviewed. We will have it completed well in advance of the time that we need to decide whether or not, and to what extent, a second rate increase may be in order.

Mr. JOHNSON. Well, how are the other projects treated? I presume that you are familiar with the Bonneville project. Although it was authorized by the Public Works Committee, it was turned over to you people for jurisdiction over the power marketing.

What is the case there? Is that provision invoked at Bonneville at this time?

Mr. STAMM. The departmental policy that was announced recently in connection with these rate increases would be applicable, pursuant to that policy decision, to Bonneville Power.

However, I do not believe that application of it would have any significant effect upon the rates that would be required by the Bonneville Power Administration.

I would like to ask Mr. Pelz to supplement my remarks or to correct them if I am in error.

Mr. PELZ. Well, that is correct, Commissioner. There would be no effect because Bonneville, in its repayment studies, does not show any deficit.

Mr. JOHNSON. Well, but that provision is not applicable to the Bonneville project, am I right?

Mr. PELZ. Well—

Mr. JOHNSON. Whether it has any effect on it or not, it does have an effect upon the Central Valley System.

Mr. PELZ. Yes.

Mr. JOHNSON. You have made the decision that there shall be no deficit year and that is causing us a good portion of this rate increase that is asked for.

Now, I do not care whether it has any effect upon Bonneville or not. Are you using that criteria and policy in the Bonneville project?

Mr. STAMM. Mr. Chairman, if I might supplement my remarks—

Mr. JOHNSON. This was a decision that you people made and which was applied at the Secretary's level as a new criteria to use in the Central Valley project. Now, this is the first time you have invoked it, right?

Mr. STAMM. Let me speak from an administrative viewpoint for a minute, and Mr. Pelz is certainly at liberty to speak from the legal point of view.

My impression, from the administrative point of view, is that the no-deficit-year policy which was announced within the last year is permissible under existing law, and is probably not mandatory under existing law. Therefore, the initial announcement of the rate increase for the Central Valley project, and that is the one case where it is at issue, was under the administrative decision that the no-deficit policy ought to be followed.

The decision was not modified when the question was raised as to the appropriateness of that policy. However, at that time the rate was divided into two components; one to be implemented on April 1 and the other set aside for 3 years during which time the policy will be totally reviewed.

And, of course, any rate increase, justified under the decision following that policy review, would be affected subsequently.

We have set up procedures whereby we will get started very shortly on the actions that need to be taken to consider the 1977 rate increase. We hope to initiate those procedures at least 2 years in advance of the time that implementation would become appropriate.

Mr. JOHNSON. Well, what would the Department's position be if we were to mandate that in this legislation?

Mr. STAMM. I would certainly hope that the Department would follow the mandates of the Congress. At least that has been my policy for many years with the Federal Government.

Mr. JOHNSON. I am not so sure, because I think you are stretching the point when you bring that interpretation in and utilize it now in the Central Valley project. We probably overlooked spelling it out when we cleared Central Valley project some time back but if we were to provide in the legislation that that would not be the criteria to be followed, we would eliminate a good portion of the rate increase that is proposed.

Mr. STAMM. Yes, sir. That is true.

Mr. PELZ. Congressman, if I may add a word to what the Commissioner said, there is a great deal of confusion about this policy, and the confusion arises because of the fact that there are two different kinds of costs that our power rates have to repay.

One is the construction costs, the initial capital investment. The other is the annual operating cost. Now, our policy on the construction costs is they have to be, each increment of construction investment has to be repayed within 50 years with interest. Now, we make a repayment study that runs to the end of the repayment period, which is a 50-year period from the last authorized increment of investment. And when you look at that 50-year-plus period and you set your rates high enough so that you will repay all of these construction costs, and then it almost always follows that you are meeting then your annual operating costs in each year in which they occur because you do not make a payment on principal until you have paid off all of your annual costs in that 1 year.

Now, historically this has always been the result, that when we set the rates high enough to meet the repayment requirements for construction investment, the result is that in each year of the repayment study we have enough revenue to cover the annual operating costs in

that year. In other words, each year we are making some payment on principal. The amount varies from year to year, but each year we are making a little payment on principal, which means we cover all of our operating costs.

But, we ran across a phenomenon that we never had to face before in the Central Valley, namely, that we could show repayment of the construction investment within the repayment period but there was a period of 19 or 20 years in which we had deficits in meeting the annual operating costs during that year. We had to take a look at what the law was, and what the policy should be in that kind of a situation.

First, we had to ask ourselves why did that happen, what is different about the Central Valley project that is different from all of the other projects? And it appeared that there were two factors.

The first factor is that we have these tremendously high costs of power that we are purchasing from the Centralia Steam Plant in the State of Washington. Those purchased power costs are very high relative to all of our other costs. I think they are probably about twice as much. We do not have any other project where we have the high purchase power costs relative to the annual operating costs.

Second, we made an assumption in our repayment study that the purchased power costs were to end before the year 2000, before the end of the payout period. So, when you make that kind of a study, and assumption, then you can show that your construction investment is all paid in the future. And the Department looked at this and there were legal elements, and there were policy problems involved. And the policy feeling was that it is not good business to run a series of deficits for this long a period of time.

With respect to the legal questions, we were requested, the solicitor's office was requested, to write a formal opinion on the subject and that has been done. And I wonder, Congressman, if it might not be useful to have that opinion placed in the record.

Mr. JOHNSON. Yes. We will accept that for the record, unless there is objection.

[The opinion referred to follows:]

COVERAGE OF PROJECTED ANNUAL EXPENSES IN BUREAU OF RECLAMATION POWER RATEMAKING STUDIES

POWER: RATES

For the purpose of power ratemaking for Reclamation projects the rate and repayment study must show that the proposed rates will produce sufficient revenues in each year of the study (except for a possible initial short transition period) to cover operation and maintenance expenses during the year, including purchased power and wheeling but excluding depreciation and replacements, together with the required interest cost for the year except as interest may be deferred and capitalized in accordance with sound business principles. This is a minimum requirement, and it is independent of the requirement for repayment of the construction investment.

U.S. DEPARTMENT OF THE INTERIOR,
OFFICE OF THE SOLICITOR,
Washington, D.C., February 15, 1974.

Memorandum to: Assistant Secretary—Land and Water Resources.

From: Assistant Solicitor, Power.

Subject: Coverage of projected annual expenses in Bureau of Reclamation power ratemaking studies.

You have requested an explanation of the legal requirements which apply to the coverage of projected annual expenses in connection with the process of setting power rates by the Bureau of Reclamation. This question has arisen in connection with the rate revisions for the Central Valley Project. Studies showed that rates which would be at the level approximately sufficient to pay off each increment of construction investment within 50 years produced deficits in meeting annual expenses in 18 or 20 years of the study period. The principal cause for this is the high cost of purchased power for CVP relative to other operating expenses and relative to the construction investment, together with the assumption that these costs will cease well before the end of the payout period. The legal question is whether the applicable statutes allow rates to be set notwithstanding one or more years of such annual deficits or whether the rates must be set high enough to eliminate some or all of such deficits even though the result is that construction costs are paid off ahead of time and a substantial surplus is created.

The applicable law is contained in Section 9(c) of the Reclamation Project Act of 1939, 53 Stat. 1187, 1194, 43 U.S.C. 485h(c), I. F. Reel, & R.L.A. 647 (1972). It provides in relevant portion as follows:

"Any sale of electric power . . . shall be . . . at such rates as in his [the Secretary's] judgment will produce power revenues at least sufficient to cover an appropriate share of the annual operation and maintenance cost, interest on an appropriate share of the construction investment at not less than 3 per centum per annum, and such other fixed charges as the Secretary deems proper."

It is readily apparent that the statute refers to three separate components of cost—"operation and maintenance cost", "interest", and "fixed charges". The particular subject of the present inquiry is the first two.

A review of the legislative history demonstrates that the words "an appropriate share of" refer to the cost allocation process and are intended to designate the costs or investment allocated by the Bureau of Reclamation to the power purpose of the project rather than to the purposes of irrigation, navigation, flood control, etc.¹

Incorporating this change into the words of the act, your question involves an interpretation of the statutory requirement upon the Secretary that—

the power rates shall be such "as in his judgment will produce power revenues at least sufficient to cover the annual operation and maintenance cost" allocated to power and "interest on the construction investment" allocated to power "at not less than 3 per centum per annum."

Upon reviewing the meaning of words of the statute by themselves and in relation to the Reclamation laws and other power ratemaking statutes, we conclude that for the purpose of power ratemaking the rate and repayment study must show that the proposed rates will produce sufficient revenues in each year of the study (except for a possible initial short transition period) to cover operation and maintenance expenses during the year, including purchased power and wheeling but excluding depreciation and replacements, together with the required interest cost for the year except as interest may be deferred and capitalized in accordance with sound business principles. This is a minimum requirement, and it is independent of the requirement for repayment of the construction investment.

THE PLAIN MEANING OF THE STATUTORY WORDS

Two elemental rules of statutory construction are that the words of the statute will be given their plain meaning and that each word or phrase will be given effect. 50 Am. Jur., Statutes §§ 225, 231. Application of these rules to the words and phrases here yields a very straightforward result, as shown by the analysis that follows.

The first phrase is "as in his judgment will produce" certain power revenues. The inclusion of the reference to the Secretary's "judgment" is significant. It means that the Congress did not require that the rates must in fact produce a certain amount of revenues but only that in the Secretary's judgment they will produce these revenues. Thus the law looks not to yesterday or today, but to tomorrow.

This is a significant difference. Ratemaking is a process that involves predict-

¹ See "Reclamation Project Act of 1939: Hearings before the Committee on Irrigation and Reclamation of the House of Representatives on H.R. 6773 and H.R. 6984", 76th Cong., 1st Sess., 26-7, 34, 140 (1939); 84 Cong. Rec. 10220 (1939); H.R. Rept. No. 1252, 76th Cong., 1st Sess. 2 (1939).

ing the future. In the rate and repayment study various judgments have to be made as to the likelihood and magnitude of future events, such as the amounts of sales, operating and construction costs, and project pumping load, the in-service dates of new powerplants, the outcome of contract negotiations, and so forth.

Also, in the case of hydroelectric projects, judgments must be made as to the expected runoff into the reservoirs, based on normal weather conditions and anticipated diversions, to support estimates of the amount of generation. These judgments must be informed and rational, based upon adequate studies and the opinions of qualified experts.² But if events develop differently than had been anticipated—for example, if costs escalate more rapidly than normal or an extended drought occurs—and as a result of these abnormal circumstances a deficit in fact occurs, there is no violation of the law. However, it is incumbent upon the Secretary to regain a non-deficit position within a reasonable transition period.

The next key phrase is "at least sufficient". It means that the stated test is a minimum, not a maximum. The power revenues, actual or predicted, may lawfully exceed the listed requirements.

For revenues "to cover" costs means that they must equal or exceed them and thereby reimburse the Treasury for these expenses. For revenues "to cover the annual" cost additionally indicates that the revenues must equal or exceed these costs in the same year in which incurred. Operation and maintenance costs are by their nature recurring costs, and the inclusion of the modifier "annual" is not unnecessary to define them.³

Finally, the term "operation and maintenance cost" would be given its customary meaning under standard accounting practice and business usage.⁴ Thus, it would include such expenses as payroll costs for plant operators and maintenance personnel, administrative expenses, supplies, repairs, utilities, purchased power, and wheeling. It would not, however, include depreciation, which for repayment purposes would fall into the category of a "fixed charge" relating to capital investment and be subject to Secretarial discretion.⁵ The same would be true of expenditures for replacements.⁶

In summary, the plain meaning of the words is that the rates must be high enough so that, in the Secretary's judgment, when applied to anticipated generation and sales, they will produce revenues at least sufficient each year to equal the operation and maintenance cost that year, but this does not include depreciation or replacements.

As to the second component of cost, the Secretary is also required to set rates which in his judgment will produce revenues at least sufficient to cover interest on the power construction investment at not less than 3 percent per year. It is worthy of note that the modifier "annual" does not appear before the word "interest", thus suggesting that, contrary to the operation and maintenance cost, the annual interest cost need not be covered each year. On the other hand, the broad discretionary phrasing relating to "other fixed charges" does not extend to interest, thus suggesting a limit on the degree to which recovery of annual interest charges could be postponed. This subject is further discussed below in relation to the 1944 Flood Control Act.

² The word "conclusive" was included before "judgment" throughout the bill drafted by the Department of the Interior and introduced on June 19, 1939, by Rep. White as H.R. 6773 and on June 12 by Sen. O'Mahoney as S. 2591. It was deleted by the House committee in executive session on June 24 and was omitted when White introduced the amended bill, H.R. 6984, on June 26. Hearings, *supra*, at 149.

³ The only other possible reason for including "annual" might be to distinguish O&M costs that do not occur annually (such as those due to unusual flood damage) from those that do; but this is not sensible because it suggests that, since they also are not "fixed charges", they are not reimbursable at all, a result not in keeping with the congressional intent; and because a rate and repayment study never anticipates an extraordinary loss or expense in any specific year.

⁴ The Bureau keeps books in accordance with the F.P.C. uniform system of accounts in accordance with section 303 of the Federal Power Act, 16 U.S.C. 825b, which requires it to do this "so far as may be practicable." Thus, this classification system would govern except where inconsistent with other provisions of Reclamation law or practice.

⁵ The depreciation of a capital item in standard cost accounting serves a function similar to the repayment of capital investment under the repayment requirements of law. The FPC "operation and maintenance expense accounts" include the items listed in the preceding sentence but do not include the "depreciation expense" account or the various categories of interest expense.

⁶ It could be argued that replacements are a maintenance expense attributable to ordinary wear and tear, particularly in view of the facts that the Bureau of Reclamation traditionally budgets replacements as an operation and maintenance expense and includes the cost of replacements in operation and maintenance charges for water users. However, inasmuch as they obviously are capital items and are accounted for as such in the FPC accounts, it cannot be said that section 9(c) definitely includes replacements within the term "annual maintenance cost" for purposes of determining the minimum rate requirements.

THE CONTEXT OF THE RECLAMATION LAWS

The Reclamation Project Act of 1939 is one of the major enactments of general application that comprise the Reclamation laws. Its primary impetus was the report⁷ of the Reclamation Commission established pursuant to the Act of August 21, 1937, 50 Stat. 737. This report contained numerous recommendations to relieve irrigators from hardship in paying construction charges and to improve other aspects of project management. The bill, which was drafted by the Department of the Interior, also sought to set forth the principles that would apply to the formulation, cost allocation, and cost reimbursement of new Reclamation projects generally, in recognition of the fact that they served multiple purposes and no longer were largely single-purpose undertakings. Unfortunately, no specific reference to the point under discussion has been found in the legislative history. However, the context of the Reclamation laws in which the provision dealing with power O&M costs throws some light on its meaning.

When the Reclamation program originated in 1902, it was contemplated that the irrigators would pay all of the operation and maintenance costs and would repay the entire construction investment without interest within 10 years.⁸ The repayment period for construction costs subsequently was extended to 20 years,⁹ then to 40 years,¹⁰ and, in the 1939 Act, an additional development period of up to 10 years was allowed.¹¹ When it was realized that Reclamation dams offered opportunities for power development and that the power could be sold at a profit, that is, that power revenues would be more than sufficient to cover power operation and maintenance costs and repay the power construction investment, Congress determined that net power revenues should be used to assist the water users in meeting their financial obligations.¹² At the same time it was made clear that the power purpose was subordinate to the irrigation purpose.¹³ Thus power became irrigation's servant, not its equal or its master.

The distinction between operation and maintenance cost and the construction investment, and the difference between operation and maintenance charges to cover the former and construction charges to repay the latter, are a cornerstone of Reclamation law and practice.¹⁴ Although Congress has enacted numerous laws to relieve the irrigators of their obligations to pay construction charges, it has ameliorated the obligation to pay operation and maintenance charges only in a relatively few instances. In fact, the insistence of Congress that the farmers pay operation and maintenance charges is so strong that these charges must be paid in advance, interest penalties of at least one-half percent a month are imposed for delinquent payments, and the delivery of water will be cut off if the payment is in arrears more than 12 months.¹⁵

In view of the firm congressional policies that irrigators are required to pay operation and maintenance charges in advance, with severe penalties for the failure to do so, and that power is subsidiary to water under Reclamation law, it would be surprising indeed if Congress intended in the 1939 Act to permit power users to postpone payment of power operation and maintenance costs beyond the year in which incurred.

OTHER POWER MARKETING STATUTES

In a 1955 opinion the Attorney General ruled that the statutes under which the Interior Department markets power from Federal dams are in *pari materia*, that is, that they generally are taken from the same body of law and are to be construed together.¹⁶ The principal statutes referred to are the Reclamation

⁷ H.R. Doc. No. 673, 75th Cong., 3rd Sess. (1938).

⁸ Reclamation Act, sections 4 and 6, 32 Stat. 389, 1 F. Recl. & R.L.A. 51, 69; *Swigart v. Baker*, 229 U.S. 187 (1913).

⁹ Reclamation Extension Act, section 2, 38 Stat. 687, 1 F. Recl. & R.L.A. 187.

¹⁰ Omnibus Adjustment Act, section 46, 44 Stat. 649, 1 F. Recl. & R.L.A. 377.

¹¹ Subsection 9(d), 76 Stat. 407, 1 F. Recl. & R.L.A. 652.

¹² Sec. 5, Act of April 16, 1906, 34 Stat. 117, 43 U.S.C. 522, 1 F. Recl. & R.L.A. 111; subsection I, *Fact Finders' Act*, 43 Stat. 703, 43 U.S.C. 501, 1 F. Recl. & R.L.A. 321.

¹³ Sec. 5 of the 1906 Act, note 12 *supra*; the last sentence of subsection 9(c) of the 1939 Act.

¹⁴ See, e.g., sec. 5, Reclamation Extension Act, 38 Stat. 687, 43 U.S.C. 492, 1 F. Recl. & R.L.A. 191, and the statutes cited in notes 8-11 *supra* and note 15 *infra*. The term "fixed charges" in section 9(c) manifestly refers to construction charges.

¹⁵ Subsect. N, *Fact Finders' Act*, 43 Stat. 704, 43 U.S.C. 493, 1 F. Recl. & R.L.A. 325; sec. 6, Reclamation Extension Act, as modified by subsec. H, *Fact Finders' Act*, 43 U.S.C. 494, 495; sec. 6, Reclamation Project Act of 1939, 43 U.S.C. 485e, 1 F. Recl. & R.L.A. 639; see also the current appropriation act language, II F. Recl. & R.L.A. 1024.

¹⁶ 41 Op. Atty. Gen. 236, 245 (1955).

Project Act of 1939 here under examination, section 5 of the Flood Control Act of 1944,¹⁷ and the Bonneville Project Act.¹⁸ In the 1955 opinion, which involved the disposition of power from an Army Corps of Engineers dam on the Savannah River in Georgia, the Attorney General in effect read into the 1944 Flood Control Act a provision from the Bonneville Project Act relating to preference customers.¹⁹

Section 5 of the 1944 Flood Control Act provides that the Secretary of the Interior shall dispose of power from projects of the Department of the Army not required for project operation. It provides in relevant part:

"[The Secretary of the Interior] shall transmit and dispose of such power and energy in such manner as to encourage the most widespread use thereof at the lowest possible rates to consumers consistent with sound business principles. . . . Rate schedules shall be drawn having regard to the recovery (upon the basis of the application of such rate schedules to the capacity of the electric facilities of the projects) of the cost of producing and transmitting such electric energy, including the amortization of the capital investment allocated to power over a reasonable period of years.

The first sentence quoted above is similar to language in section 6 of the Bonneville Project Act, and the second sentence is taken essentially verbatim from section 7.²⁰

The provisions of section 5 are comparable in many respects to those of section 9(c) of the Reclamation Project Act that were discussed earlier. Thus, the phrase "shall be drawn having regard to" is comparable to "in his judgment will produce" in section 9(c), that is, the rate studies must show compliance but the actual results may vary because of the occurrence of events which could not reasonably be anticipated. The Congressional debate shows that the phrase in parentheses was included to show that the principal need not be paid in predetermined annual payments as in conventional mortgages but that the amount of payment would vary from year to year with changes in water and market conditions.²¹ The "cost of producing and transmitting" the power comprehends both operation and maintenance costs and construction costs. The term "allocated to power" is equivalent to "appropriate share". The reference to "the amortization of capital investment over a reasonable period of years" serves the same purpose as "such other fixed charges as the Secretary deems proper." The phrase "amortization of capital investment" has been administratively interpreted, by both the Secretary and the FPC, on the basis of the legislative history, to include interest. The term "amortization" is akin to "depreciation" and buttresses the conclusion that the latter is not to be considered an operation and maintenance expense for purposes of ascertaining compliance with the ratemaking standards.

The fact that the amortization of only the capital investment is referred to suggests that operation and maintenance costs are not to be amortized, that is, that they are to be reimbursed as incurred and not deferred for later repayment.

The first sentence also must be considered. The key phrase is "the lowest possible rates to consumers consistent with sound business principles". This provision may illuminate the other requirements of law, but it does not supersede them. The word "possible" includes the meaning "legally possible"; the term "sound business principles" incorporates the other statutory requirements. Thus, for example, it is neither "possible" nor a "sound business principle" not to "cover the annual operation and maintenance cost", not to include interest on the power investment at Reclamation projects at a rate of at least 3 percent per annum, and not to amortize the power investment within a reasonable period of years. On the other hand, where the other statutory terms allow a discretionary range of action, the precept for "the lowest possible rates consistent with sound business principles" may be referenced for further guidance in the exercise of that discretion. For example, the absence of the modifier "annual" before "interest" in section 9(c) may be interpreted to allow the deferment of the annual interest charge where a good reason exists that is in

¹⁷ 58 Stat. 890, 16 U.S.C. 825s, II F. Recl. & R.L.A. 801.

¹⁸ 50 Stat. 731, 16 U.S.C. 832 et seq., I F. Recl. & R.L.A. 568.

¹⁹ The reference to other statutes is an aid in interpretation, but it cannot be used to amend the statute. For example, the interest rates on Reclamation projects cannot be less than the 3 percent specified in 9(c), and conversely, the interest rate on Army projects may be lower under the Flood Control Act.

²⁰ 50 Stat. 735, 16 U.S.C. 832e, f, I F. Recl. & R.L.A. 574, 575.

²¹ 81 Cong. Rec. 8524 (1937).

accordance with sound business principles, including accepted utility accounting practice.²²

STATEMENTS OF REPAYMENT POLICY

It has been suggested that the conclusion herein reached regarding coverage of annual operational costs is inconsistent with two statements of repayment policy, but an analysis of these statements shows this not to be the case. The first of these is found in H.R. Rept. No. 1409, 89th Cong., 2d Sess. 9-10 (1966), in connection with the third powerhouse at Grand Coulee Dam, where the House Interior Committee explained the Department's repayment study as follows:

"The repayment study is based upon year-by-year forecasts of system revenues and costs over the repayment period. Revenues are applied first to pay the costs of operation, maintenance, replacements, and interest. All remaining revenues are applied to repay the capital investment in commercial power facilities, and irrigation assistance as it falls due. Accordingly, there is no annual schedule of capital repayment. The test of the sufficiency of revenues is whether the capital investment can be repaid within the overall repayment period established for each power project, each increment of investment in the transmission system, and each block of irrigation assistance. Hence, repayment may proceed at a faster or slower pace from year to year as conditions change. Annual operating costs and revenues, of course, may vary from year to year since they are affected by weather conditions, streamflows, current economic conditions, changing markets, and the absorption of new projects into the system.

"This approach to repayment scheduling has the effect of averaging the year-to-year variations in costs and revenues over the repayment period. This results in a uniform cost per unit of power sold, and permits the maintenance of stable rates for extended periods. It also facilitates the orderly marketing of power and permits Bonneville Power Administration's customers, which include both electric utilities and electroprocess industries, to plan for the future with assurance."

This discussion focuses on the repayment of capital investment after operational costs are paid. This premise is stated succinctly in the first two sentences: In a year-by-year forecast of system revenues and costs, the revenues are applied first to pay the costs of operation, maintenance, replacements, and interest. There is no suggestion that the annual revenues would not be at least sufficient to cover the annual operation and maintenance cost.

The second policy statement to which attention has been called is the following paragraph from Part 583 of the Reclamation Instructions:

10. *Net revenues.*—The difference between total operating revenues, and the total revenue deductions is the amount of net revenues. This revenue is applied toward repayment of project investment costs, payable from power system revenues. In early years of project power system operations, the estimated net revenue may result in an annual deficit. Such deficits increase the interest-bearing repayable obligation.

The penultimate sentence suggests the possibility that in the early years of project power system operations the estimated "net revenue" may result in an annual deficit. However, the instructions explain that net revenues are arrived at only after interest and provision for replacement are deducted from estimated gross revenues. As indicated earlier, replacements are not included within "the annual operation and maintenance cost" which section 9(c) requires to be met, and interest may be capitalized in accordance with sound business principles. With the elimination of these items from the calculation, it is highly unlikely that any deficit would be experienced.

RICHARD K. PELZ.

Mr. PELZ. I brought a copy of it along.

Mr. JOHNSON. Please make it available to us. In your own testimony or in your recommendations that have come to light today, you project this accumulation of this in a fund. Now give us a little enlightenment on that, such as the amount of surplus that is accumulated based upon using this fund?

²² For example, the Bureau for convenience begins charging interest on the total joint costs allocated to power when the powerplant first becomes revenue producing. However, for purposes of ascertaining the minimum legal requirement, it would be permissible to capitalize a portion of this interest attributable to additional generating units until they become operational if this is shown to be in accordance with accepted utility accounting practice.

Mr. STAMM. Before he does that, could I clear up one possible misinterpretation on Mr. Pelz' earlier words. Somebody might get the impression that we pay off in our bookkeeping procedures capital costs, principal, before we pay off O. & M. Revenues are applied first to meet the annual obligations for operation, maintenance, and replacement, and then comes interest and principal.

The question relates to the extent to which interest and principal might be deferred in a current year, to be picked up at a later time.

Mr. JOHNSON. We recognize that the operation, maintenance, and replacement costs are higher over this period of inflation probably than ever was anticipated.

Now, you mentioned two things; the deficit years that we are going to face in your study, and the high cost of the Centralia power. But, the high cost of Centralia power as related to the Central Valley project, you could have reconsidered that a year or so back. I think it was 1971, was it not, when it was up for review as to the cost of it?

Mr. STAMM. That is true.

Mr. JOHNSON. Would you explain that?

Mr. STAMM. It is up for review every 5 years, 1971, 1976, and 1981. The increase in the cost, the significant increase in cost for Centralia power has come about since the time that it would have been appropriate to reopen or modify the rate in 1971.

Mr. JOHNSON. Well, would you explain to me and for the record—

Mr. STAMM. I am sorry. I think maybe I gave you some wrong information. I am going to ask maybe Mr. Barta, who is from that area, and is intimately familiar with the Centralia contract, to answer your question.

Mr. JOHNSON. These were the two big causes of your project running in the hole; one, the cost of Centralia power, and the deficit years that you were facing in your projection. Now, we were also told that there would be a sizable surplus, and I think that was mentioned in Congressman Moss' statement.

Mr. STAMM. Yes, sir.

Mr. JOHNSON. I did not know anything about the position of the Solicitor, but it seemingly recognized that there would be a considerable surplus there. Now, could you tell me just what is our arrangement as far as Centralia power is concerned?

Give us, for the record now, as you are the person in charge out there, and you negotiated the Centralia contract as far as the Bureau was concerned—

Mr. BARTA. No, sir. I did not negotiate the contract.

Yes, sir; I am in charge of at least the administration of that contract directly.

The first power under that contract, I believe, was delivered to the Bureau in January of 1972, and it will continue until December of 1981. It is a 10-year contract. It did not start to accumulate costs under that contract until I think in January—no, July of 1972 or 1971 when we were buying our first initial investments in the coal pile, and we had no cost records on which to base any negotiations, if you want to call them that, prior to April 1 of 1971.

Am I addressing myself to your question?

Mr. JOHNSON. Yes. We would like to learn as much as we can about it. The way it looks to me, is that there are increased costs involved. The Central Valley people were told, when the Bureau was looking

for a source of power in the Northwest, that Centralia would be fairly economical power. This power was supposed to be made available as a low-cost power supply for the Central Valley System but then it became a very costly power source. It was subject to review, I think, in 1971.

Mr. STAMM. Mr. Chairman, you and I both referred to the Centralia contract. The 1976 date refers to our contract with the P.G. & E. and it is the rates in that contract relating to Centralia power that have been in contention. The rates in that contract come up again for review or modification in 1976.

Mr. JOHNSON. Well, I presume that most of that power was used by P.G. & E., not by the Central Valley customers.

Mr. STAMM. I think it was about 50-50 as I recall.

Mr. BARTA. I think that is correct.

Mr. STAMM. About half goes to the preference customers and about half goes to P.G. & E. It might not be precisely 50-50, but it is in that range.

Mr. JOHNSON. Can you tell me just how that contract operates, and what are the additional costs to the Bureau?

Mr. STAMM. Well, under that contract, we are obligated to pay the costs attributable to our interest in the powerplant. As those costs of operations go up, and the operation includes a tremendous cost for adding facilities and equipment to make the plant acceptable environmentally, we are obligated to pay those costs. Under those arrangements for Centralia power, the cost has gone up to approximately 9 mills per kilowatthour. And under the contract with P.G. & E., the power to them is available from Centralia at substantially less, about half that.

This is not, of course, the only provision of the P.G. & E. contract involved.

Mr. JOHNSON. Is that the reason that Centralia is costly to the Central Valley project?

Mr. STAMM. Yes, sir. That is the principal reason.

Mr. JOHNSON. Because we pay approximately 9 mills for the power and P.G. & E. pays the Government about $4\frac{1}{2}$ mills for the power. Is that not right?

Mr. GRAHAM. That is essentially right. Now, but we are putting it in a bank account, and we have to consider when we take it out.

Mr. JOHNSON. Well, what I am trying to get at is: Are these costs what affected the rates in the Central Valley?

Mr. GRAHAM. The costs from Centralia, yes, and the costs are based on a 400—we get 427 megawatts out of Centralia. Our costs are 427 over the total output, and we will get a ratio of cost.

Mr. JOHNSON. What amount of increased costs? What does it amount to in dollars?

Mr. GRAHAM. The increase?

Mr. BARTA. Between the original estimates, you mean and what we are paying?

Mr. GRAHAM. We originally estimated about 3 mills, and now we are paying about 9.

Mr. JOHNSON. Well, I mean in dollars.

Mr. BARTA. I do not think we have that.

Mr. JOHNSON. You say there are two things that would justify this rate increase. One was the increased cost of Centralia to the Central Valley project and the other was your deficit years that you found in your projection. Now, the hydrologic study which you have modified did not amount to very much. But there are one or two other matters of concern.

But, these are the two key matters of concern, and they justified your rate increase, as I understand it.

Mr. STAMM. I think that is right.

Mr. JOHNSON. I am trying to find out in dollars and cents what does this mean to us, what is the dollars and cents?

Mr. BARTA. I do not have those numbers in front of me, sir.

I think they can be supplied. The total estimated costs, as I recall from correspondence I have seen in this regard, it was about—the initial costs were somewhere in the neighborhood of about \$13 or \$14 million.

Mr. STAMM. One other point I think that we did not leave clearly understood, although the Centralia power is costing us about 9 mills today, it is my understanding that the preference customers are not paying 9 mills for the portion of Centralia power that goes to them.

The 50 percent of the Centralia power that goes to the preference customers is being marketed to them at the 3-mill rate. It is this current difference between our costs for Centralia power and what that power is marketed for that has caused our purchased power account to go up substantially.

Mr. JOHNSON. Our preference customers are being asked to write this deficit off at the present time. They are being asked for an immediate 28-percent rate increase and a possibility of a 52-percent rate increase overall. They are paying for it. The preference customer is faced with as of now 28 percent, and if the second bit goes into effect, it is about 52 percent.

Mr. STAMM. What you are saying is we are making the adjustment with the preference customer now and we would make a similar adjustment with P.G. & E. until 1976 and that the time differential is discriminatory.

Mr. JOHNSON. In the meantime, we have lost a lot of money and you have accumulated this huge deficit.

Mr. STAMM. Well, yes. This is very complicated, Mr. Chairman.

Mr. JOHNSON. I realize that.

Mr. STAMM. The power that is going to P.G. & E. goes primarily in the bank account Mr. Graham mentioned and comes out of that bank account at the rate it goes in, plus certain increased costs in operation and maintenance during that time of the surplus, and a service charge. The lower the rate that prevails when it goes into the bank, the lower the rate will be when it comes out, so the differential partially washes out with time. But, for the interim period, it has created a sizable impact upon our annual cost.

Mr. JOHNSON. I admit that it is very complex, this whole thing. But our people are being asked to pay an increase of 28 percent now with the possibility of another increase to bring it up to about 52 percent. There are only two things that cause that rate increase, as I understand it, to any great degree.

Mr. STAMM. Our studies, just to correct the record on this point, indicate the first step increase would be 23 percent rather than 28. Whether or not the second step is implemented will depend upon the studies that will be undertaken this year.

Mr. JOHNSON. Well, you are down to 23 percent from 28 as first announced?

Mr. STAMM. Well, there was some confusion, and I think that is right. I think there were some different figures tossed around in the early stages between the initial general announcement and the finally announced two-step increase. But, our figures show that the first step of the two-step rate announcement is 23 percent above prevailing rates.

Mr. JOHNSON. Well, our people are quite concerned with being asked for that huge increase. As you have stated there has not been a previous increase. You have been operating along with very good relations between the Bureau of Reclamation and its preference customers. Now we are confronted with a large increase. There are only two causes that I can see, that produce this large increase. They are the cost of Centralia power, and the way it is handled, and the no-deficit year policy that you people have adopted.

Mr. STAMM. At the time the Centralia contract was negotiated, in fairness to those who negotiated it, it had some other advantages.

It permitted us to increase our marketing capacity from the figure of about 850 megawatts or rather 450 megawatts up to 1,050 megawatts.

Mr. JOHNSON. We went all through that.

Mr. STAMM. And we anticipated—

Mr. JOHNSON. And we got a half a loaf. The preference customers got a half a loaf. We went all through that, and we accepted it, and it was agreed to and that was it. But, we were not told that we were going to have to pay for it with these large increases.

Mr. STAMM. And we were unaware of that. If our foresight were as good as our hindsight, we might have done differently. But, as you know, the inflationary costs have just been tremendous. The costs attributable to the environmental equipment alone have had a tremendous effect upon costs, and because of the environmental influence it took much longer to get the plant into reasonably full production than was anticipated.

Mr. JOHNSON. We realize that the Environmental Protection Act requirements have raised the costs of most things. But, the only thing that I am trying to do here is to protect those preference customers and make sure we are not paying any more than what we should pay.

Mr. STAMM. Well, I can assure you, Mr. Chairman, that the sympathies of Reclamation are similar. There were many superlative adjectives used in your colleague's comments, Congressman Moss. I, personally, have probably negotiated or participated in negotiation of as many contracts as any other person in Reclamation, both water and power, over a good many years. And the implication there, I think, does not reflect the generally prevailing position, attitude, or approach of the Bureau of Reclamation, and we will stand on the record in that regard.

Mr. JOHNSON. It has been my experience to have been closely involved with the Central Valley's water and power squabbles, too, and I always figure that when we get through with the negotiation and agreement

that we have to live with it. I am satisfied with the agreements that were made as far as the people I was involved with. Here, again, I think that there has been a decision made, which is contrary to the best interest of the preference customers, I might say. And I think maybe we can correct it with legislation now. Whether we can ever get it signed or passed, that is something else.

But, I think in this subcommittee we are going to probably try.

Mr. STAMM. I am hopeful to the extent that is true that we can correct it administratively without legislation between now and 1977. However, it would clear it up once and for all if this were made a matter of legislation.

Mr. JOHNSON. The gentleman from Georgia, Mr. Stephens.

Mr. STEPHENS. Mr. Chairman, I have not got but one question that I would like to ask. I would like to express my appreciation for the testimony I have heard from these gentlemen.

But, the entire operational costs and the repayment of construction costs, are paid out of the projects themselves? There is no Federal direct funds involved in the operation of the projects?

Mr. STAMM. That is right, Mr. Stephens. By law the portion of the power costs attributable to commercial power are repaid in full with interest. The portion of irrigation costs that may be assigned to power for repayment are repaid interest free.

But, nevertheless, the capital costs of irrigation are repaid fully out of the power revenues to the extent that irrigation costs may be assigned to power.

Mr. STEPHENS. There are no appropriated funds in the operation?

Mr. STAMM. Well, yes. We operate with appropriated funds.

Mr. STEPHENS. For the construction initially, yes. But do you have appropriated funds for the operation of it now?

Mr. STAMM. Yes, because the revenues each year go into the U.S. Treasury, the general fund, and then funds are appropriated out of that fund each year for the operation.

Mr. STEPHENS. Are they equal? Are they equal?

Mr. STAMM. Power generally is profitable, and that is the way we can pay off a portion of the irrigation costs that may be assigned to power. So, yes, the revenues are sufficient to repay the capital costs for commercial power, with interest, and any other costs assigned there, with one exception. One of these five projects is the Rio Grande project, and in that area the revenues are not sufficient to meet the capital costs with interest within the time periods of law. We are in the red. We have raised the rates as high as we can in comparison with the market rate. Now, obviously, if we raise the rate above the market rate we will not sell any power so we have raised rates just as high as we can and still retain a full market for the power.

Mr. STEPHENS. Thank you very much, Mr. Chairman.

Mr. JOHNSON. The gentleman from New Mexico, Mr. Lujan.

Mr. LUJAN. Thank you, Mr. Chairman. Mr. Stamm, you say that these projects generally operate without a deficit?

Mr. STAMM. Yes, sir.

Mr. LUJAN. Why don't you just sell them off to somebody to run them as private utilities instead of having the Government run them?

What is the advantage of us as a government running them as opposed to selling them off?

Mr. STAMM. Well, in the first place, in addition to paying off the costs assigned to the commercial power, with interest, they do pay a sizable portion of irrigation costs that have been assigned to power for repayment. Therefore, irrigation costs in many project areas, like the Columbia Basin project, for example, and the Pick-Sloan Missouri Basin program will be repaid that otherwise could not have paid their way in total.

Mr. LUJAN. What you are saying is the power operation, the power customers, are subsidizing some irrigators?

Mr. STAMM. The power customers are providing some assistance to the irrigators. But, the irrigation benefits go far beyond the irrigator himself. The benefits of irrigation go to the communities in the region, in the State and even far beyond the locality of the project. A great deal of the transportation facilities, communication processing, marketing, and even service facilities in the towns that are established in these areas benefit from irrigation.

Now, these beneficiaries are also the power users. So the power users that are providing some assistance for irrigation are also beneficiaries of the irrigation. Irrigation provides a fundamental economic underpinning in the numerous valleys of the West that would be nothing more than high plains or sagebrush were it not for the irrigation itself.

Mr. LUJAN. Or the areas that buy this power, the customers that buy this power ultimately, because that is who really gets to pay the cost. Generally it is the same people as the irrigators?

Mr. STAMM. They are in the area of influence and benefit of the irrigation project and it would include the irrigators, yes. The irrigators as well as others in the general area of the irrigation project.

Mr. LUJAN. Is it quite a substantial subsidization of the irrigation project?

Mr. STAMM. It varies from area to area. On some irrigation projects the irrigators are able to pay the irrigation costs fully. In other areas, with high elevations and short growing seasons, the irrigators are not able to pay a substantial part. It might be as low as 10 or 15 percent of irrigation costs, in which cases the remainder is assigned to power.

Mr. LUJAN. And those projects are pretty easy to identify where the irrigation costs can be met by themselves and not rely on power operation?

Mr. STAMM. Yes. That is determined in the detailed studies that are made before the projects are authorized.

Mr. LUJAN. Those where it is not, why would it be against public policy to sell them off?

Mr. STAMM. Well, the powerplants are not consigned to specific projects. Powerplants may be on the main stem or major tributaries in a river basin and the irrigation projects are also in that basin, but not directly related to a specific powerplant. The powerplants are all interconnected, those in the basin as well as between basins. There would be no feasible way to allocate the power from a specific powerplant to a specific irrigation district. The value of the power is greatly enhanced because of the interconnection between projects, not only among our Federal powerplants, but also among non-Federal. We are interconnected with the non-Federal system also. And also, our

powerplants are all hydroelectric, which is uniquely adapted to meeting peak loads, while fossil fuel fired steamplants are best suited to meet base loads.

And by coordination and cooperation we can exchange power in this total interconnected system whereby the steamplants can meet base loads and the hydro can meet the peak loads.

Mr. LUJAN. But that could happen anyway regardless of who owned the plant.

Mr. STAMM. You get into some extremely difficult accounting, and cost keeping.

Mr. LUJAN. Well, you just said that it is so complex, and really it is, but I thought perhaps that we could—

Mr. STAMM. There is one other thing that I didn't mention. Originally—I should not say originally, but back in the thirties one of the justifications for the Federal Government being in the power production business was to establish a yardstick to demonstrate what the costs of power were, and as you know, during the thirties and thereafter, due largely to several Federal programs in the power field, the availability of power has been extended to almost everybody in the West, rural areas as well as urban areas, and this was not true prior to the thirties.

Mr. LUJAN. Do you think a lot of that might have been from the rural electric co-ops?

Mr. STAMM. Yes, and by law they are preference customers. We serve them first by law, and if we have power available, beyond that which preference customers can use it is made available to the non-preference customers.

Mr. LUJAN. Let me leave that subject for a moment and get to probably the very reason for the introduction of this legislation and the problems that you are having. It appears at least to those that do not agree with you that there is not sufficient input from those people affected as you would have in a hearing with the public service commission for example.

The public service company of New Mexico, should it want to raise its rates, would have to go to the Public Service Commission in New Mexico and establish its needs. Of course, the Commission would make the final determination. There seems to be the impression, at least I gather from Mr. Moss' testimony, that there is not enough customer input. You say that there is. But, they say there is no sworn testimony for example, there is no cross examination to bring out the facts. Do you not really think that these things are needed and should be incorporated into a hearing process?

Mr. STAMM. I believe completely in open, objective communication with people with whom we deal. I believe in public involvement. We have launched a strenuous program in this regard and I believe that we should meet with all those folks concerned and involved with rate increases.

Now, regarding the types of meetings that are held, whether they have been an informal or a formal type, it seems to me that the general practice would favor the informal type. I believe the Federal Power Commission follows the informal approach. I believe the environmental hearings follow the informal approach. The formal hear-

ings do get unduly complicated. Sometimes for those you bring in an outsider to chair the meeting and he might be somebody that really has no technical background or policy background for the hearing. And these issues are mostly technical. We believe they can be discussed openly, across the table in a better way and get a better understanding among all concerned on an informal give-and-take basis, face to face.

Mr. LUJAN. But you do not think that kind of lends itself to the feeling by the one who is opposing the action to be taken that well, I went in and I testified and they patted me on the head and said well, fine, thank you for coming in and we will see what we can do about it, and just go on and do whatever would have been done?

Mr. STAMM. Well, that person's testimony would be included in the records of the hearings. And I believe in the hearings that we held any submitted testimony, including statements which were filed, were made a part of the record of the hearing. All testimony was compiled as a total backup to the hearing and was made available for any and all to review.

Mr. LUJAN. You are saying that that testimony is thoroughly reviewed and all recommendations are taken very seriously and a decision is made?

Mr. STAMM. Yes, sir. I think it is reviewed as thoroughly as if you went through the formal route. Now, I am not saying there is no room for improvement. I think there is always room for improvement. We are constantly striving for improvement.

As was indicated today, this was the first time that the rates in the Central Valley project have ever been raised since the inception of the project, and of the five projects involved. I think perhaps that is true of three of them. The most recent rate increase anyplace was 9 years ago, but we anticipate that rate increases will be required more frequently in the future and, therefore, we are establishing a formalized procedure. We will make that procedure available to this committee and to our customers and others. If they have comments on the procedure as proposed, and we think it needs modification, we will take that into account. We do propose to establish and announce a procedure so that all will be aware of our intentions.

Mr. LUJAN. One final question. You close your statement by saying you would have no objection, that the Department would have no objection to a requirement that this rate change be confirmed or approved by the Federal Power Commission.

What you are really saying there is to let them, who have the expertise, review what we have done rather than opening the whole hearing process up all over again, and if they agree, then that stands.

What if they don't agree? Does that prevail over the judgment of the Secretary?

Mr. STAMM. I want to ask Mr. Pelz to answer that.

Mr. PELZ. Well, that is generally true, yes, sir.

Mr. LUJAN. And then you are abdicating, the Department is—

Mr. PELZ. With respect—we are not particularly advocating this, Congressman. We would not object, if the Congress feels that this is wise, to subjecting the reclamation rates to the same review procedures that apply to the rates of the Bonneville Power or Southeastern or Southwestern Power Administrations. In effect, the FPC has a veto power.

Mr. LUJAN. Thank you.

Mr. JOHNSON. The gentleman from Oregon, Mr. Dellenback.

Mr. DELLENBACK. Thank you, Mr. Chairman.

What you are saying really on that, in response to Mr. Lujan's last question, is that you would not object if the Congress were to bring into harmony the procedure already being followed on four of the projects with this particular fifth project that we are here talking to, is that in effect correct?

Mr. STAMM. That is correct.

Mr. DELLENBACK. So you are not, I understand, affirmatively appearing before us and requesting that change in the law, but you just see the consistency where they are already doing it in fourth-fifths, and if they bring the fifth one in harmony that would make sense and then what you are saying this bill would be inconsistent where we have a new kind of a procedure?

Mr. STAMM. That is correct.

Mr. DELLENBACK. Mr. Stamm, in one part of your testimony you indicate why it is that you really feel that it would not be sound policy to give to the Federal Power Commission not this power of review that we are talking to, but the power to make independent judgments on pages 6 and 7 of your testimony.

I think very cogently you talk about the complexity of the decision, you talk about the matter of the proper accounting, cost allocations, and the administration of the repayment and the planning for projects, and you say they involve important policy judgments, and that the FPC has no experience in these important aspects. And you think that it would cause confusion and inefficiency and uncertainty if the FPC were given this particular power. I wonder whether you can make clear to me why you feel they do not have the expertise to make this kind of a policy judgment, if we gave them the authority to make it independently?

At the same time you say you are willing to have them have a veto power. Do they not take into account, if they are leaning toward a veto, the same type of policy questions that you just alluded to when objecting to giving them authority?

Mr. STAMM. I do not think so, Mr. Dellenback. Our projects are multiple purpose in character. By act of Congress in the authorization they include not only power generation, but management of a river system for irrigation, for municipal water, for industrial water, for fish and wildlife enhancement, for recreation, for pollution control, or flood control.

And to mesh all of these responsibilities together into their relative priority in any given situation is a very complex approach. Our day-to-day operation involves not only our own people, but the Corps of Engineers in particular in the flood control aspects of the operation, and the State officials in connection with the water laws and the authorities and the private rights under State law, and we do file under State law for water rights for all of our projects.

Power does not have No. 1 priority. It might have the last priority in some cases. And these are the kinds of things that do have an effect on the power generation, the costs as well as the revenues, and I think that because of that situation it is highly significant that the Secretary have the responsibility to determine rates pursuant to his own obligations under the law.

As to the Federal Power Commission, as I said, we would have no objection to their reviewing these rates. If they find in considering the obligations of the Secretary that they think he has done wrong, or has overemphasized something, or failed to consider some aspect, they would have veto power and in that case we would have to take their views under advisement.

If we agreed with them we would modify the rates and resubmit for their approval. If we disagreed, we would certainly negotiate with them to see if we could not find a meeting of the minds.

Mr. DELLENBACK. As I have listened to this testimony and to what the chairman and the subcommittee has said, I can understand his being troubled in this situation.

You can understand it no doubt. You can understand no doubt the pressure the preferential users have been put to in this regard and I am most empathetic to this. At the same time, I am troubled about the Congress legislating uniquely on this one issue when there are four others that we have a different policy on. I am not persuaded myself as yet that we should make this kind of a unique stand in this case as contrasted with enacting legislation dealing with the five projects in Harmony. But, I am not sure, Gil, that I see the point of distinction that you are trying to make for me. I find very logical your contention that this is not a mechanical thing of setting rates, that there are all sorts of complexities involved in it, and those complexities are of such a nature that you feel that it would be unsound to give to the Federal Power Commission, which does not deal with this kind of policy, generally speaking, the authority to move in and dictate to you what the rates will be. I think that is a very sound type of argument. But, I am not sure that I see clearly why it is unsound that they must crank all of these processes in if they are to set the rate independently, that you apparently do not think it is unsound if they crank all of the processes in in reviewing what you have already done. Now, do you think that there is really a major distinction as to what they would bring into consideration if they were independently establishing a rate with the power to tell you what you must do?

Mr. STAMM. I see your point. And I think you have a good point. I do not think that establishing the rate on reclamation project is more complex than it is in regard to the other four Interior power administrations. And as Mr. Pelz said, we are not advocating legislation in this regard.

We feel, however, that we do not have a strong ground on which to argue that there should be two separate policies in administering the power program of the Department of Interior. I think that adding reclamation to the list would put burdens on the Federal Power Commission, and responsibility and added complications that they do not now have in connection with the other four administrations in Interior or with the non-Federal sector where they have regulating authority. And I am not sure whether they would feel the necessity to broaden the scope of expertise within their organization to review all proposed rate increases or not, or whether we, through a process of briefing, which we do within the Department at several levels, would carry that type of briefing to the Federal Power Commission. If so, I think what they would really be doing would be deciding whether they think our rationale is acceptable.

Mr. DELLENBACK. So, I read now you as really saying, as we try to think it through, that it is possible that this one of the five is really more complex than the other four and there are certain additional factors and certain policy factors, that are present in this reclamation project that are not present in the other four. As to those other four, when the power commission reviews what you do, they do not need to exercise as much independent judgment and they are, therefore, qualified to exercise the largely nonpolicymaking review?

In this one project, because you do feel it should be different, you really would prefer that there be no review, that if you have to make a change in procedure to get somebody independent moving in because it is more complex, do you think it would be sounder to give them only a veto power instead of a power to move in and independently determine a rate which you would have to go along with?

Mr. STAMM. I think that is correct and I think we have to base our judgment and recommendations on anticipation rather than on experience. It is difficult to say categorically that this could not work because, in fact, in the area of operation of the Bonneville Power Administration, there are involved Federal reclamation projects, along with the Corps of Engineers projects. This requires a great deal of coordination with the Corps, with Bonneville, and with us in the management of the river. This has been worked out through a very sophisticated computer system, so it is not impossible. But, it would add significant complication if it were extended to the broad areas where reclamation has the management and marketing authority.

Mr. DELLENBACK. One other thing I would make comment on or ask about is I must confess that as you were in dialogue with my colleague, Mr. Lujan, about the formal hearings versus the informal discussion, the full evidentiary procedure versus the non, I saw the analogy to the present circumstance.

Because you are here in a situation where under the procedures that we all follow, the final decision will be made on this side. It is much more difficult for you to appear before us from your standpoint in a rigid, rigidly controlled procedure and be testifying before us instead of all sitting at a table together talking about the project. Now, you are saying that in the situation where you sit on this side of the desk, and there are others appearing before you, you think that instead of this kind of a formal relationship, and we are sort of relaxing under our able chairman today, but which is really what we are dealing with, it is better to have informal discussions and an informal give and take and you and I are giving and taking a little bit at this time, that it is a better way to get to some sound conclusions than in the rigid, structured, one person testifying before the other? Is that really what you are telling us?

Mr. STAMM. Yes, sir. That is true. And that is based on my personal experience over the years. I like the informal approach where we can lay all of the cards on the table face up, we can discuss the pros and cons with people that have interest, and disinterest, and if the pros outweigh the cons we ought to be able to convince them of that. If we cannot resolve differences at least we each know the position of the other. We know why he has to take the position he has taken. And I think reasons and justification comes out much more clearly in the informal discussion than in formal ones.

Mr. DELLENBACK. Just in this last week, as we all do on this side, I had occasion to sit down there and appear before another subcommittee testifying and I want to assure you that both the view and the comfort of the seat is much better here.

But, one last question on that.

You are not suggesting that in this kind of an informal discussion, as opposed to a formal hearing, that it should be in secret?

Mr. STAMM. In secret? No, sir.

Mr. DELLENBACK. You are willing that it be fully open with the public and the press and everything present? That it would be better to have it in an informal type of hearing rather than a formal one?

Mr. STAMM. Yes sir. That is correct.

Mr. DELLENBACK. Thank you very much, Mr. Stamm.

Mr. STAMM. Any attempt to keep it secret would only defeat our purpose.

Mr. DELLENBACK. Thank you, Mr. Chairman.

Mr. JOHNSON. Mr. Casey, our consultant, has a question or two.

Mr. CASEY. It is not a great deal different from the colloquy that you have already had, but the Secretary does market power under two separate statutes, one being section 5 of the Flood Control Act of 1944, is that correct?

Mr. PELZ. Yes; that is true.

Mr. CASEY. And that is his sole authority for the marketing of power in the four other systems that have been referred to here this morning?

Mr. PELZ. Well, that is not correct in the case of the Bonneville project, which has a special act which is similar to the Flood Control Act, but not identical with it. So, we really have three major statutes: Section 5 of the 1944 Flood Control Act, the Bonneville Project Act, and then the reclamation laws, principally section 9(c) of the Reclamation Project Act of 1939.

Mr. CASEY. Now, Congressman Moss quoted you with regard to section 9(c) and you have furnished us an opinion, a formal opinion concerning section 9(c), I assume?

Mr. PELZ. Yes.

Mr. CASEY. And you furnished that for the record, which we have not had a chance to read. Now, would you consider section 9(c) as a model of clarity and statutory expression, or would you consider it like I do, almost incomprehensible?

Mr. PELZ. Well, my view would be somewhere in between. I don't think it is incomprehensible, but it is like the Constitution, it speaks in rather general language and it is possible——

Mr. CASEY. Can we stipulate——

Mr. PELZ [continuing]. Possible to disagree.

Mr. CASEY. Can you stipulate that your predecessors, ever since 1939, have been interpreting section 9(c) and that various solicitors have rendered some very widely varying interpretations of it. Some as far-fetched as saying that the interest component on power could be used for repayment of certain other things like that, that have been repudiated by their successors and that, suffice to say, section 9(c) has a long, and lurid history of solicitors' interpretations? Would you stipulate that?

Mr. PELZ. No; I could not stipulate——

Mr. CASEY. All right, you don't need to.

Mr. PELZ. I couldn't stipulate to that, no.

Mr. CASEY. If you would not object to bringing the Bureau under the same procedural system that applies to the other four, as your last paragraph of your witness statement says, why could we not accomplish that by just repealing section 9(c) and letting the Secretary market power and reclamation under the same type of language that appears in section 5 of the 1944 act? Then we would not have to interpret section 9(c) any longer and we could do for the Bureau what we do for Bonneville or what we do for S.P.A.—Southeast Power Administration—and just once and for all clean up what section 9(c) means or does not mean by repealing it from the statute books?

Mr. PELZ. I assume you are referring just to that sentence in 9(c) that deals with rates and not the balance of the sentence.

Mr. JOHNSON. Yes.

Mr. PELZ. I would not want to comment on that right now, because there might be various legal ramifications of that.

Mr. CASEY. Well, if the committee decides to move forward with something here, and there have been a lot of suggestions made today, and a lot of different viewpoints reflected, and certainly one of the things that is going to be controversial in our deliberations is what you have said in your legal opinion, what you can do under 9(c) vis-a-vis no-deficit years. Now, maybe a good way to just take care of what you can do under 9(c) is to cause 9(c) to go away.

Mr. PELZ. Well, as the opinion points out, the Attorney General of the United States, in a 1955 opinion, did state that section 9(c) would be read in *pari materia* with the Bonneville Project Act and Flood Control Act, by which he meant to indicate that in general they should be construed as different statements of the same body of law so that the conclusion which that opinion reaches, by taking a look at the specific wording of 9(c), could be reached under the Flood Control Act.

Mr. CASEY. Well, you have testified that because of the spiraling costs and other costs to purchase power, that under existing rates, or under more modestly increased rates, that your study might show deficits for as many as 20 consecutive years and still show a payout at the end of the 50-year period?

Mr. PELZ. That is correct.

Mr. CASEY. The last study, and I am quoting from memory. As you can see I do not have the study, but the one that supported the 23 did, indeed, show a couple of years of deficit.

Mr. GRAHAM. You said the 23 percent. That is \$1.15, and that shows 21 years of deficit, or 19 years, I am sorry.

Mr. CASEY. Well, I have seen a study which I believe purports to support your promulgated rates that shows about 2 years of deficit.

Mr. BARTA. Yes. And that included both portions of the rate increase, the 77 as well as the other.

Mr. CASEY. Well, what bothers me about that, gentlemen, is simply this, that we can have a legal opinion that deficits are bad and therefore there should be none and yet we have a study that shows 2 years. You have promulgated rates on the basis of that. Thus I am wondering what you would promulgate if you had 4 years of deficits, or 8 years or 12 or 21. If it is discretionary on the part of the Secretary

that he can indeed have 2 years of deficits but he cannot have 21 years of deficits it seems to me that any statute that would lend itself to that type of a determination or any legal opinion that would seem to sanction that type of a determination, is controversial to the point of just having the words mean nothing and, therefore, we would be wise to be rid of that kind of statute.

Mr. STAMM. There is minimum there, Mr. Casey. I think that any rate established in any one of these areas must meet the repayment obligations of law within the 50-year period if that is what prevails for a specific project. And that should be primarily the minimum criteria. There is nothing in the law that requires a surplus at the end of the payout period.

Some of these issues have developed over the fact that our projects are not identically authorized. In many cases we have a project in which the total project is authorized at one time and in one action, in which case we know precisely then what the irrigation assistance must be from the power revenues for that project.

In the case of the Central Valley project that is not the case. The Central Valley project is an open-ended project, and we keep adding to it through authorization of additional units. And as you add each unit, to the Central Valley project, it has an effect on the obligation of power revenues to pay the power costs as well as the irrigation assistance. So the obligation on power revenues is constantly changing.

In the process of authorization, one of the first questions that frequently is asked in testimony on the unit for authorization is: Are there sufficient power revenues to cover the assistance required. Heretofore there have been. There has been a surplus sufficient to cover the required assistance for each new unit. That surplus shows up in our annual rate and repayment studies.

After some 25 years of operation, that surplus has diminished because the assistance required has used it up. So, the question logically comes: What do you do now? Do you establish a rate which has no surplus, and then the answer to the committee's question is no, sir; there are not sufficient revenues to cover this unit. It will require a rate increase if it is authorized in order to cover the assistance that is required.

Or, do you have some cushion in revenues to cover this type of situation? Now, a cushion was not designed into the rate increase initially announced that resulted in the large surplus. Some surplus has been desirable, and some surplus has always been prevalent heretofore. But the initially announced rate, before it was split into two parts, was related very largely to the issue of the no-deficit year because under that policy it required a rate sufficiently large to meet the point the annual repayment schedules in continuing that rate caused the surplus at the end of the payout period. Presumably if no new authorizations came into the picture, or no other items of cost increase came into the picture to justify the surplus, the logical thing to do and I think the only thing the Department could eventually do in that circumstance would be to announce a rate decrease.

Thus you would, in fact, come out at the end of the payout period with no surplus.

Mr. CASEY. Well, I understand this very well. The point that I am trying to get around to, and I may or may not ever elicit any agree-

ment from you gentlemen on this, is relative to a statute, that statute being section 9(c) which clearly applies in the Bureau of Reclamation—the 1944 act has no bearing in this case of the Central Valley at all. Under a rigid interpretation of that statute of no-deficit years, you are enabled to announce a proposed rate increase approaching 50 percent.

You made certain other adjustments in your criteria on the replacements and on the hydrology and you relaxed the no-deficit year rules sufficiently to allow 2 years of deficits. That put the rate increase down to 23 percent. A statute that is capable of such widely varying swings in interpretation, in my humble opinion, is a poor statute. You could have perhaps tolerated 4 years of deficits and got that rate increase from the 1920's down to the teens.

So this is a statute that is so loose that it allows, to my mind, an inappropriate degree of subjectivity in determining how many years of deficit you can have. I would expect that this committee, if it brings out anything, will give you some guidelines on the subject of how many years of deficit you may indeed have.

But, I am not too sure that it would not all wash out if we did what you suggested that you would not be offended by in the last paragraph of your statement, of having a disinterested overview and veto by the Federal Power Commission. And certainly your critics, and your customers ought to be satisfied with that.

Maybe one of the good ways to accomplish it is just to have you market Bureau power under the provisions of the 1944 act rather than the 1939 act. That is the balloon I am floating. That is all.

Mr. STAMM. I am sure, Mr. Casey, that not all of the difficulties would wash out solely with having an independent review because any rates recommended would have to be based on certain assumptions. And one of the assumptions could be with respect to the policy that you have enunciated and discussed, that is, if you can have 2 years of deficit why could you not have 3, and if you can have 3, why not have 4, and where do you stop. And I do not think an independent review or an independent reviewer would necessarily be in a position to interpret policy in the Department. So, there may be two issues.

Mr. CASEY. Yes. I understand that. And that is section 2 of my act, is to give you some guidance on how many years of deficit you might have, as I visualize a statute in that regard.

Complaints have been leveled against you—and I will not characterize them except to say they have been shrill—regarding your alleged failure to give due process and disclosure. These are things that you have now assured the committee you are working on in your system to prevent that administratively. Another part of our problem is that we do not have this continually coming up in the future.

The second part is; what are we going to do about the Central Valley project specifically. I guess the root of that is found in what is a reasonable number of years in which to have a deficit. It just may be that the committee will see fit to legislate something fairly specific in that area, if we can figure out how to draft it. I do not know.

That is all I have.

Mr. JOHNSON. Any further questions?

If not, we want to thank you gentlemen for coming here and giving us the benefit of your testimony on behalf of the legislation we are

considering here. And this has been a very controversial subject matter for the past 2 years with many people. As I said earlier, I have been involved because we have five of the preference customers who are affected by the new rate increase.

As I understand it, they are now in court with the Bureau of Reclamation and the Department of the Interior.

Mr. PELZ. Yes, sir.

Mr. JOHNSON. And what will happen to their case there is more than I can say. But, I thought possibly if we could work out a piece of acceptable legislation, why it might eliminate problems in the future.

Mr. STAMM. We appreciate the opportunity to meet with you, Mr. Chairman, as always.

Mr. JOHNSON. Mr. Casey has one more thing.

Mr. CASEY. No, no. This has to do with the schedule for this hearing. It was scheduled for 2 days. If it has escaped anybody's attention, the Monday session will be in the Interior Committee room in 1324.

Mr. STAMM. Yes, sir, and that hearing is for non-Federal witnesses, I understand.

Mr. CASEY. Yes.

Mr. JOHNSON. The committee will be adjourned.

[Whereupon, at 1 p.m., the hearing was recessed to reconvene on Monday, May 20, 1974, at 10 a.m.]

REVIEW OF ELECTRIC POWER RATE INCREASES

MONDAY, MAY 20, 1974

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON WATER AND POWER RESOURCES OF THE
COMMITTEE ON INTERIOR AND INSULAR AFFAIRS,
Washington, D.C.

The subcommittee met, pursuant to notice, at 10 a.m., in room 1324, Longworth House Office Building, Hon. Harold T. Johnson (chairman of the subcommittee) presiding.

Mr. JOHNSON. The Subcommittee on Water and Power Resources will please be in order.

The hearings on H.R. 14221—to provide for the review of increases promulgated by the Secretary of the Interior on November 1, 1973, in rates for electric power sold at five Bureau of Reclamation projects, and for other purposes, will be resumed today.

The bill, the departmental report from the Interior Department and reports from the Office of the Comptroller General and Federal Power Commission were entered in the record at the beginning of the Friday hearings.

This morning our first witness will be Mr. Melvin Richter. Attorney, representing Arizona Power Authority, purchasers of Parker-Davis Colorado River storage project.

Mr. Richter, you are welcome here this morning, and we are ready to hear your testimony.

We are sorry we don't have more people, but on Monday morning it is a job to get people to attend hearings.

STATEMENT OF MELVIN RICHTER, ATTORNEY, ARIZONA POWER AUTHORITY, PURCHASERS OF PARKER DAVIS AND COLORADO RIVER STORAGE PROJECT

Mr. RICHTER. The problem is not the people attending but the people who ultimately read the record and will hopefully read the record in these proceedings.

Mr. JOHNSON. You have a very complete and lengthy statement here. It will appear in the record as if read in full, and you may summarize in any way you see fit.

Mr. RICHTER. My submission consists of a full statement and three attachments.

Mr. JOHNSON. The attachments will appear in the record also.

Mr. RICHTER. Thank you, sir.

My summary statement, if I may, I would like to read. It won't take more than 5 minutes. It is the top paper.

Mr. JOHNSON. Go right ahead.

Mr. RICHTER. Mr. Chairman and members of the subcommittee, my name is Melvin Richter. I am a member of the law firm of Littman, Richter, Wright, and Talisman with offices at 1001 Connecticut Avenue NW., Washington, D.C. 20036. As such, I am Washington counsel for the Arizona Power Authority. On behalf of the authority and the Arizona purchasers of Parker-Davis and Colorado River storage project power represented by it, I wish to thank the committee for permitting me this opportunity to appear before it in support of H.R. 14221.

The Arizona Power Authority is a State agency established by the Arizona Legislature in 1944 to enable Arizona to secure and utilize power and energy generated on the Colorado River. The authority has worked effectively with both publicly owned and privately owned utilities and has made hydropower from the Colorado River available to all major load centers throughout the States at a minimum of cost.

In light of its experience with the Parker-Davis and Colorado storage project rate increases, which is detailed at length in the hearings before the Subcommittee on Conservation and Natural Resources on January 22 and 23, 1974, and which is summarized, Mr. Chairman, in the attachments which are attached to the full statement, the authority strongly supports the enactment of H.R. 14221, in order to remove any question as to the need for full hearings as a precondition to the promulgation of rate increases for Bureau power. By full hearings, we mean hearings at which the customers affected by the proposed rate increase are given full and complete opportunity to study and analyze all the relevant data and other materials and at which they have an opportunity to cross-examine Bureau witnesses with regard to such data and materials on the record and to present rebuttal materials in opposition thereto.

It is our position that the law as enunciated by the courts, particularly by the Court of Appeals for the District of Columbia Circuit, clearly indicates that full hearings are required before the Bureau can validly promulgate and make effective any rate increase for Bureau power.

I might say by way of digression that attachment C to my full statement consists of a memorandum analyzing many of the more recent cases of the District of Columbia Circuit. I might indicate there is one case not included but I point to it in my full statement which is the *Mobil Oil Corp. v. Federal Power Commission*, by a 1973 decision of the Court of Appeals of the District of Columbia Circuit on the matter.

I realize, of course, that the NCPA has a complaint pending against Secretary Morton in the District Court for the District of Columbia. However, that is in a very preliminary stage at this point and it will be some time before we have a definite ruling on it.

Accordingly, in order to remove any question with regard to the need for full hearings, we believe that Congress should enact H.R. 14221, specifically providing for full hearings as a precondition to the promulgation and making effective of any rate increase for Bureau power. The desirability of such legislation is, in our view, emphasized

by the facts (1) the Bureau and the Solicitor of the Department of the Interior has taken the position that it is not required to hold any hearing before it makes such rate increases effective and, (2) that while the Department's Assistant Solicitor for Power conceded at the hearings before the Conservation and Natural Resources Subcommittee that the Bureau had "goofed"—and this is a precise quote from his statement—in its handling of the rate increases promulgated November 1, 1973, there is no clear commitment on the part, at that time, of the Interior Department that full hearings will be provided in the next round of rate increases, much less that there would be any "hearings" held beyond the limited meeting held in connection with the rate increases promulgated November 1, 1973. I might digress, my full statement points out how meager that so-called hearing was that we were provided with.

In light of the wide variations in the interpretation of the phrase "public hearings" and the limited type of hearing which the Department officials apparently envision in connection with the subsequent increases in Bureau rates, the phrase "adequate public hearings" as used in Section 6, (page 5, line 21) of H.R. 14221 to describe the type of hearings required with regard to future Bureau rate increases would appear to be ambiguous, and I think that is an understatement. It leaves the door wide open as to the hearings the Bureau may hold. To remove the ambiguity and make clear that full hearings are required, we recommend that that language be revised to describe the required hearings for future rate increases as "hearings conducted in accordance with the requirements of Section 554 of the Administrative Procedure Act."

Provision 554 of the Administrative Procedure Act relates to hearings in adjudicatory proceedings.

There is one additional potential ambiguity as to which we believe a clarifying amendment may be in order. In contrast to the provisions of section 3 of H.R. 14221 which expressly provide for judicial review of the decisions of the Federal Power Commission with regard to the rate increases promulgated November 1, 1973, section 6 of the bill relating to future rate increases makes no provision of judicial review of such rate increases once promulgated by the Secretary. To remove the potential controversies which might arise as to whether such rate increases are or are not subject to judicial review and as to the scope of such judicial review, we recommend that language be added to section 6 so as to provide for judicial review in accordance with the provisions of section 701-706 of the Administration Procedure Act.

I want to thank you again at this time for permitting me to make this statement.

Mr. JOHNSON. Very good.

Your statement is quite clear as far as the record and the presentation here is concerned. Your support for the passage of H.R. 14221 is recommended unanimously.

The other material that you have left with us here will appear in the record, too, because you do refer to it in your statement as supporting data to your statement that was read.

[The above referred to statement plus attachments follows:]

STATEMENT OF MELVIN RICHTER, WASHINGTON COUNSEL FOR ARIZONA POWER AUTHORITY

My name is Melvin Richter. I am a member of the law firm of Littman, Richter, Wright and Talisman with offices at 1001 Connecticut Avenue, N.W., Washington, D.C. 20036. As such, I am Washington counsel for the Arizona Power Authority. On behalf of the Arizona Power Authority and the Arizona purchasers of Parker-Davis and Colorado River Storage Project power represented by it, I wish to thank the Committee for permitting me this opportunity to appear before it in support of H.R. 14221.

The Arizona Power Authority is a state agency established by the Arizona legislature in 1944 to enable Arizona to secure and utilize power and energy generated on the Colorado River. The Authority has worked effectively with both publicly-owned and privately-owned utilities and has made hydro power from the Colorado River available to all major load centers throughout the state at a minimum of cost.

We are here today to lend the Authority's whole-hearted support for the enactment of legislation which would make clear the obligation of the Department of the Interior to hold full hearings before increasing rates at which Bureau of Reclamation power is sold. By full hearings, we mean hearings at which the customers affected by the proposed rate increase are given full and complete opportunity to study and analyze all the relevant data and other materials, and at which they have an opportunity to cross examine the Bureau experts with regard to such data and material on the record, and to present rebuttal materials in opposition thereto.

As the Committee undoubtedly is aware, the Subcommittee on Conservation and Natural Resources has already held two days of hearings on January 22 and 23, 1974 at which it went in depth into the background and basis for rate increases promulgated by the Secretary of Interior on November 1, 1973. While these hearings were focused in large measure upon the rates proposed for Central Valley Project power, the Arizona Power Authority through its Chairman, Marshall Humphrey, and its consulting engineer, Gordon D. Jorgensen, managing partner of R. W. Beck & Associates of Phoenix, Arizona, presented statements detailing the Authority's experiences with regard to rate increases proposed by the Bureau for the Parker-Davis and Colorado River Storage Project power. An oral statement on these increases was also presented by Robert S. Lynch who also represented Electrical Districts 3, 4 and 6 of Pinal County, Arizona. To avoid undue repetition, the prepared statements submitted by Messrs. Humphrey and Jorgensen at those earlier hearings are attached hereto as Attachments A and B, respectively.

As detailed in these statements, the procedures followed by the Department in processing these rate increases made it virtually impossible for the Authority and purchasers of Parker-Davis and Colorado River Storage Power effectively to protect their interests. The Authority is not opposed to rate increases which are necessary to achieve payout. However, we are opposed to rate increases which will result in revenues in excess of those necessary to achieve payout. Moreover, we believe that we are entitled at least to test any proposed rate increase against such standards before it finally becomes effective. We had no such opportunity in connection with the Parker-Davis and Colorado River Storage Project rate increases which were promulgated November 1, 1973.

Although the Bureau held what it called a hearing, it was merely a brief meeting at which the Bureau and interested parties submitted statements. Thus, a one-hour meeting was held at Boulder City, Colorado on July 10, 1973 with respect to the Parker-Davis rate increases and similarly a two-hour meeting was held at Salt Lake City, Utah on July 12, 1973 with respect to the Colorado River Storage Project rate increases. Obviously, meetings taking that little time in connection with such intricate and complicated matters as these rate increases could not even begin to scratch the surface, and are in reality solely ritualistic.

Thus, what the Bureau has chosen to describe as a "hearing" consisted of nothing more than (1) a presentation, on the part of the Bureau, of exactly the same general materials which it had earlier furnished in the so-called "brochures" accompanying the rate increase announcements and (2) presentations, on the part of interested parties, of statements generally objecting to the lack of underlying data which they too had earlier submitted in writing. No questioning of Bureau personnel was permitted. Nor was there permitted any dialogue be-

tween their experts and ours. In a word, there was no interaction between the Bureau's presentation and those of the customers. They were like ships passing each other in the night.

I should add at this point that at the time of the "hearings" it is doubtful that even if given an opportunity, our experts could have asked all the appropriate questions or maintained an appropriate dialogue. At that time our experts had seen very little of the data on which the Bureau based the numerous assumptions it had to make in determining (1) the need for the rate increases and (2) the level of these increases. The so-called "brochures" accompanying the rate increase announcements on May 28, 1973, contained virtually no basic information. To be sure, our experts were able to request such data prior to the "hearings" on July 10 and 12, and did obtain some of the information requested, but what they had obtained by the time of the "hearings" left a lot of questions unanswered and raised innumerable new questions.

Even the Bureau recognized at those "hearings" that the parties had not sufficient time in which to complete their analysis of the proposed rate increases. As a result, it agreed to receive further comments on the proposed rate increases until August 31, 1973. However, even this additional seven weeks was woefully inadequate, particularly in light of (1) the number, scope and complexity of the assumptions underlying the proposed rate increases and (2) the Bureau's approach of not volunteering information but only furnishing information as asked in response to specific questions. While in many instances the Bureau supplied the additional data in response to specific questions, the data supplied frequently raised further problems and in some instances there was substantial delays in furnishing the data, so that it arrived just shortly before, or even after, the August 31, 1973 deadline. Consequently, when the August 31, 1973 deadline came for submitting our further comments, we still had not been able completely to analyze all the data that went into computer program which the Bureau had used in developing the proposed rate increases.

Thus, the lack of information and the tightness of the time schedule prevented our experts from doing the requisite in-depth analysis of the data underlying the proposed rate increases. The following chronology gives you some idea of the tight time frames within which we were called upon to react:

May 28, 1973—Bureau announces rate increases and "open hearings";

June 7, 1973—Regional Director Lundberg writes to Arizona Power Authority announcing hearing on July 10, 1973, enclosing Bureau "report" on Parker-Davis rate increase and requiring submission of comments by July 6, 1973;

June 8, 1973—Regional Director Crandall writes to CRSP customers announcing hearing on July 12, 1973, enclosing Bureau "report" on rate increase;

June 26, 1973—Arizona preference customers meet with APA to discuss rate increases and hear first preliminary report from consulting engineers emphasizing inadequacy of Bureau "reports" and lack of time to acquire and analyze essential information;

July 2-3, 1973—APA, Electrical Districts, et al., write to Secretary Morton and Regional offices protesting situation;

July 10 and 12, 1973—"Open hearings" at Boulder City, Nevada and Salt Lake City, Utah between customers and staff of Bureau Regional offices at which the Bureau offered no more information than was in their "reports";

July 26, 1973—Meeting in Phoenix, between customers and Bureau staff concerning Parker-Davis rate increase at which questions were proffered by customers and discussed;

July 30, 1973—Customers submit additional questions on Parker-Davis;

July 31, 1973—Customers submit questions to Regional Director Crandall concerning CRSP rate increase;

August 10, 1973—Regional Director Lundberg submits additional information on Parker-Davis increase;

August 28, 1973—Customers attend monthly APA meeting and hear report from consulting engineers concerning rate increases, information still not available, lack of justification for rate increases;

August 29, 1973—Customers write to Secretary Morton and Regional offices protesting rate increases and closing of record on August 31, 1973 without opportunity for sufficient study;

August 31, 1973—R. W. Beck submits its studies to Bureau on rate increases on behalf of APA and its customers;

August 31, 1973—Record closes without sufficient informational and analytical background.

Although, our experts were unable to complete their study and analysis of the proposed rate increases by the August 31, 1973 deadline, the limited study they were able to make nevertheless disclosed a number of serious errors and deficiencies in the Bureau's assumptions sharply undercutting the appropriateness of the proposed rate increases. These errors are summarized in the statements of both Messrs. Humphrey and Jorgensen attached hereto. Suffice it to add at this point that we are convinced that had we been accorded an opportunity for appropriate full hearings and an objective evaluation of the resulting record, we would have been able to demonstrate that the rate increase proposed for Parker-Davis power was excessive and that proposed for Colorado River Storage Project power was completely unwarranted.

In light of our experience with the Parker-Davis and Colorado River Storage rate increases which were promulgated November 1, 1973, we strongly support the enactment of H.R. 14221, in order to remove any question as to need for full hearings as a pre-condition to the promulgation of rate increases for Bureau power. It is our position that the law enunciated by the courts, particularly by the United States Court of Appeals for the District of Columbia Circuit, clearly indicates that full hearings are required before the Bureau can validly promulgate and make effective any rate increase for Bureau power. This position is, we believe, supported by the several cases discussed in a memorandum which we submitted at the hearings before the Subcommittee on Conservation and Natural Resources on January 22 and 23, 1974. For the convenience of this Committee, we are attaching a copy of that memorandum as Attachment C hereto. Another recent case supporting our position in this regard is *Mobil Oil Co. v. Federal Power Commission*, 483 F.2d 1238, 1260 (decided July 11, 1973).

While we believe that the Bureau must hold full hearings before promulgating and making effective any increase in rates for power sold by it, there is as yet no express statutory provision or definitive court ruling on all fours. We realize, of course, that the Northern California Power Agency and various of its affected members recently filed a complaint against Secretary Morton and Commissioner Stamm in the United States District Court for the District of Columbia (No. 61-74), claiming, *inter alia*, that the Bureau failed to provide the requisite procedural due process in promulgating the rate increases for Central Valley Project power. But that case is in a very early stage and it will probably be some time before a final definitive ruling will be forthcoming from that litigation.

Accordingly, to remove any question, particularly with regard to the form of, and the forum for, the required full hearings, we believe that Congress should enact H.R. 14221, specifically providing for full hearings as a pre-condition to the promulgation and making effective of any rate increase for Bureau power. The need for such legislation is, in our view, emphasized by the facts (1) that the Bureau has taken the position that it is not required to holding *any* hearings before it promulgates such rate increases and (2) that while the Department's Assistant Solicitor for Power conceded at the hearings before the Conservation and Natural Resources Subcommittee that the Bureau had "goofed" in its handling of the rate increases promulgated November 1, 1973, there is no clear commitment on the part of the Interior Department that full hearings will be provided in the next round of rate increases, much less that there would be any "hearings" beyond the limited meetings staged in connection with the rate increases promulgated November 1, 1973.

Thus, whereas the Department's Assistant Solicitor also claimed that the Bureau would "try to do a better job in laying out our procedures in advance" the next time around (p. 131) and "is committed to going through a procedure which permits our customers a full and reasonable opportunity to understand what the basis for our proposal is and to submit their comments to us" (p. 125), he nevertheless declined to go beyond that and claimed instead that government agencies hold many types of hearings and that "you get into a semantic argument as to what is a hearing (p. 125).

Moreover, when the Assistant Solicitor was asked to state what the Bureau's "new policy" was with regard to future rate increases, including "the type of public hearings that you envision", the Assistant Secretary for Power interjected in effect that the Department had no new policy on hearings and that the hearings which had been held on the November 1, 1973 increases constituted in his view appropriate "public hearings".

Subsequently, when the question was asked with reference to the Administrative Procedure Act as to the type of public hearing the Department was talking about, the Assistant Solicitor responded (1) that in the opinion of the

Solicitor's office the Administrative Procedures Act did not apply and (2) that the closest analogy was " * * * the rule type of proceeding where the proposed rule is published in advance and then a hearing is held at which the public has an opportunity to come in and submit their comments to the proposing agency, as to their reaction to it.

In light of the great variety in types of "public hearings" and the limited "hearing" which the Department officials apparently envision in connection with future increases in Bureau rates, it would appear that the description in Section 6 (page 5, line 21) of H.R. 14221, of "adequate public hearings" as to the type of hearings which would be required for such future rate increases in ambiguous and subject to widely varying interpretation. To remove this ambiguity and make clear that full hearings as described earlier herein are required, we recommend that that language be revised to describe the hearings required as "hearings conducted in accordance with the requirements of Section 554 of the Administrative Procedure Act."

There is one additional potential ambiguity as to which we believe a clarifying amendment may be in order. In contrast to the provisions of Section 3 of H.R. 14221 which expressly provides for judicial review of the decisions of the Federal Power Commission with regard to the November 1, 1973 rate increases. Section 6 of the bill relating to future rate increases makes no provision for judicial review of such rate increases once promulgated by the Secretary. To remove the potential controversies which might arise as to whether such rate increases are or are not subject to judicial review, and as to the nature and scope of such judicial review, we recommend that language be added to Section 6 so as to provide judicial review in accordance with the provisions of Section 701 *et seq.* of the Administrative Procedure Act.

ATTACHMENT A

ARIZONA PREFERENCE CUSTOMERS OBJECT TO THE BUREAU OF RECLAMATION'S ARBITRARY CONDUCT AND LACK OF ESTABLISHED PROCEDURES IN PROPOSING POWER RATE INCREASES FOR THE PARKER-DAVIS AND COLORADO RIVER STORAGE PROJECTS

Reclamation power has always been marketed at the lowest rate which would produce enough revenue to pay for the project from which the power is generated. Indeed, this is the basic concept in public power. Ostensibly to meet statutory requirements to pay for the projects, the Department of the Interior and the Bureau of Reclamation announced, on May 28, 1973, proposed rate increases for power generated at its Parker-Davis and Colorado River Storage Project facilities. The Arizona Power Authority and other preference customers have, in the short time allowed and with the incomplete information provided, analyzed these increases and cannot find justification for either of them.

Thus, we fear that the Bureau and the Department may be departing from the Congressional policy by which reclamation power is sold and raising rates to generate income for purposes other than to pay for the projects. The haphazard procedures, restrictive time limits, and informational gaps we have experienced only confirm our fears. Moreover, the Bureau's resistance to realistic determination and treatment of expenditures adds to these feelings and makes us wonder whether the Bureau is intending to become or has already become a profit-oriented organization, contrary to law and Congressional policy.

We believe that the Bureau is without authority to change such basic policy without Congressional approval. We object to implementation of any rate adjustments now and until the policy issues are clarified and the customers' objections are resolved. We support the investigation by Chairman Reuss and the Conservation and Natural Resources Subcommittee of the Committee on Government Operations. We have followed the Chairman's efforts and those of Congressmen Moss and McCloskey to uncover the Bureau's supposed justification for these rate increases. We note that such justification has not yet been supplied to the Bureau's preference customers and that such lack has generated the necessity for this hearing. For these reasons, the ultimate decisions on the necessity for any rate increases should not be taken, if at all, until the beginning of the next fiscal year, July 1, 1974. We emphasize that we are not opposed to any rate increase(s) demonstrated to be necessary to achieve pay out in a reasonable manner. We are, however, opposed to implementation of any rate increases without full and meaningful participation by the preference customers and their consulting engineers.

THE BUREAU OF RECLAMATION LACKS PROCEDURAL SAFEGUARDS TO PREVENT ARBITRARY
DECISIONS IN RATEMAKING

The basic problem is that the Bureau does not have established procedures which safeguard against administrative arbitrariness and abuse of discretion in the decision-making process which the Bureau must go through before proposing rate increases. If proper procedures had been in existence, none of these problems would be before the Subcommittee. Appropriate procedures and an adequate administrative record would have already developed fully all the points of controversy and highlighted the policy considerations inherent in them. This hearing must instead probe basic areas of information because no adequate record and no proper administrative process were developed.

As we see it, the Department and the Bureau have certain obligations which must govern their deliberations concerning any proposed rate increases:

1. The Bureau must comply with the law and Congressional policy in analyzing the need for rate increases.

2. The Bureau must compile an administrative record to demonstrate that its decisions are not arbitrary or capricious, do not abuse the discretion delegated to it, and are not otherwise unlawful. We agree with the Chairman and Congressmen Moss and McCloskey that a major change in rates such as announced for several of the projects deserves extensive and broad review procedures not now used by the Bureau.

3. The Bureau must assess the environmental, as well as the economic, consequences of its program to raise rates on these projects as well as alternatives to such program. We note that no program environmental statement has been filed and that negative determinations have been filed separately for each increase. Yet, the Chairman has pointed out that the rate increases will affect some four hundred preference customers and about 5,000,000 kilowatts capacity out of a total of 7,000,000 kilowatts marketed by Reclamation, ultimately impacting on millions of consumers.

4. The Bureau has an affirmative obligation to demonstrate the absolute necessity of any increases in order to comply with the spirit of the President's economic program to fight inflation. The Bureau has not discussed nor considered alternatives to rate increases such as adjusting spending and construction schedules.

5. The Bureau must give its preference customers sufficient access to its records and studies and adequate time for preparation and analysis in order to participate meaningfully in this decision-making process. As our consulting engineers' summary comments below point out, this is one of the most glaring inadequacies in the administrative process by which these rate increases were handled. Rate analysis that must start with Bureau figures robs independent review of much of its meaning. These figures reflect basic assumptions that stand unchallenged unless they, too, are analyzed.

The procedural inadequacies of the Bureau's administrative process are magnified considerably when one considers that this is the first rate increase attempted by the Bureau for Parker-Davis or CRSP and is doubly unique because increases have been announced for five projects totalling 5/7ths of the Bureau's entire kilowatt capacity. This endeavor will set the precedent for future rate increases on individual projects or "across the board". Thus, the significance of the Bureau's action transcends the immediate impact of a rate increase.

The Bureau's lack of procedural safeguards in its decision-making process on rate increases has led to at least one glaring disparity in treatment among the Bureau's preference customers: Missouri Basin customers were granted additional time (to October 24, 1973!) to submit their consulting engineers' report, but Parker-Davis and CRSP customers were not given such a delay, even though requested, and were compelled to file their reports by August 31st. This disparate treatment has not and cannot be justified by the Bureau and serves further to illustrate the need for the procedural safeguards which are now lacking in the Bureau's administrative processes for rate analysis.

One further item shows the need for procedural safeguards. The Bureau admits that these rate increases affect some four hundred preference customers and about 5,000,000 kilowatts of the Bureau's 7,000,000 kilowatts of capacity. Yet the Bureau refuses to recognize that the rate increases are a Bureau program for which an environmental impact statement is necessary. The Bureau asserts that it has complied with NEPA by filing negative determinations for each of

these increases. Federal action of this magnitude certainly warrants more. (Indeed, it could be argued that each increase should be accompanied by an impact statement focusing on local matters following a broad program statement.) We fear this myopia is a further indication of the Bureau's lack of sensitivity to the serious policy questions that underlie its proposed actions.

THE INADEQUACY AND ARBITRARINESS OF THE BUREAU'S ADMINISTRATIVE PROCESS
UNFAIRLY RESTRICTED ANALYSIS BY OUR CONSULTING ENGINEERS

Three basic problems confronted our consulting engineers, R. W. Beck & Associates. These problems were (1) the lack of opportunity to examine and analyze sufficient background data used by the Bureau of Reclamation; (2) the lack of time to analyze the information which was available and determine what additional information was necessary, and (3) the lack of proper hearings.

The first problem arose when the Bureau, in notifying Parker-Davis and CRSP customers of the proposed rate increases, enclosed only brief reports ("Brochures") concerning the increases. These reports contained little or no data to substantiate the assumptions used by the Bureau in calculating the need for power rate increases. More importantly, no concise and clear criteria were set forth showing how the rate studies were made. Back-up data for these brief reports was not included and it was necessary to ask specific questions and request specific data with regard to back-up material and assumptions. In response to these specific questions, the Bureau supplied additional data concerning its power system payout studies. The data, while helpful to a degree, raised additional questions as to the propriety of the proposed rate increases. Additionally, certain other basic data was not readily available and therefore was not supplied by the deadline for submission of our reports, August 31, 1973. Caught in this position, we were unable to analyze all the background data that went into the Bureau's computer program. What we were able to do was model a computer program after that used by the Bureau and then make independent repayment studies modifying certain elements of the Bureau's studies. Even with this major handicap we were able to point out a number of questions about the adequacy of the Bureau's studies and raise serious questions about the need for these rate increases.

The second and equally limiting problem was the time frame within which we were forced to operate. The following chronology of events indicates the fantastic time strain our consulting engineers were under in attempting to come up with an analysis of the proposed rate increases. In effect, our engineers had only seven weeks after the Bureau's so-called "open hearings" in which to elicit information from the Bureau, develop an independent computer program and analyze the rate increases. Lack of information and lack of time prevented our engineers from doing any sort of in-depth analysis of background data used by the Bureau. The following chronology speaks for itself:

May 28, 1973—Bureau announces rate increases and "open hearings";

June 7, 1973—Regional Director Lundberg writes to Arizona Power Authority announcing hearing on July 10, 1973, enclosing Bureau "report" on Parker-Davis rate increase and requiring submission of comments by July 6, 1973;

June 8, 1973—Regional Director Crandall writes to CRSP customers announcing hearing on July 12, 1973, enclosing Bureau "report" on rate increase;

June 26, 1973—Arizona preference customers meet with APA to discuss rate increases and hear first preliminary report from consulting engineers emphasizing inadequacy of Bureau "reports" and lack of time to acquire and analyze essential information;

July 2-3, 1973—APA, Electrical Districts, et al., write to Secretary Morton and Regional offices protesting situation;

July 10 and 12, 1973—"Open hearings" at Boulder City, Nevada and Salt Lake City, Utah between customers and staff of Bureau of Regional offices at which the Bureau offered no more information than was in their "reports";

July 26, 1973—Meeting in Phoenix, between customers and Bureau staff concerning Parker-Davis rate increase at which questions were proffered by customers and discussed;

July 30, 1973—Customers submit additional questions on Parker-Davis;

July 31, 1973—Customers submit questions to Regional Director Crandall concerning CRSP rate increase;

August 10, 1973—Regional Director Lundberg submits additional information on Parker-Davis increase;

August 28, 1973—Customers attend monthly APA meeting and hear report from consulting engineers concerning rate increases, information still not available, lack of justification for rate increases;

August 29, 1973—Customers write to Secretary Morton and Regional offices protesting rate increases and closing of record on August 31, 1973 without opportunity for sufficient study;

August 31, 1973—R. W. Beck submits its studies to Bureau on rate increases on behalf of APA and its customers;

August 31, 1973—Record closes without sufficient informational and analytical background.

The third problem encountered by our engineers was the lack of opportunity to confront Bureau officials with conflicting data and to have a dialogue with them or cross-examine them with regard to these conflicts prior to the close of the record. On March 9, 1973, Deputy Assistant Secretary Wilson wrote to Chairman Reuss promising that the Department would conduct hearings on the rate increases and would provide ample opportunity to the customers to examine supporting documentation for the rate increases and to question Bureau officials about relevant aspects of the increases. However, when we were notified about these so-called "open hearings", we were advised in June that the July hearings would be "informational" and would consist of an explanation of the rate increases by Bureau officials and position statements by those customers who wished to attend or submit written statements. When we arrived at the hearings we found that the Regional staffs were taking their directions from Washington. Under such directions, the Bureau's presentation consisted of exactly the same material that had been presented in its brief reports accompanying the rate increase announcements, and nothing more. We were not allowed to question any of the Bureau officials present and were restricted to merely making our presentations which we had already been required to submit in writing. Our position at the "hearings" was essentially that we had not been given enough time or information to make an appropriate study of the proposed rate increases. We advised the Bureau that our engineers would require at least sixty days after the furnishing of sufficient data in which to make analyses of the proposed increases. We were advised that we could submit further written material to the Regional Offices of the Bureau no later than August 31, 1973. Over the next seven weeks our engineers began acquiring data in order to analyze the increases and submitted questions to the Bureau concerning additional data and clarification that was needed. The record closed on August 31, 1973. The open hearings promised by Deputy Assistant Secretary Wilson never took place. Several of our questions and requests went unheeded. A number of troublesome areas were left completely unexplored. Informal meetings were held after the close of the record both at Regional Offices and in Washington, but these were essentially useless. The die was cast.

Because of the lack of essential data and the extremely limited period in which to make an evaluation of the proposed rate increases, it was not possible to make a complete and detailed evaluation of the Bureau's actions. The arbitrary treatment given the customers and their engineers prevented this. Had adequate procedural safeguards been available, we would have had, at the minimum, at least three months of time in which to study and review the proposed rate increases, the opportunity to have complete access to all essential data used in preparing the rate increase studies, and the right to cross-examine, or at least question, employees of the Bureau who participated in or supplied essential information for the studies.

PROBLEMS COMMON TO ALL BUREAU PROJECTS

The method used by the Bureau with regard to costs of replacements for facilities was improper. According to a memorandum dated August 2, 1972, from the Acting Assistant Secretary—Water and Power Resources to the Commissioner, Bureau of Reclamation, and to the administrators of the Bonneville Power Administration, the Southeastern Power Administration, the Southwestern Power Administration, and the Alaska Power Administration, certain criteria were established with regard to Average Rate and Repayment Studies. The memorandum stated:

"Effective not later than June 30, 1973, all power repayment analyses (Average Rate and Repayment Studies) prepared by the above Interior agencies for formulating, justifying, or obtaining approval of wholesale power rates will embody the following concepts and procedures:"

"Future replacement costs will be included in the payment studies by adding the estimated capital cost of replacements to the 'unpaid Federal investment' in the year each replacement is estimated to go into service, with an appropriate adjustment in the 'allowable unpaid investment'." (Emphasis supplied)

The criteria required by the memo with regard to treatment of replacement costs were not followed by the Bureau in the Average Rate of Repayment Studies for these rate increases. Instead of adding the capital cost of the replacements to the unpaid Federal capital investment, the Bureau treated cost of replacements for projected years as expenses, or deductions from revenues, in the year the costs of replacements were estimated to be incurred. The effect of such treatment on the Colorado River Storage Project is minimal for the present proposed rate increase. However, as discussed below, the effect on the Parker-Davis rate increase is substantial. When we confronted the Bureau with the August 2, 1972 memo, we were told that the criteria concerning replacement costs were not used because such criteria were to be "effective not later than June 30, 1973". However, we suspect (and have not been shown otherwise) that the Bureau officials working on the rate studies inadvertently overlooked the memo. Oddly enough, the Bonneville Power Administration has implemented the memo.

It is not proper, in any event, to base the need for an increase in power rates upon criteria which will be outmoded by the time the rate increase is effective. The Bureau virtually ignored our position and our inability to convince the Bureau on this point clearly illustrates the type of problem which adequate procedural safeguards would cure. The Bureau has not justified its treatment of replacements as expenses. The requirement for an adequate administrative record would most certainly require such justification.

The Bureau has not justified the imposition of a penalty for contract overruns. The Bureau has indicated that "the rate to be charged for energy and/or capacity over and above that amount Reclamation is committed to deliver will be billed at a rate five times the capacity and energy charges included in the new rate schedule". No data has been furnished by the Bureau to substantiate this seemingly punitive charge. It is conceivable that a USBR customer could incur such a penalty unintentionally. It would be more appropriate for the Bureau to base its charges on the actual costs of supplying such capacity and/or energy.

SPECIFIC COMMENTS REGARDING PARKER-DAVIS AND CRSP

Some of the specific comments by our consulting engineers relating to the Parker-Davis and CRSP projects are listed below. These comments illustrate the procedural and certain of the substantive inadequacies of the Bureau's processes.

PARKER-DAVIS PROJECT

(1) *The Bureau did not make available its hydrologic studies.*—Total energy available (energy sales) is estimated by the Bureau to result in an average of 1,195,700 MWH per year for the ensuing 40-year period. The estimates of energy availability are based on certain hydrologic studies, downstream water requirements in the early years of the projection, and upstream depletions in future years. Neither hydrologic study-period data nor upstream depletion data was included in the Bureau report.

If the available energy in the ensuing 40 years would be equal to the average availability in the historic 21-year period (the period in which both Parker and Davis Dams have been in operation) and such additional energy would be sold at the presently contemplated rate of 3.0 mills per kWh, revenues from total energy sales would be increased by approximately 5.8%. This would, of course, permit a smaller increase in the rate for firm commercial power. We did not have the basic hydrologic data nor sufficient time to gauge the reasonableness of the study results used.

(2) *Revenue projections by the Bureau do not reflect realistic pricing of non-firm energy.*—The projections of the Bureau as shown in the Average Rate and Repayment Study show the availability of energy in certain years in excess of irrigation pumping requirements and firm power sales. In their Repayment Study, the Bureau assumes that such excess non-firm energy will be sold at the rate of 3.0 mills/kWh. It is inconsistent to assume that non-firm energy will be purchased by the Bureau at the rate of 5.0 mills/kWh, while available non-firm energy is sold at 3.0 mills/kWh. Most certainly the current and future market value of non-firm energy is more than 3.0 mills/kWh. These two categories of energy have similar characteristics, and therefore the projections should reflect the same value for both categories of energy. A value of 5.0 mills/kWh does not appear unreasonable.

(3) *The transmission revenue projections of the Bureau are too conservative.*—“Other Revenue” as estimated by the Bureau are those revenues derived from transmission wheeling service facilities charges. They include revenues from short-term contracts, in the amount of \$106,000 per year, which are not projected beyond FY 1973. Without question, transmission capacity will continue to be available and required by customers beyond FY 1973, and therefore short-term other revenues beyond FY 1973 should be included. Additionally, details concerning construction of new transmission facilities and resultant revenues were not provided.

(4) *No details were provided concerning estimates of expenditures for replacements.*—The Bureau has indicated that the projected costs of replacements are based on studies by the Bureau in which actual replacement costs are related to the investment by various plant accounts. The Bureau has advised that the projected costs of replacements were determined by computer studies reflecting actual experienced replacement costs by plant accounts. The details of these studies have not been made available to date. It is noted, however, that the annual projected replacement costs in relation to plant investment by the Parker-Davis Project are considerably higher than projected for other USBR Projects. Following is a summary of the projected average annual costs of replacements as a percent of project investment for other Bureau Projects as taken from the Average Rate and Repayment Studies.

<i>Average annual costs of replacements as a percent of total project investment</i>	
	<i>Percent</i>
Parker-Davis Project.....	0.64
Colorado River Storage Project.....	.22
Central Valley Project.....	.19
Rio Grande Project.....	.47

The above summary indicates that a review should be made of the estimates of replacement costs to determine if they are overstated, with the result that additional funds might be available for repayment of investment, thus permitting a smaller rate increase.

(5) *The Bureau's study reflects an overstatement of interest expenses.*—The Bureau's repayment study upon which the proposed rate increase is based reflects an annual interest charge on the principal balance due at the beginning of the fiscal year. In actual practice, payments of principal are made monthly and therefore the interest expense should be reduced accordingly.

COLORADO RIVER STORAGE PROJECT

(1) *The Bureau did not make available its hydrologic studies.*—The Bureau's estimates of energy availability were based on certain hydrologic studies and upstream depletions in future years. Neither hydrologic study period data nor upstream depletion data was included in the Bureau's Report. It is noted that in the later years of the projection, the non-firm energy is approximately 10% of the firm energy sales. This appears to be a rather high percentage. We did not have the basic hydrologic data nor sufficient time to gauge the reasonableness of the study results used.

(2) *Revenue projection by the Bureau do not reflect realistic pricing of non-firm energy.*—The projections of the Bureau as shown in the Average Rate and Repayment Study shows the availability of energy in excess of project use and firm power sales presumably at 58.2% load factor. In their Repayment Study, the Bureau assumes that such excess non-firm energy will be sold at the rate of 3.0 mills/kwh. It is inconsistent to assume that non-firm energy will be purchased by the Bureau at the rate of 5.0 mills/kwh while available non-firm energy is sold at 3.0 mills/kwh. Most certainly the current and future market value of non-firm energy is more than 3.0 mills/kwh. These two categories of energy have similar characteristics and therefore the projections should reflect the same value for both categories of energy. A value of 5.0 mills/kwh does not appear unreasonable.

(3) *No details were submitted by the Bureau concerning increases in Operation and Maintenance (O & M) expenses.*—Operation and Maintenance Expenses are projected by the Bureau to increase each year for FY 1973, FY 1974, and FY 1975, presumably due to inflationary trends, then further increased in FY 1980 presumably due to the addition of new project facilities. The projection of O & M Expenses for the ensuing three years is based on budget amounts, which is in

accordance with present criteria. Further increases in O & M Expenses are projected in later years, presumably due to new facilities added to the project. However, complete data has not been submitted to gauge the reasonableness of the projected expenses.

(4) *The Bureau's rate for power will result in pay-out of the project in less than the allowed 50 years.*—The power rates proposed by the Bureau are estimated by the Bureau to result in complete payout of the commercial power portion of the project in FY 2008 and for the irrigation portion of the project in FY 2010. This projected payout period should be compared to the allowable payout period extending to FY 2029 for commercial power and FY 2017 for irrigation. The projected early payout of the project is the result of setting a power rate which will eliminate the temporary deficit in the payout of participating projects in FY 2045.

(5) *The Bureau's study reflects an overstatement of interest expenses.*—The Bureau's repayment study upon which the proposed rate increase is based reflects an annual interest charge on the principal balance due at the beginning of the fiscal year. In actual practice, payments of principal are made monthly and therefore the interest expense should be reduced accordingly.

CONCLUSIONS

The handling of the proposed rate increases for the Parker-Davis and Colorado River Storage Projects clearly demonstrates that the Bureau and the Department need a formalized administrative process which will provide the procedural safeguards lacking here. Statistics without justification handicap analysis. Review periods that terminate before data is available are useless. "Open hearings" without dialogue are a sham. Procedures must be established to prevent such capriciousness. It is only in this way that the administrative arbitrariness and abuse of discretion that we have outlined will be prevented.

In our view, we have clearly demonstrated that the Bureau is in no position to implement any rate increase for either the Parker-Davis or Colorado River Storage Projects. We insist that the Bureau and the Department reaffirm the legal requirement and Congressional policy of pricing Reclamation power as low as possible consistent with payout requirements. Further, we think that procedural safeguards, including full and fair participation by the preference customers and their engineers, would force the Bureau to admit:

1. That no increase in CRSP rates is presently justified;
2. That any increase in Parker-Davis rates, as shown by our consulting engineers' reports, should be limited to no more than 5.4% (and perhaps less) instead of the announced increased of 21.6%;
3. That increases, if any, should be delayed to allow time for proper procedures to be implemented, as well as to coordinate any increases with the fiscal year budgets of the customers; and
4. That the November 1, 1973 announcement of rate increases should be withdrawn.

Equitable and uniform rate-fixing procedures are a prerequisite to mutually acceptable power rate adjustments.

Respectfully submitted this 21st day of December, 1973.

THE ARIZONA POWER AUTHORITY,
By MARSHALL HUMPHREY, *Chairman*,
ELECTRICAL DISTRICTS 3, 4 AND 6,
PINAL COUNTY, ARIZONA,
By ROBERT S. LYNCH, *Attorney*.

In addition, the following entities have authorized the Arizona Power Authority to submit the foregoing in their behalf:

Buckeye Irrigation Co., P. O. Box 726, Buckeye, AZ 85326, O. L. Holly, President.

Central Arizona Irrigation & Drainage District, Pinal Co., AZ, P. O. Box 605, Eloy, AZ 85231, James L. Savage, President.

Cortaro-Marana Irrigation District, 13864 B North Sandario Rd., Marana, AZ 85238, Ludd M. Payne, President.

Harquahala Valley Power District, Buckeye, AZ, W. N. "Jack" Shawver, President, c/o James H. Green, Legal Counsel, 32 Luhrs Arcade, 11 W. Jefferson, Phoenix AZ 85003.

Electrical District No. 2, Pinal County, P. O. Box 66, Coolidge, AZ 85228, Arthur J. Faul, Chairman.

Electrical District No. 3, Pinal Co., P. O. Box 191, Maricopa, AZ 85239, W. A. Dunn, Chairman.

Electrical District No. 4, Pinal Co., P. O. Box 605, Eloy, AZ 85231, Wm. T. Elliott, Chairman.

Electrical District No. 5, Pinal Co., P. O. Box 8, Red Rock, AZ 85245, Norman Pretzer, Chairman.

Electrical District No. 6, Pinal Co., c/o Wm. D. Baker, Legal Counsel, Rawlins, Ellis, Burrus & Kiewit, 2300 Valley Center, Phoenix, AZ 85073, Raymond D. Schnepf, Chairman.

Electrical District No. 7, Maricopa Co., P. O. Box 642, Litchfield Park, AZ 85340, Percy Smith, Chairman.

Maricopa County Municipal Water Conservation District No. 1, P. O. Box 730, Peoria, AZ 85343, Scott L. Libby, President.

Maricopa-Stanfield Irrigation & Drainage District, P. O. Box 57, Maricopa, AZ 85239, John E. Smith, President.

New Magma Irrigation & Drainage District, R No. 1, P. O. Box 97, Queen Creek, AZ 85242, Joe C. Cooper, Chairman.

Roosevelt Irrigation District, P. O. Box 95, Buckeye, AZ 85326, Charles F. Younger, President.

San Tan Irrigation District, P. O. Box 8, Chandler Heights, AZ 85227, David W. Moss, President.

ATTACHMENT B

Mr. Chairman and Members of the Committee: My name is Gordon D. Jorgensen. I am a consulting engineer in the firm of R. W. Beck & Associates, Phoenix, Arizona.

As indicated by Mr. Humphrey, we were confronted by three basic problems in making our analyses of the proposed rate increases for both the Parker-Davis and Colorado River Storage Project Power Projects.

These problems were (1) the lack of opportunity to examine and analyze sufficient background data used by the Bureau of Reclamation; (2) the lack of time to analyze the information which was available and determined what additional information was necessary, and (3) the lack of proper hearings.

Our experience was the same as those working on the Central Valley project. While local Bureau officials did their utmost to supply us with *requested* information, they too were handicapped by the limiting time frame in which to secure the requested information requested and in the form desired. For example, regarding the Colorado River Storage Project, approximately 22 pages of questions were submitted to the Bureau on July 31, 1973. Answers to some of these questions were not received until August 27, a few days before our August 31 deadline for submitting the results of our studies to the Bureau. Other answers did not arrive until after the deadline date. Accordingly we did not have the opportunity to fully evaluate them nor gauge their effect upon the proposed rate increase. These answers, did however, rate additional questions.

In the case of the Parker-Davis Project we were further hampered in making our studies due to the fact that the detailed repayment studies were not made at the regional level but in Washington. Accordingly, the regional Parker-Davis staff were handicapped in answering specific questions relating to details of studies made.

In regard to both Projects, we were most disappointed that the pertinent detailed back-up information relating to the repayment studies had not been compiled in a form that would have allowed a more meaningful examination and review of the revenue and cost elements considered and their treatment.

Nevertheless while we were unable to complete a thorough investigation of all the areas pertinent to the proposed rate increase, certain basic studies were made relating to the important areas of repayment procedures and estimates of future revenues.

We find that the repayment procedures employed in the Parker-Davis and CRSP Project Power System Average Rate and Repayment Studies are not consistent with the Memorandum covering such procedures issued by the Acting Assistant Secretary—Water and Power Resources, Department of the Interior, dated August 2, 1972. Additionally, we believe that estimates of revenues pertaining to the sale of non-firm energy are low and not consistent with the market value of such energy.

While we have other areas of concern which are covered in our detailed statement to the Committee, we do want to touch on these two areas of concern with you today.

(1) *Revenue projections by the Bureau do not reflect realistic pricing of non-firm energy.*—The projections of the Bureau as shown in the Average Rate and Repayment Study shows the availability of energy in excess of project use and firm power sales. In their Repayment Study, the Bureau assumes that such excess non-firm energy will be sold at the rate of 3.0 mills/kWh. It is inconsistent to assume that non-firm energy will be purchased by the Bureau at the rate of 5.0 mills/kWh, which these studies show, while available non-firm energy is sold at 3.0 mills/kWh. Most certainly the current and future market value of non-firm energy is more than 3.0 mills/kWh. These two categories of energy have similar characteristics and therefore the projections should reflect the same value for both categories of energy. A value of 5 mills/kWh does not appear unreasonable.

(2) *The method used by the Bureau with regard to costs of replacements for facilities was improper.*—According to a memorandum dated August 2, 1972, from the Acting Assistant Secretary—Water and Power Resources, certain criteria were established with regard to Average Rate and Repayment Studies. The memorandum stated:

"Effective not later than June 30, 1973, all power repayment analyses (Average Rate and Repayment Studies) prepared by the above Interior agencies for formulating, justifying, or obtaining approval of wholesale power rates will embody the following concepts and procedures:

"Future replacement costs will be included in the payment studies by adding the estimated capital cost of replacements to the 'unpaid Federal investment' in the year each replacement is estimated to go into service, with an appropriate adjustment in the 'allowable unpaid investment'." (Emphasis supplied)

The criteria required by the memo with regard to treatment of replacement costs were not followed by the Bureau in the Average Rate of Repayment Studies for these rate increases. Instead of adding the capital cost of the replacements to the unpaid Federal capital investment, the Bureau treated cost of replacements for projected years as expenses, or deductions from revenues, in the year the costs of replacements were estimated to be incurred. The effect on the Parker-Davis rate increase is substantial. When we confronted the Bureau with the August 2, 1972 memo, we were told that the criteria concerning replacement costs were not used because such criteria were to be "effective not later than June 30, 1973". Oddly enough, the Bonneville Power Administration has implemented the memo.

In our opinion, it is not proper, in any event, to base the need for an increase in power rates upon criteria which will be outmoded by the time the rate increase is effective.

Yesterday, as a part of Mr. Horton's statement, we received a copy of a memo, dated October 28, 1973, from William F. Graham, Chief of Power addressed to the files covering Capitalization of Replacements.

In the memo he outlines future procedure to be followed in this matter. We respectfully but strongly take exception to these proposed procedures as being inconsistent with the intent of Acting Assistant Secretary's Wilson memo of August 2, 1972 on the subject. The proposed procedure does not follow the current procedures utilized by the Bonneville Power Administration which we feel are correct and proper.

Additionally, the memo specifies the possible use of a higher interest rate in making replacement computations. The memo in effect also indicates that the consultants were in error to accept the Bureau's projected replacements, as contained in their study on the basis that such replacements now should be indexed to reflect current costs beyond the normally three year projections. This is a major departure from prior Bureau practices and is one that warrants very careful review.

We have not had an opportunity to examine this memo in detail but do bring this to your attention since yesterday you requested the Department to recast the CVP repayment studies to reflect capitalizing of replacements. You may wish to specify which replacement procedure you wish followed—that specified in Mr. Graham's memo or the procedure followed by Bonneville which we feel is proper and correct.

We have made independent computer repayment studies reflecting our areas of disagreement and these results have been submitted to both the Bureau and this Committee. They indicate:

1. That no increase in CRSP rates is presently justified ;
 2. That any increase in Parker-Davis rates should be limited to no more than 5.4% (and perhaps less) instead of the announced increase of 21.6%.
- I am available for any additional questions you may have.

ATTACHMENT C

LEGAL STATEMENT IN SUPPORT OF PRESENTATION OF ARIZONA PREFERENCE CUSTOMERS CONCERNING NECESSITY FOR ADEQUATE PROCEDURES IN INCREASING RATES FOR BUREAU POWER

This statement deals with two of the legal questions germane to the statement submitted by the Arizona preference customers with regard to the rate increases proposed by the Department of the Interior for power generated at the Parker-Davis and Colorado River Storage Projects. These questions relate to (1) legal standards governing the fixing of rates for power generated at these projects and (2) the due process rights of these preference customers to a meaningful participation in Interior's rate fixing processes and procedures.

I. STANDARDS GOVERNING THE FIXING OF RATES

The Secretary of the Interior recognized several years ago that notwithstanding the provisions in Section 9(c) of the Reclamation Act of 1939, 43 U.S.C. 485(c),¹ the rates for power marketed from reclamation projects under the Reclamation Laws including the Parker-Davis and Colorado River Storage Projects are to be fixed in accordance with the mandate of Section 5 of the Flood Control Act of 1944, 16 U.S.C. 825 requiring that power from the projects involved be marketed:

"* * * in such manner as to encourage the most widespread use thereof at the lowest possible rate to consumers consistent with sound business principles."

As summarized in the annotations to Section 9(c) set out in Volume II of Federal Reclamation and Related Laws Annotated (at p. 649) which was prepared and published by the Department of the Interior in 1972, Secretary Udall took the position in a letter dated May 15, 1965 to Congressman Aspinall that although the criteria in Section 9(c) of the 1939 Reclamation Act pertaining to power rates "are stated in terms of the minimum charge for power, *they are also clearly intended to set the maximum charge.*"² The annotation quotes Secretary Udall as stating:

"The Government of United States markets power to serve the public interest, not to make a profit. We believe that the public interest is best served by marketing power at the lowest rate consistent with orderly repayment of all proper costs, and *we believe that is what Congress intended.*"

As further explained in the annotation, Secretary Udall took the position that the general provisions for marketing power in the 1939 Reclamation Act are to be read *in pari materia* with the power marketing provisions of other statutes dealing with specific projects or types of projects also administered by the Department of the Interior:

"The provisions relating to power marketing and power rates in section 9(c) of the Reclamation Project Act of 1939, section 5 of the Flood Control Act of 1944, and section 6 of the Bonneville Power Act are *in pari materia*, and each may be examined to shed light on the Congressional intent with respect to the others.

"Indeed, as a practical matter, as illustrated by the Bonneville Power Administration, because a single system may be used to market power from three different sources, the three statutes have to be read together and interpreted as establishing identical criteria for power rates. Consequently, the mandate of the Flood Control Act of 1944 to market power from Army projects 'in such manner as to encourage the most widespread use thereof at the lowest possible rates to consumers consistent with sound business principles,' applies also to power marketed from reclamation projects under reclamation law."

¹ Section 9(c) provides in pertinent part: "* * * Any sale of electric power or lease of power privileges, made by the Secretary in connection with the operation of any project or division of a project, shall be for such periods, not to exceed forty years, and at such rates as in his judgment will produce power revenues at least sufficient to cover an appropriate share of the annual operation and maintenance cost, interest on an appropriate share of the construction investment at not less than 3 per centum per annum, and such other fixed charges as the Secretary deems proper. * * *"

² Emphasis supplied throughout unless otherwise noted.

The Attorney General has similarly taken the position that the various statutes dealing with the marketing of power generated at Government facilities must be read *in pari materia*. See 41 Op. A. G. — (1955). This Opinion was issued by the Attorney General in response to the inquiry from the Secretary of the Interior whether under the preferences in Section 5 of the Flood Control Act of 1944, the Secretary could sell the power from the so-called Clark Hill project to non-preference customers since neither the Government nor the preference customers had access to facilities for transmitting the power. While Section 5 contained no provision allowing preference customers a reasonable period of time to arrange for the necessary transmission facilities, the Attorney General noted that:

"The preference provisions of other Federal power statutes [contain] 'reasonable time' requirements, such as the Boulder Canyon Project Act (43 U.S.C., sec. 617d(c)), the Tennessee Valley Authority Act (16 U.S.C., sec. 831k), and the Bonneville Project Act (16 U.S.C., sec. 832c(d)). For example, the last cited provisions are that in order 'to preserve the * * * preferential status of * * * public bodies and cooperatives' with respect to the disposition of electric energy, they shall be afforded 'reasonable time and opportunity to take any action necessary to authorize the issuance of bonds or to arrange other financing necessary to construct or acquire necessary and desirable electric distribution facilities * * *'. And, it will be noted that the Bonneville Project Act further protects the preferential status of public bodies and cooperatives by providing that an application of such an organization is not to be denied, or a competing application of a private corporation granted 'until after a reasonable time, to be determined by the Administrator (of the project), has been afforded such public body or cooperative' to issue or market securities needed to enable it to sell and distribute the electric energy proposed to be purchased (16 U.S.C., sec. 832c(c))."

Further, the Attorney General referred to the observation of one of his predecessors:

"In construing any statute the legislative intent, if it can be ascertained, must control; and in arriving at the legislative intent the entire statute, its form, its several parts, its purposes, its relation to other statutes, and the effects of construing it one way or another, must be considered' (39 Op. Att. Gen. 42, 44)."

Applying these criteria, the Attorney General held that Section 5 must be read to provide preference customers with a reasonable time to make appropriate arrangements for the receipt of this power:

"I cannot conceive, in the face of a plain mandate for preference to public bodies and cooperatives and the congressional concern, as evidenced in related statutes, for protection of their preferential status, that it is possible to say apropos of section 5 that the Congress intended a preference purchaser to demonstrate its present ability to take and distribute the power in order to avail itself of its statutory privilege. It is reasonable to attribute to the Congress that enacted section 5 the same solicitude for preference customers that had been recognized as necessary on other occasions. Congress knew that public bodies or cooperatives whom it wished to benefit would hardly be likely to own or control transmission lines reaching out to a power project, and hence it could not have intended them, in order to contract for the power, to be possessed with those facilities in advance."

This conclusion, the Attorney General went on to point out, was supported by the legislative history of Section 5, in that the Senate Committee, in dealing with an earlier version of what became of Section 5, had *inter alia*:

"* * * emphasized that the amendment was designed 'to attain the greatest benefit to the general public' and that specific reference was made to the Bonneville Act, which, as has been pointed out above, contained 'reasonable time' provisions with respect to preference purchasers."

This reasoning of the Attorney General is fully applicable to the problem we have here. In the first place, both the preference provision in Section 9(c), and the plain Congressional intent manifested in that and related statutes leave no doubt that Congress intended to assure that the benefits from federally generated power be made available first to such preference customers. In these circumstances, it is inconceivable that Congress intended in Section 9(c) to provide the Secretary with only a floor, rather than a ceiling, with respect to the rates to be charged for the power sold to such customers. To construe the provisions of Section 9(c) as prescribing only a floor with regard to rates charged preference customers would leave the Secretary free to include in the rates whatever profit

component he thought the market would bear. This would be contrary to the whole thrust and purpose of marketing of this power at the lowest possible rates to such preference customers.

In the second place, the legislative history of the 1939 Reclamation Act discloses that the Secretary, who had drafted the proposed legislation, described Section 9 (See H. Rep. No. 994, 76th Cong., 1st Sess., p. 5) as:

"* * * substantially in accordance with recent special acts of Congress relating to multiple-purpose projects constructed by the Bureau of Reclamation and would give effect to sound public policy. They recognize the widespread and multiple benefits derived from construction under the reclamation program and provide for an equitable and more widespread distribution of the costs of those benefits."

Among the "recent special acts of Congress relating to multi-purpose projects" thus referred to by the Secretary were (1) the Fort Peck Project Act of 1938, 16 U.S.C. 833, (2) the Bonneville Project Act of 1937, 16 U.S.C. 832, and (3) the Tennessee Valley Authority Act of 1933, 16 U.S.C. 831. Section 5 of the Fort Peck Act, 16 U.S.C. 833d, significantly provides *inter alia*, that the rates for the Fort Peck power "shall be fixed and established with a view to encouraging the widest possible diversified use of electric energy." And Section 6 of that Act 16 U.S.C. 833e, provides:

"It is the intent of Congress that rate schedules for the sale of electric energy which is or may be generated at the Fort Peck project in excess of the amount required for operating the dam and appurtenant works at said project shall be determined with due regard to and predicated upon the fact that such electric energy is developed from water power created as an incident to the construction of the dam in the Missouri River at the Fort Peck project for the purposes set forth in section 833 of this title. Rate schedules shall be drawn having regard to the recovery (upon the basis of the application of such rate schedules to the capacity of the electric facilities of Fort Peck project) of the cost of producing and transmitting such electric energy, including the amortization of the capital investment over a reasonable period of years. * * *"

Similarly, Section 6 of the Bonneville Power Act, 1 U.S.C. 832e prescribes that the rates for power generated at the project

"* * * shall be fixed and established with a view to encouraging the widest possible diversified use of electric energy. The said rate schedules may provide for uniform rates or rates uniform throughout prescribed transmission areas in order to extend the benefits of an integrated transmission system and encourage the equitable distribution of the electric energy developed at the Bonneville project."

And Section 7 of the Bonneville Act, 16 U.S.C. 832f provides

"It is the intent of Congress that rate schedules for the sale of electric energy which is or may be generated at the Bonneville project in excess of the amount required for operating dam, locks, and appurtenant works at said project shall be determined with due regard to and predicated upon the fact that such electric energy is developed from water power created as an incident to the construction of the dam in the Columbia River at the Bonneville project for the purposes set forth in section 832 of this title. Rate schedules shall be drawn having regard to the recovery (upon the basis of the application of such rate schedules to the capacity of the electric facilities of Bonneville project) of the cost of producing and transmitting such electric energy, including the amortization of the capital investment over a reasonable period of years. * * *"

In the same vein, Section 10, the Tennessee Valley Authority Act, 16 U.S.C. 831i provides:

"The Board is empowered and authorized to sell the surplus power not used in its operations, and for operation of locks and other works generated by it, to States, counties, municipalities, corporations, partnerships, or individuals, according to the policies hereinafter set forth; and to carry out said authority, the Board is authorized to enter into contracts for such sale for a term not exceeding twenty years, and in the sale of such current by the Board it shall give preference to States, municipalities, and cooperative organizations of citizens or farmers, not organized or doing business for profit, but primarily for the purpose of supplying electricity to its own citizens or member: * * *"

And Section 11 of that Act, 16 U.S.C. 831j, goes on to state:

"It is declared to be the policy of the Government so far as practical to distribute and sell the surplus power generated at Muscle Shoals equitably among the States, counties, and municipalities within transmission distance. This policy is further declared to be that the projects herein provided for shall be

considered primarily as for the benefit of the people of the section as a whole and particularly the domestic and rural customers to whom the power can economically be made available, and accordingly that sale to and use by industry shall be a secondary purpose, to be utilized principally to secure a sufficiently high load factor and revenue returns which will permit domestic and rural use at the lowest possible rates and in such manner as to encourage increased domestic and rural use of electricity."

The foregoing excerpts from the provisions of some of statutes dealing with the marketing of federally generated power—all enacted shortly before the 1939 Reclamation Act—are, of course, in addition to Section 5 of the Flood Control Act of 1944, 16 U.S.C. 825s which provides in pertinent part:

Electric power and energy generated at reservoir projects under the control of the Department of the Army and in the opinion of the Secretary of the Army not required in the operation of such projects shall be delivered to the Secretary of the Interior, who shall transmit and dispose of such power and energy in such manner as to encourage the most widespread use thereof at the lowest possible rates to consumers consistent with sound business principles, * * * Rate schedules shall be drawn having regard to the recovery (upon the basis of the application of such rate schedules to the capacity of the electric facilities of the projects) of the cost of producing and transmitting such electric energy, including the amortization of the capital investment allocated to power over a reasonable period of years."

Thus, when Section 9(c) is read in light of its purposes and those of the related statutes, it is obvious, we believe, that as stated in Secretary Udall's letter to Congressman Aspinall, Congress intended for the federally generated power marketed under Section 9(c) of the 1939 Reclamation Act to be marketed "not to make a profit" but rather "at the lowest rate consistent with orderly repayment of all proper costs."

II. PREFERENCE CUSTOMERS' RIGHT TO A MEANINGFUL PARTICIPATION IN THE RATEMAKING PROCESS

Whatever may have been the law in this regard even 5 short years ago, the clear import of the developments currently taking place in this area leave no doubt that the preference customers have a due process right in a meaningful participation in the Secretary's rate making process and procedures.

It is clear, under the recent decisions in this area, not only that the due process protection provided extends to statutory rights, as well as constitutional rights, but that it extends broadly to "any significantly property interest". *Boddie v. Connecticut*, 401 U.S. at 379, including statutory entitlements. See *Bell v. Barson*, 402 U.S. at 539; *Goldberg v. Kelly*, 379 U.S. at 262; *Fuentes v. Shevin*, 407 U.S. 67, 86 (1972). The purpose and purport of the power marketing provisions of Section 9(c) of the Reclamation Act of 1939, and the cognate statutes discussed earlier showing that the preference customers are intended to be benefited in the sale of reclamation power clearly demonstrates that the preference customers have at least a statutory interest and entitlement embraced within the protection of due process under these recent cases.

As stated in *Goldberg v. Kelly*, 397 U.S. 254, 267 (1970), such due process rights include the "opportunity to be heard" *Granness v. Orlean*, 234 U.S. 385, 394 (1914), and the hearing thus to be provided is to be "at a meaningful time and in a meaningful manner" *Armstrong v. Manzo*, 380 U.S. 545, 532 (1965). Together with the notice also required, such hearing must, in addition, be "appropriate to the nature of the case". Further, such due process requirements apply to executive and administrative as well as judicial determinations (see e.g., 210 U.S. 373, 486 (1908); *Slochow v. Board of Higher Education*, 350 U.S. 551 (1956), an extension which follows from recognition that the constitutional right to be heard is a basic aspect of the duty of government to follow a fair process of decision making * * *) *Fuentes v. Shevin*, 407 U.S. 67, 80 (1972).

The principles thus enunciated by these several recent Supreme Court decisions have been applied very recently by the Court of Appeals for the District of Columbia Circuit in *Thompson v. Washington, D.C. Cir. No. 71-2049* (decided December 10, 1973). Since the situation there was closely analogous to the present one, the Court's decision in that case, we believe, eliminates any possible doubt that the preference customers purchasing Bureau generated power are entitled to due process with regard to the procedures followed by the Bureau in determining the rates for that power.

Thompson v. Washington involved the question as to the due process rights of residents in low-income housing to participate in the rent increase schedules promulgated by the National Capitol Housing (NCHA). Pointing out that one of the prime purposes of the program there involved was that rents should be substantially lower than those obtainable in the private market, the Court held that the tenants were the intended beneficiaries of that program and hence were entitled to participate in the rent-fixing process *even though the Housing Act was silent on the question* (slip opinion p. 13):

"In providing for controlled rents, Congress plainly intended to create a benefit in favor of tenants to enjoy subsidized housing at less than market price. The Housing Act is silent on the question whether Congress intended to provide the tenant beneficiaries with procedural rights to assert further their interests during the process of rent-fixing by LHAs. We uphold the tenants' claim of a right to be heard, * * * finding such rights in the statute, albeit by implication rather than express provision."³

See also, *Marshall v. Lynn*, D.C. Cir. No. 71-1786 (also decided December 10, 1973) (slip opinion p. 8):

"From our reading of the legislative history, we have no doubt that the 1961 program of below-market interest rate subsidies was intended to benefit low- and moderate-income tenants. Therefore we follow our analysis in *Thompson v. Washington*, decided today, and hold that tenants in housing financed with Federal subsidy in the form of below-market interest rate loans have a statutory right to be heard before their rents are increased. (footnote omitted)"

Marshall v. Lynn involved housing constructed pursuant to Section 221(d)(3) of the National Housing Act with both FHA mortgage insurance and below-market-interest-rate loans. The Court there similarly commented (slip opinion p. 3):

"Although the statute governing § 221(d)(3) housing does not provide on its face for a hearing, this housing is 'designed to assist private industry in providing housing for low and moderate income families and displaced families.' 12 U.S.C. § 17151(a). When § 221 was enacted in 1954, Congress plainly contemplated that low- and moderate-income tenants were to be the principal beneficiaries of this program."

Since, as shown earlier, Congress also intended to provide preference customers the benefits of low-cost generation, it is obvious that the preference customers likewise have due process rights to participate in the process of rate making by the Department of the Interior. This is emphasized by the Court's further express rulings in *Thompson v. Washington* (1) that procedural due process if "fully applicable to any executive or administrative forum entrusted with the determination of significant rights" (slip opinion, pp. 15-16) and (2) that "the zone of interests protected by due process procedural requirements includes interests created by statute in favor of a generally-defined class" (slip opinion, p. 17).

Having thus determined that the tenants were entitled to participation in the rate making process, the Court in *Thompson v. Washington* turned to the "fleshing out of these requirements" (slip opinion, p. 25). In this connection, the Court first ruled that the tenants should be allowed to participate in the formulation of recommendations at the local, *i.e.*, NCHA, level (slip opinion, p. 26):

"The local housing authority is familiar with the details of project operations. Its staff is likely to have more contact with tenants and their representatives than that of HUD. Thus the local housing authority is the more appropriate initial forum for the tenant. *Allowing the tenants to present their views first to the local housing authority gives them an opportunity to influence the preparation of proposals at an early stage, before important issues have been foreclosed and objection has become a futile gesture.*"⁴

* * * * *

Here, of course, the preference customers have not been permitted to participate in the Department's rate making process at all. Indeed, preference customers were not even given any access to the rate adjustments themselves until after all the basic decisions with regard thereto had been made within the Department and as a result, the preference customers were confronted with a *fait accompli*. Patently, any hearing held by the Department thereafter does not satisfy the requirements of due process, *Cf. Ashbacker Radio Corp., v. F.C.C.*, 327 U.S. 326 (1945).

³In so holding, the Court rejected out of hand claims of sovereign immunity, lack of jurisdiction in the courts and lack of standing. See slip opinion pp. 9-10.

⁴See *Goldberg v. Kelly*, *supra*, in which the Court emphasized that presentation of opposing views at an early stage is particularly important."

Since "the number of tenants potentially involved is quite large," the Court in *Thompson v. Washington* then went on to note "we must be careful to shape procedures to protect the tenants interests that avoid this becoming unduly burdensome" (slip opinion, pp. 25-26). Accordingly, in deference to the "need to impose some limits to keep the proceeding manageable", the Court indicated that the tenants should be afforded at least "a hearing of the type prescribed by the Administrative Procedure Act for rule-making proceedings: an opportunity to make written presentations" (slip opinion, p. 29). In so holding, the Court, of course, had in mind the requirements noted earlier herein that the opportunity to be heard must be in a meaningful manner and appropriate to the nature of the case. In other words, such a holding must be more than the "open hearings" had in the instant proceedings which were held after the Bureau had already made its decision and where the Bureau's presentation—limited as they were to material contained in the brochures—and those of the preference customers passed each other like ships in the night.

While the Court in *Thompson v. Washington* thus accommodated the scope of the hearing out of deference to the large number of potential participants, the Court nevertheless recognized that such a hearing would not be appropriate in all circumstances. Instead, in accord with the established principles that the requirements of due process vary with the needs of the situation involved, the Court went on expressly to point out that there may be occasions where considerations of fairness require in addition, not only the right to make "oral submissions even in a legislative type proceeding" (citing, e.g., *American Airlines v. CAB*, 359 F.2d 624, 631-632 (1966), cert. denied 385 U.S. 842 (1966); *Walter Holm & Co. v. Hardin*, 449 F.2d 1009 (1971)) but also the right of cross-examination by the interested parties (citing *International Harvester Co. v. Ruckelshaus*, 478 F.2d 615 (1972)). (slip opinion, pp. 28-29).

That the issues here involved with regard to the Bureau's proposed rate increases call for both the right to make oral submissions and to cross-examine the presentations of others is clear from the decisions thus cited by the Court of Appeals. For example, take the *International Harvester Co.* case, where the Court of Appeals remanded for further proceedings an EPA denial of a one-year suspension of the 1975 emission standards prescribed under the Clean Air Act. While the statute there provided for a hearing on requests for suspension, it also required that a decision therefor be issued within 60 days after receipt of the request. Since the hearing had in that case consumed two weeks even though counsel had been limited to submitting written questions to the Hearing Panel to be asked the witnesses, the Court declined to hold it error not to permit "broad cross-examination" in light of the time restraints on decisions. In so holding, however, the Court distinguished between a broad right of cross-examination, on the one hand, and "cross examination of live witnesses on a subject of critical importance which could not be adequately ventilated under the general procedures". While it rejected the "broad right", it nevertheless reiterated that (478 F.2d at 631):

"* * * a right of cross-examination, consistent with time limitations, might well extend to particular cases of need, on critical points where the general procedure provided inadequate to probe 'soft' and sensitive subjects and witnesses."

Chief Judge Bazelon concurring, thought that despite the time restraints a "broad" right of cross-examination should have been provided (*Id.* at p. 652):

"The majority's approach permits the parties to challenge the Administrator's methodology only through the vehicle of judicial review. I do not think this is an adequate substitute for confrontation prior to the decision. I reach this position not only out of concern for fairness to the parties ('... for if a party first learns of noticed facts through the final report ... the burden of upsetting a decision announced as final is a heavy one.' (footnote omitted)) but also out of awareness of the limits of our competence for the task. The petitioners' challenges to the decision force the court to deal with technical intricacies that are beyond our ken. (footnote omitted) These complex questions should be resolved in the crucible of debate through the clash of informed but opposing scientific and technological viewpoints.

* * * [I]n cases of great technological complexity, the best way for courts to guard against unreasonable or erroneous administrative decisions is not for the judges themselves to scrutinize the technical merits of each decision. Rather, it is to establish a decision-making process which assures a reasoned decision that can be held up to the scrutiny of the scientific community and the public (footnote omitted) '[T]he best test of truth is the power of the thought to get itself

accepted in the competition of the market.' (footnote omitted). If we were to require procedures in this case that open the Administrator's decision to challenge and force him to respond, we could rely on an informed 'market' rather than on our own groping in the dark to test the validity of that decision."

Walter Holm & Co. v. Hardin, *supra*, involved a suit by importers questioning the procedure followed by the Secretary of Agriculture in issuing orders prescribing the minimum size of tomatoes to be imported and marketed in the United States. The Court there held that this issue was to be resolved not on the basis of whether the "order" involved came within the APA's definition of "order" but rather on the basis of the kinds of questions which are raised and required resolution (449 F.2d at 1015):

"This is not an area that may rightly be approached in terms of absolute rigidity of requirement. It is not the law that all orders must be preceded by oral hearings when hearing is sought only on matters not involving material issues of fact. (citations omitted) And it is not the case that all administrative actions legitimately denominated regulations are *ipso facto* freed from any need for oral hearings. (citations omitted)

"* * * The kind of procedure required must take into account the kind of questions involved * * *"

Further noting that in light of the problems there, "a procedure not requiring an opportunity for oral presentation in crucial matters, and not requiring evidence in the record, is a seed bed for the weed of industry domination" (*Id.* at 1016), the Court concluded that (*Ibid.*):

"* * * the kind of underlying issue * * * and the issue of fairness * * * combine to require that on those matters where importers make a not insubstantial claim that an effective showing requires oral presentation to Department officials, that this right is available to them. *American Airlines* indicates that the oral hearing may be legislative in type, although fairness may require an opportunity for cross-examination on the crucial issues. This requirement of hearing is not shackled by rigidities of procedure that may stultify the regulatory program. *What counts is the reality of an opportunity to submit an effective presentation, to assure that the Secretary and his assistants will take a hard look at the problems in light of those submissions* * * *"

Taking into account the complexity of the issues here, coupled with the lack of any restraints as to the timing upon the imposition of the rate adjustment, if any, it is clear, we submit, that the only appropriate procedure for determining the propriety of such a rate adjustment is through oral presentation and cross-examination at hearings. Only in this way can the "soft" and sensitive subjects be probed; only in this way can there be any assurance that those making the decisions are in fact taking the necessary hard look at all sides of the case; and only in this way can there be any assurance that the decision reached is a reasoned one.

In addition to its claim that no hearings are required by law, a matter dealt with at length earlier in this memorandum, Interior has based its failure to accord the preference customers a greater participation in the rate-making process on the ground that it would involve undue delay and expense. One answer is that there is no particular time frame prescribed for the imposition of a rate adjustment, and thus there is no justification for even a partial denial of due process to the preference customers, let alone a complete denial thereof. Indeed, even where tight time limits were involved, the courts, while adjusting thereto, have nevertheless insisted upon an appropriate measure of due process. Here, where there is, in fact, no prescribed time restraint and where, indeed, the nature of the rate making process encompassing the entire repayment period readily permits of delays in making rate adjustments without in any way impairing the totality of the pay back obligation, avoidance of delay is no excuse for failure to provide all due process called for by the complexity of the issues and their importance to, and impact upon, the preference customers.

Another answer is provided by *Bell v. Barson*, 402 U.S. 535, 540-541 (1971) :
 "While the problem of additional expense must be kept in mind, it does not justify denying a hearing meeting the ordinary standards of due process' *Goldberg v. Kelly*, 397 U.S. at 261, quoting *Kelly v. Wyman*, 294 F. Supp. 893, 901 (SDNY, 1968)."

See also *Wong Yang Sung v. McGrath*, 339 U.S. 33, 46-47 (1950).

Respectfully submitted,

COUNSEL FOR ARIZONA POWER AUTHORITY,

MELVIN RICHTER,

Litman, Richter, Wright & Talisman.

COUNSEL FOR ELECTRICAL DISTRICTS 3, 4 & 6

JAMES P. BARTLETT,

Jones, Hunter, Bartlett & Lerch.

ROBERT S. LYNCH,

Rawlins, Ellis, Burrus & Kiewit.

PINAL COUNTY, ARIZONA

January 17, 1974.

Mr. RICHTER. As I said, Mr. Chairman, this statement I read was just a summary statement. I was advised that I should try to keep the statement down to 5 minutes. I have included in that material submitted, fuller statements which details some of our experiences with the Bureau as far as November 1973 rate increases are concerned and it goes into some of the materials developed at the hearings before the Subcommittee on Conservation and Natural Resources with regard to the commitments or noncommitments by the Interior Department as to what they would do in the future.

As I said in my summary statement, they have made no commitment whatsoever as to what hearings they would provide for any future rate increases and their position is, as stated by the Solicitor's Office that no hearings whatsoever are required. We think there should be legislation enacted by Congress to make it clear that hearings are required and we think that that legislation should define the nature of those hearings so there will be no question about it.

Mr. JOHNSON. The gentleman from New Mexico, Mr. Runnels.

Mr. RUNNELS. Thank you, Mr. Chairman.

Mr. Richter, is it your belief of your people that you represent that there was not a true and full hearing by the public?

Mr. RICHTER. I think I am strongly of the belief that there was no hearing whatsoever. There was an informal meeting held with respect to each of the two rate increases that affect my people. One was a hearing on July 12 related—at Salt Lake City related to the Colorado River Storage rate increases and the other was a hearing on July 10 relating to rate increases for the Parker-Davis power. Now, both of those "hearings," and I use the word hearings in quotations, I would like to make it clear—neither of those hearings lasted more than an hour or two. One day was set aside for each of the hearings, and the hearings—I would call them meetings rather than hearings, and the meeting at Boulder took less than an hour. The meeting at Salt Lake City took no more than 2 hours. No questions were permitted.

Mr. RUNNELS. No questions?

Mr. RICHTER. No questions of the Bureau personnel were permitted whatsoever. All it consisted of was a presentation in each instance, a presentation by the Bureau of some summary material which they had already distributed as part of the brochures which in and of itself was just generalizations on the one hand. On the other hand there was written presentations presented by the interested parties which basically consisted of a complaint that they hadn't been able to analyze the Bureau rate increase sufficiently because of the time lag. The hearings were held on, as I say, in early July. The announcement wasn't made until late in May or early June and the Bureau wasn't volunteering any materials. You would have to ask them for materials before they would furnish it to you. As a matter of fact, they recognized the inadequacy of that hearing by permitting us to file another report by August 31 and even then we didn't have enough time. We had to ask the right questions to get the right information.

Mr. RUNNELS. Then under section 6 of the proposed bill it provides that the Secretary of the Interior publish proposed regulations and provide public hearings and written decisions, and I have been led to believe that under section 9(c) of the Reclamation Project Act of 1939 such public hearings and written decisions on the records are not now required for rate schedules issued by the Secretary for Federal power marketed pursuant to section 5. Do you agree that we need to have a set of guidelines and rules and regulations?

Mr. RICHTER. One-hundred percent, Congressman Runnels. There is no procedure now. There are no guidelines. As I say, the Interior takes the position that no hearings are required at all.

As I say, I think the law is evolving in the District of Columbia that there would be hearings required, but that will take a long while and it isn't clear yet. That is why it is our recommendation that the phrase in section 6 that adequate public hearing be not only included in the bill, but the concept should be included but not that language. The reason why that, an adequate public hearing doesn't mean much, as the hearings before the Subcommittee on Conservation and Natural Resources make clear. There is a great variety of hearings. The Assistant Secretary of the Interior took the position that adequate hearings were accorded to us on the late rate increases. So if you just leave the phrase "adequate public hearings" you are leaving a Pandora's box left to be resolved by the courts. It seems to me at this juncture if you are considering legislation the legislation should make it clear that full hearings are required and what those hearings should be.

Mr. RUNNELS. I have no questions.

Mr. Chairman. Does the committee have copies of the hearings that these people held in Salt Lake City and so forth available for the committee?

Mr. JOHNSON. To the best of my knowledge, we have not received copies of those hearings. The other committee that held hearings on this matter received copies of the hearings that were held in various places, whether related to the rate increase or not, I don't know. We have not received them.

Mr. RICHTER. If I may interject, I would be glad to furnish them. We have copies. As a matter of fact, in connection with the hearings on Conservation and Natural Resources, we compiled what we would

call the record which was made before the Interior Department with regard to both the Parker-Davis and the Colorado River storage project and included in that record is the transcript of the hearings in both of those cases.

Mr. RUNNELS. Mr. Chairman, may I request that Mr. Richter furnish for the file these hearings so we might look them over and see what was said?

Mr. JOHNSON. I think, if the gentleman would yield, that as long as we are getting those for the people that he represents that we should have a copy of the transcripts for all of the hearings.

Mr. RICHTER. We only have the two.

Mr. JOHNSON. If you will give us those two.

Mr. RICHTER. How many copies would you like?

Mr. JOHNSON. Just one copy.

Mr. RICHTER. One copy. I will be glad to.

Mr. JOHNSON. Do I hear objections to the request that we receive, for the files of the subcommittee, a copy of the transcript for all of the hearings that were held in connection with the rate increases?

Is there objection?

Hearing none, so ordered.

If you will furnish yours that will be fine. That covers two of the meetings.

Mr. RICHTER. I will be glad to furnish them, send them over today or later tomorrow.

Mr. JOHNSON. The gentleman from Nevada, Mr. Towell.

Mr. TOWELL. Mr. Chairman, I wouldn't have any questions of the witness. I would have one comment, though.

His problem seems to be very much like the other problems we have with Government agencies out in the field, that there either is no hearing or the hearing is brief and apparently not listened to and the public interest or public input is quickly put aside and business continues as usual. So I have been following your testimony with great interest, and I am I think like the rest of us deeply concerned that this continues to happen, not only your problem, but with other agencies out in the field.

That would be my only comment right now. I would look forward to seeing what was said at that meeting.

Mr. JOHNSON. The gentleman from California, Mr. Ketchum.

Mr. KETCHUM. No questions, Mr. Chairman.

Mr. JOHNSON. Mr. Casey, do you have a question of the witness?

Mr. CASEY. Thank you, Mr. Chairman.

Mr. Richter, your testimony went almost in its entirety to the thrust of section 6.

Mr. RICHTER. Right.

Mr. CASEY. Now, there are other substantive sections of this bill, namely, sections 2, 3, 4, 5, which deal with recommended curative procedures as they would relate to the rate increases that have already been promulgated.

Mr. RICHTER. Right.

Mr. CASEY. Do you have handy that you could give for our record the approximate magnitude of the rate increases that were promulgated for the two power systems that you represent?

Mr. RICHTER. Parker-Davis, I think I can give you a percentage figure. For Parker-Davis the increase is about 20 percent, and for Colorado River storage it is in the order of 2 or 3 percent. However, the Parker-Davis, as you know, is relatively small, 200 megawatts, Colorado storage 300 megawatts.

Mr. CASEY. Now, the Parker-Davis system has been marketing power for how long, sir; approximately?

Mr. RICHTER. Oh, about 20, 30 years now.

Mr. CASEY. And there have been no previous rate increases?

Mr. RICHTER. None that I know of.

Mr. CASEY. Until one was promulgated at about 20 percent?

Mr. RICHTER. Right.

Mr. CASEY. Now, the storage project—

Mr. RICHTER. In operation since about 1965. It began selling power at that time.

Mr. CASEY. It is not even in complete operation yet?

Mr. RICHTER. That is right. It commenced selling power in 1965.

Mr. CASEY. And the rates would have been initially established as of that date?

Mr. RICHTER. Right.

Mr. CASEY. And there had been no intervening rate increases until November 1973?

Mr. RICHTER. Right.

Mr. CASEY. At which time a rate increase of about—

Mr. RICHTER. Two or three percent.

Mr. CASEY. Was promulgated?

Mr. RICHTER. Let me go back a minute, if I may. On the Parker-Davis it is on the order of 20 percent. We are not saying no rate increase is appropriate. We are saying the order of magnitude is too high. What we want to do is to be given an opportunity to look into the authority and work out on the record what the rate increase should be.

Mr. CASEY. Then you do endorse the sections of H.R. 14221 that deal with the review of the rates that have been promulgated and the provision for perhaps a set-aside or a reduction or an increase or whatever might come from that procedure?

Mr. RICHTER. I didn't mean to leave the impression we did not. The only reason I spoke in relation to section 6 is I think those two clarifying amendments should be made. As far as section 1 through 5 we have no problem with and we are supporting it.

Mr. CASEY. That is all I have.

Mr. RUNNELS. Mr. Chairman.

Mr. JOHNSON. The gentleman from New Mexico.

Mr. RUNNELS. So that I will understand thoroughly, you are not objecting to an increase, all you are doing is objecting to the method by which it was derived at and to make sure the 26 percent or whatever the increase was is a proper increase because going back to the original bill and under which it falls, it is not to make a profit, but rather at the lowest rate consistent with orderly repayment of all the property costs; is that what we are trying to get at?

Mr. RICHTER. We are trying to make sure the rate increase complies with the statutory standards, not as viewed necessarily solely by In-

terior, but viewed objectively, if you will, by an objective agency. We think from the limited inquiry and analysis that our people are able to make of these increases indicates that the Parker-Davis increase was excessive by about 15 or 20 percent. We think no more than 5 percent increase and maybe less would be appropriate. The reason why I say no more than 5 and maybe less is because we are unable to complete our study of it so we don't know exactly how much is appropriate. But we know at least as far as Parker-Davis is concerned from our point of view it is excessive. At least from our point of view of the Colorado River storage project is that none is appropriate at this time.

Mr. RUNNELS. Why did we say they were increasing it by 20-odd percent?

Mr. RICHTER. They developed what they called a payout study which covers the whole remaining term of the life of the project, and based on numerous assumptions which they have to make, which go for 30, 40 years into the future which are necessarily highly conjectural, and they come up with a rate increase by 20 percent in order to make sure that they have enough revenues by the end of the period, not only to cover each year as well as the total payout period, so that I think in our case they would end up with a substantial surplus on their own projections at this point, but it would make sure that they had incurred no deficits at any time during the period. They make a number of invalid assumptions. For instance, I understand they understated expected revenues. They understated the level of how they can sell surplus power. They use the wrong hydrology—there are questions about the hydrology they use. The question is by making a projection of 50 years in advance and trying to cover every year to make sure you don't have any deficit during that period you are going to get into a heck of a lot of assumptions which there could be substantial questions about.

As I understand in the case of one of the other projects we had ended up with surplus of over \$600 million.

Mr. RUNNELS. Thank you, Mr. Chairman.

Mr. JOHNSON. Any further questions of the witness?

If not, we want to thank you for appearing here, Mr. Richter, and giving us the benefit of your statement and your oral statement and the attachments. If you will furnish us a copy of the two hearings we will appreciate it.

Mr. RICHTER. I will be glad to.

Mr. JOHNSON. Our next witness is Mr. Timothy Dillon, attorney, representing the Sacramento Municipal Utility District.

Mr. DILLON.

STATEMENT OF TIMOTHY DILLON, ATTORNEY, REPRESENTING THE SACRAMENTO MUNICIPAL UTILITY DISTRICT

Mr. DILLON. I have a prepared statement. I have a brief summary of it and I will present the summary.

Mr. JOHNSON. Your complete statement will appear in the record as if read in full, and you may summarize.

[The above referred to statement follows:]

STATEMENT OF TIMOTHY V. A. DILLON, IN BEHALF OF SACRAMENTO MUNICIPAL
UTILITY DISTRICT

I am pleased to appear before the Subcommittee this morning to urge enactment of H. R. 14421, a bill to provide for the review of increases promulgated by the Secretary of the Interior on November 1, 1973, in rates for electric power sold at five Bureau of Reclamation projects, including the Central Valley Project, California.

The Sacramento Municipal Utility District is a publicly owned electric utility serving over a quarter-million customers spread over a 650 square mile service area which includes California's capitol city of Sacramento.

SMUD sold over 4 billion kilowatt hours of electricity last year. This power was derived from various sources including generation of over 600,000 kilowatts at its hydroelectric project on the South Fork of the American River, purchases from the Pacific Gas and Electric Company and the Pacific Northwest and from the purchase of 360,000 kilowatts of power developed at the Central Valley Project pursuant to a long term contract with the United States.

SMUD believes that the new rate schedule promulgated by the Secretary of the Interior violates the terms of its contract with the United States. Under the new schedule our customers will have to pay an additional \$1.7 annually for power purchased from the Central Valley Project.

Little would be served by a recitation of the melange of dubious legal actions, denials of elementary procedural due process, and other inadequacies on which the Secretary's promulgation was based. The letter dated January 28, 1974, from the Chairman of this Subcommittee, Congressman Johnson, to the Secretary traces the steps leading to the latter's promulgation, and identifies the points at issue. The record of the hearing last January 22 and 23 before the Subcommittee on Conservation and Natural resources of the House Committee on Government Operations documents the deficiencies of the proceedings on which the rate increase was grounded. Also, the first section of H.R. 14221 clearly and concisely sets forth the justification for a review of the new rates.

H.R. 14221 would direct the Secretary to, within 30 days of its enactment, transmit to the Federal Power Commission the rate schedule promulgated by him at each of the five projects, together with all relevant back up material. The FPC would then be required, with the assistance of the Comptroller General—

"to promptly conduct a thorough review of the promulgated schedules and the criteria and procedures followed by the Secretary in developing such schedules, for the purpose of determining their reasonableness and adequacy and their consistency with applicable requirements of law and regulations."

The bill further requires that upon completion of such review the FPC must issue a declaration as to each project, approving such schedules or recommending their modification. It is to be noted that H.R. 14221 requires that (1) each decision be based on the record after opportunity for public hearing as provided in the Federal Power Act, and (2) that "All materials, documents, and other written matter related to the Commission's decision shall be available to the public." It is difficult to resist the inclination to make an invidious comparison between the procedures followed by the Secretary since the first public announcement in January, 1973, of his intention to increase power rates, and those mandated under the provisions of H.R. 14221.

In Part II of the Federal Power Act of 1920 Congress conferred upon the FPC comprehensive powers over the regulation of electric utilities engaged in interstate commerce, including, in Section 205, control over their rates and charges. Section 6 of the Act of August 20, 1937, 16 U.S.C.A. 822e, which authorized the Bonneville Project, requires FPC "confirmation and approval" of rates and charges for electric energy produced at that project. In the discharge of these responsibilities the Commission has developed the expertise necessary to conduct a thorough and fair rate study.

Before closing I would respectfully suggest that Section 4 of the bill be amended by the addition to it of the following italicized words:

"Sec. 4. The rate schedules promulgated by the Secretary on November 1, 1973, for each of the five projects referred to in this Act shall continue in effect *as to all customers for which such rates were validly promulgated on that date pending review thereof pursuant to this act.* . . ."

SMUD is weighing a court challenge of the validity of the rate schedule promulgated on November 1, 1973, by the Secretary. Inclusion of the suggested wording would obviate any possibility that Section 4 would be construed as interfering with SMUD's right to litigate that issue.

SMUD believes that H.R. 14221 should be enacted at the earliest possible date.

Mr. DILLON. Mr. Chairman, if I may, I would like to briefly summarize the main points of my statement in behalf of the Sacramento Municipal Utility District (SMUD) in support of the adoption of H.R. 14221. It is our district's position that the Secretary's promulgation of the November 1, 1973, rate schedule was deficient in many respects. Among other things, we feel it constitutes a denial of procedural due process, and further, with respect to SMUD, we believe the rate increase violates our contract, specifically article 5(b) thereof. We firmly believe the procedures required under the terms of H.R. 14221 would be in the best interests of all concerned, namely, to refer the controversy of the Federal Power Commission for a decision to the reasonableness and adequacy of rate schedule promulgated by the Secretary, followed by a decision as to each of the five projects either approving or recommending their modification.

Lastly, we recommend that the bill be amended to prevent its being construed as interfering with SMUD's right to litigate the Secretary's action in raising the rate in what we feel is in direct violation of contractual provisions.

Our amendment, and I would like to note that it is the same amendment suggested to the committee in Congressman Moss' statement which was presented by Mr. Indritz last Friday. Section 4 of the bill as introduced reads as follows: "the rate schedule promulgated by the Secretary on November 1, 1973, for each of the five projects referred to in this act shall continue in effect." At this point we would suggest insertion of the following wording: "As to all customers for which such rates were validly promulgated on that date." The remaining language of section 4 "pending review thereof pursuant to this act" would follow our suggested wording.

In summary, SMUD believes that H.R. 14221 as amended in section 4 should be enacted at the earliest possible date.

That concludes my statement, sir.

Mr. JOHNSON. We want to thank you for your statement here as it relates to H.R. 14221.

As I interpret what you have said here, you are in full support of the legislation that is pending before this committee and that you recommend additional language to section 4.

Mr. DILLON. That is right.

Mr. JOHNSON. In your concern as to the rate increase, have you any information as to what was wrong with the amount of increase? What do you attribute the rise in rates to, based on your study of the rates that were asked for by the Secretary in the way of an increase?

Mr. DILLON. As the previous witness testified, we believe they are based on many invalid and illegal assumptions, one being that rate and repayment schedules cannot show deficit in the Central Valley project even in a single year. There are others, including the changing startup costs of projects that have not yet been funded in the rate base, and efforts to recover the high cost of power purchased by the Bureau from the Pacific Northwest. The Department did hold a hearing on July 10 in Sacramento, but it was a completely ex parte proceeding. We had no opportunity to cross-examine the witnesses or review the assumptions on which their conclusions as to CVP power rates were grounded. The material just was not available to us.

Mr. JOHNSON. Well, then I presume that the people that you represent did not object to some increase, but you figured the increases were excessive?

Mr. DILLON. That is right. We are subject to a 22-percent increase and that would cost in the range of \$1.7 million a year in additional power costs for the Central Valley project to our customers; we feel that is unjust.

Mr. JOHNSON. I also understand you have a little different type contract with the Federal Government than many of the preference customers in the Central Valley project?

Mr. DILLON. Yes sir. I think we are in a different position from most of them, certainly the same position as to the authority of the Secretary, but we do have a contract and under 5(b) it cannot be reviewed as to rates until May 25, 1978. Now, the Interior Department takes a different position, but that is our position.

Mr. JOHNSON. The gentleman from New Mexico, Mr. Runnels.

Mr. RUNNELS. Mr. Chairman, may I request at this time that we would have either in the record or for the file the contract that they are working under where you are of the assumption that it cannot be reviewed until May of 1978, because I think this would be most important to the members of this committee.

Mr. DILLON. I will be happy to supply that, sir.

Mr. JOHNSON. You have heard the request of the gentleman from New Mexico that he would like to have a copy of the contract between the municipal utility district and Department of the Interior. Is there objection?

Hearing none, so ordered.

[The contract follows:]

United States Department of the Interior, Bureau of Reclamation, Central Valley Project, California

CONTRACT FOR ELECTRIC SERVICE TO THE SACRAMENTO MUNICIPAL UTILITY DISTRICT

This contract, made the 11th day of December, 1952, and revised the 26th day of January, 1954, in pursuance of the Act of Congress approved June 17, 1902 (32 Stat. 388), and acts amendatory thereof or supplementary thereto, and particularly pursuant to the Act of Congress approved August 26, 1937 (50 Stat. 844, 850), as amended, and the Act of Congress approved August 4, 1939 (53 Stat. 1187), all collectively herein called the Federal Reclamation Law, between the United States of America, its successors or assigns in interest in the power production and transmission facilities of the Central Valley Project, hereinafter called the United States, represented by the officer executing this contract, his duly appointed successor, or his duly authorized representative, hereinafter called the Contracting Officer, and the Sacramento Municipal Utility District, a municipal utility district duly organized, created and existing under and by virtue of the laws of the State of California, hereinafter called the Contractor, its successors and assigns:

Now, therefore, for and in consideration of the matters hereinabove referred to and the mutual covenants herein set forth, the parties hereto agree as follows:

DEFINITIONS

1. Wherever used in this contract, the following terms shall have the respective meanings set opposite thereto:

(a) *Project*.—The electric power facilities of the Central Valley Project, California, as now or hereafter authorized by the Congress of the United States, or pursuant to Acts thereof, including that portion of multiple-purpose facilities properly allocable to electric power production.

(b) *Wheeling Contract*.—Contract No. 175r-2650 between the United States and the Pacific Gas and Electric Company, herein called PG&E, dated April 2, 1951, providing for transmission and exchange service, or under such contract as it may be amended or extended from time to time, or under the terms and conditions of any contract that may supersede said contract.

QUANTITY OF POWER AND ENERGY TO BE FURNISHED

2. (a) The United States, subject to the terms and conditions stipulated herein, will furnish to the Contractor, and the Contractor will purchase, accept and pay for according to the schedule hereinafter provided from and after the initial date of service as herein defined, firm electric power and energy at not greater than the Contractor's system load factor and in the amounts required by the Contractor up to a maximum simultaneous 30-minute demand of 180,000 kilowatts, herein called the contract rate of delivery for firm power. Such contract rate of delivery for firm power shall be subject to increase as follows: Contractor shall submit to the Secretary of the Interior annually, on or before October 31, an estimate of its foreseeable system load for the ensuing calendar year for review and approval by the United States. Upon approval such estimate shall become the contract rate of delivery for firm power for the ensuing year; provided, however, that if the actual power and energy requirements of Contractor's customers exceed such estimate then the United States shall furnish sufficient power and energy to meet such actual requirements for that year. The annual increase of the contract rate of delivery for firm power of 180,000 kilowatts shall be permitted until the contract rate of delivery for firm power is a maximum simultaneous 30-minute demand of 290,000 kilowatts.

(b) If, at any time during the term of this contract, the United States is unable, for causes other than uncontrollable forces as defined herein or service interruptions as set forth in General Power Contract Provision C, to supply from its own generating facilities the electric power and energy required by the Contractor, but not in excess of the quantity the United States is obligated to supply hereunder, the United States shall be obligated to supply such deficiencies by interchange, or by purchase or by other means if such purchase or other means are authorized and appropriated therefor by the Congress.

DELIVERY OF POWER AND ENERGY OVER PG&E FACILITIES

(3) (a) Beginning with the initial date of service and until commencement of delivery under the provisions of Article 4 hereof, the United States will deliver the power and energy to be supplied hereunder over the facilities of PG&E, pursuant to PG&E's obligation to make such delivery in accordance with the Wheeling Contract as evidenced by PG&E's letter to the United States dated November 25, 1953, and at such other delivery points, at the voltages and in the quantities at each point, upon which the United States, the Contractor and the PG&E shall have agreed or shall hereafter agree. At each delivery point at which power and energy is to be delivered over PG&E facilities, the United States shall request PG&E to provide adequate sectionalizing breakers, switches, or other protective equipment to maintain continuity of service.

(b) For as long as the power and energy to be supplied under this contract is delivered by the United States over the facilities of PG&E, the United States shall request PG&E to maintain the voltage regulation thereof at least as well as that which PG&E has heretofore maintained for the Contractor.

DELIVERY OF POWER AND ENERGY TO THE CONTRACTOR OVER FACILITIES OF THE CONTRACTOR

4. (a) Beginning on July 1, 1957, or any earlier date designated by the Contractor, the United States shall commence deliveries of power and energy to be supplied hereunder to the 230 kv facilities of the Contractor at Elverta Switchyard of the United States, in Sacramento County, California.

(b) To enable the Contractor to accept delivery of power and energy to be supplied hereunder in accordance with paragraph (a) of this Article, and to transmit such power and energy for use by its customers, the Contractor will construct (1) switching protection and transformation facilities adequate and necessary to receive 290,000 kilowatts from adequately protected bus structures at 230 kv at Elverta Switchyard and to transform such power to nominal voltages of 115 kv and 69 kv; and (2) two transmission circuits between Elverta Switchyard and a location adjacent to the lines of the United States in the southern portion of the service area of the Contractor, herein referred to as Contractor's South Sacramento Switchyard. Such construction shall be undertaken by the Contractor promptly following a grant of right of way by the United States as provided in paragraph (c) of this Article.

(c) Upon execution of this contract, or as soon thereafter as possible, the United States, to the extent that its legal interests in land will permit, shall grant to the Contractor the right to install and maintain on the eastern part of Elverta Switchyard, owned by the United States and upon the United States' transmission rights of way from Elverta Switchyard to Contractor's South Sacramento Switchyard, the transmission and delivery facilities provided in paragraph (b) of this Article. The United States shall also grant to the Contractor the right to enter on such rights of way for the purpose of removing such facilities at any time during the term of this contract and for a reasonable time thereafter.

(d) Following completion of the Contractor's facilities described herein, the United States shall, upon request by the Contractor, discontinue delivery of power and energy over the facilities of PG&E at the locations, and at the time and date for each location, as designated by the Contractor. To the extent that such delivery over PG&E facilities is discontinued United States shall deliver a corresponding amount, adjusted for losses, of power and energy to the Contractor at Elverta Switchyard at 230 kv.

(e) The United States agrees to permit the Contractor to operate in parallel with the electric system of the United States any generating capacity which the Contractor shall construct or acquire during the term of this contract. Parallel operation of the generating capacity of the United States and the Contractor shall be pursuant to such terms and conditions as the parties may hereafter agree upon, and for the purpose of reaching such agreement the United States and the Contractor shall confer together within a reasonable time after the Contractor shall notify the United States that it intends to place in operation its own generating capacity.

RATES AND CHARGES

5. (a) Beginning with the initial date of service, the Contractor shall pay for electric power and energy supplied by the United States at the following monthly rates and charges:

Demand Charge: \$.75 per kilowatt of Billing Demand.

Energy Charge: First 130 kwh per kw of Billing Demand at 4 mills per kwh; Next 130 kwh per kw of Billing Demand at 3 mills per kwh; Excess over 260 kwh per kw of Billing Demand at 2 mills per kwh.

Minimum Bill: \$1.00 per kilowatt of the contract rate of delivery for firm power.

Meter Readings: Meter readings at the several points of delivery at which power and energy is supplied under this contract shall be combined for billing purposes.

Billing Demand: The maximum sum of 30-minute integrated demands occurring simultaneously at all points of delivery through which electric power and energy is supplied to the Contractor under this contract.

Adjustments: If delivery is made over facilities of PG&E, as contemplated by Article 3, five percent (5%) discount will be allowed on the demand and energy charges applicable to such delivery. If delivery is made to the 230 kv facilities of the Contractor as provided in Article 4, ten (10%) discount will be allowed on the demand and energy charges applicable to such delivery.

(b) The rates and charges set forth in paragraph (a) of this Article shall remain in effect without modification for a period of ten (10) years from and after the initial date of service, or until the date (herein referred to as the New Capacity Date) on which there is placed in operation new generating capacity of the Project totalling not less than 62,500 kva and in addition to that constructed or to be constructed at Shasta, Keswick, Folsom, and Nimbus dams, whichever date shall first occur. The schedule of rates and charges shall be subject to review and modification on (1) the day after the tenth anniversary of the initial date of service or (2) the New Capacity Date, whichever is earlier, and at five (5) year intervals thereafter, in accordance with any changes made in the United States' schedule of rates and charges for the sale of Project firm power for resale, and any such changes shall establish a level of rates and charges to produce revenue which, considered together with all other revenue from the sale or disposition of all other Project power, is not in excess of that required:

(i) to defray the annual operation and maintenance expenses of the Project, and

(ii) to provide for the replacement of Project units of property, the service lives of which are fifty (50) years or less, such provision to be accrued ratably over the service lives of such property units by the sinking fund method using:

an interest rate of three percent (3%) per annum and based upon the actual cost of such property units to the United States, and

(iii) to return to the United States

(1) its construction investment in the individual commercial electric facilities of the Project, including that portion of multiple-purpose facilities properly allocable to electric power production, within a minimum repayment period of fifty (50) years, or such repayment period as is provided for in the Federal Reclamation Law, from the date each such facility is first placed in operation, plus

(2) interest on the annual unamortized balance of such construction investment, at a maximum interest rate of three percent (3%) per annum, by means of a combined annual payment of said construction investment and interest thereon in any year of not less than three percent (3%) and not more than three and eighty-nine one hundredths percent (3.8%) of the accumulated undiminished investment of the United States in said commercial electric facilities of the Project during any year for which such combined annual payment is computed, and

(iv) to return to the United States, within a minimum repayment period of fifty (50) years, or such repayment period as is provided for in the Federal Reclamation Law, such other costs as are properly recoverable from Project power revenue, pursuant to Federal Reclamation Law in effect on the date of the execution of this contract.

(c) The United States will establish and maintain, subject to modification as herein provided, schedules of rates and charges of a single standard for the sale of Project firm power for resale, and will make available said standard schedules to all resale customers served by the Project, including the Contractor.

(d) In the event that (1) the rates and charges set forth in paragraph (a) of this Article are increased as provided herein to a level which results in annual costs to the Contractor in excess of the annual costs of an equivalent amount of power and energy which the Contractor could produce by means of its own generating facilities, operated alone or operated in conjunction with purchases from other public agencies, including the United States, and (2) the Contractor shall have commenced construction of its own generating facilities, the Contractor shall have the option of terminating this contract. The Contractor shall exercise such option within two (2) years after the date on which the United States promulgates such increased rates and charges by giving written notice of its exercise thereof to the Contracting Officer. In the event that the Contractor shall elect to terminate this contract, it shall specify a termination date not less than eighteen (18) months after such notice to the Contracting Officer.

REIMBURSEMENT OF THE UNITED STATES FOR PG&E DELIVERY CHARGES

6. (a) When the United States delivers power and energy to the Contractor through the facilities of PG&E, the Contractor shall, in addition to paying the rates and charges for power and energy set forth in Article 5, reimburse the United States for capacity costs and transmission losses incurred by reason of such delivery according to the following schedule:

Capacity cost reimbursement

(1) For deliveries at 44 kv or higher at any metering point where the demand is 25,000 kilowatts or more:

The amount by which \$0.25 per kilowatt applied to the maximum 30-minute integrated demand at such point in any month exceeds \$0.001 per kwh applied to total energy delivered through such point in the same month.

(2) For deliveries at less than 44 kv but not less than 22 kv:

(a) where the demand is not less than 20,000 kw: \$0.10 per kilowatt per month of maximum 30-minute integrated demand measured individually at each metering point.

(b) where the demand is less than 20,000 kw: \$0.22 per kilowatt per month of maximum 30-minute integrated demand measured individually at each metering point.

(3) For deliveries at less than 22 kv:

\$0.22 per kilowatt per month of maximum 30-minute integrated demand measured individually at each metering point.

Transmission loss reimbursement

For all deliveries at less than 44 kv, the amount of power and energy for which the Contractor shall be billed shall be increased by four percent (4%) to compensate the United States for transmission losses.

(b) The schedule according to which the Contractor shall reimburse the United States for capacity costs and transmission losses, as provided in paragraph (a) of this Article, shall be adjusted by the United States in the event and to the extent that such costs or allowances for losses are adjusted by PG&E pursuant to a decision of the Public Utilities Commission of the State of California affecting the Wheeling Contract.

CONTRACTOR'S RESPONSIBILITY FOR SERVICE WITHIN ITS BOUNDARIES

7. (a) In recognition of (1) the Contractor's status as a public agency of the State of California, (2) its ownership and operation of a single integrated interconnected electric distribution system serving what is essentially one large metropolitan area surrounded by a satellite rural area, (3) its status as sole participant for the area within its exterior boundaries in the rural electrification program of the Rural Electrification Administration, and (4) the responsibility which it has under this contract to construct the transmission and delivery facilities described in Article 4, the United States during the term of this contract agrees not to serve electric power and energy for use inside the Contractor's exterior boundaries, except to the Contractor, for as long as the Contractor shall continue its present policy of extending electric service to every applicant within its exterior boundaries (specifically including customers entitled to preference under the Federal Reclamation Law) at nondiscriminatory rates which accomplish the objectives of this contract, without any charge for such extension except for temporary service or service of questionable permanency. The agreement of this paragraph (a) applies to every area annexed to the Contractor pursuant to law where the factors recognized above exist, except as to any customers therein served by the United States at the time of such annexation.

(b) The Contractor shall not resell any of the power and energy furnished hereunder to any public agencies, person, firm, or corporation for resale without the consent of the United States.

METERING AT VOLTAGES OF 60 KV OR HIGHER

8. If the delivery voltage is at 60 kv or higher and power and energy are metered on the low voltage side of the Contractor's substation, transformer-loss compensators may be used to adjust meter readings taken on such low voltage side to the level which would be recorded if power and energy were metered at the delivery voltage.

POWER FACTOR

9. The Contractor normally will be required to maintain a power factor of not less than ninety percent (90%) lagging or leading except that the Contractor will be permitted to operate at a lower power factor when conditions are such, as determined by the Contracting Officer, that such lower power factor will not prevent the United States from making full use of its available generation and transmission facilities.

UNCONTROLLABLE FORCES

10. Neither party shall be considered to be in default in respect to any obligation hereunder, if prevented from fulfilling such obligation by reason of uncontrollable forces, which term, for the purpose of this contract, shall be deemed to include, but not be limited to, failure of facilities, flood, earthquake, storm, lightning, fire, epidemic, war, riot, civil disturbance, labor disturbance, sabotage, restraint by court or public authority, and similar occurrences, which by exercise of due diligence and foresight such party could not reasonably have been expected to avoid, but shall not include inadequacy of water for the generation of electric power and energy herein contracted for either party rendered unable to fulfill any obligation by reason of uncontrollable forces shall exercise due diligence to remove such inability with all reasonable dispatch.

TERM OF CONTRACT

11. This contract shall become effective upon the date of execution. The date of initial service shall be July 1, 1954, or such other date as the United States begins delivery of power and energy to the Contractor. This contract shall remain in effect for a period of forty (40) years from and after such initial date of service unless otherwise terminated as herein provided.

GENERAL POWER CONTRACT PROVISIONS

12. The General Power Contract Provisions attached hereto are hereby made a part of this contract the same as if they had been expressly set forth herein, except that Provisions D, E, F, I(b), M, Q, and R shall not apply, and to Provision A thereof shall be added the following language: "Wherever delivery to the Contractor is effected directly from electrical facilities of the United States, the United States will maintain the voltage at each delivery point within the limits of five percent (5%) above or below the nominal delivery voltage."

In witness whereof, the parties hereto have caused this contract to be executed the day and year first above written.

Approved as to Legal Sufficiency: William J. Burke, Special Assistant to the Solicitor, Department of the Interior.

Approved as to Form: Ralph A. Tudor, Under Secretary of the Interior.

Approved as to Form: Frank L. Sprague Attorney, Sacramento Municipal Utility District.

THE UNITED STATES OF AMERICA,

By FRED G. RANDAHL,

Assistant Secretary.

SACRAMENTO MUNICIPAL UTILITY DISTRICT,

By JAS. E. McCAFFREY,

General Mgr. & Chief Engr.

Effective June 10, 1952.

U.S. Department of the Interior, Bureau of Reclamation

GENERAL POWER CONTRACT PROVISIONS

A. CHARACTERISTICS OF POWER AND ENERGY

Electric energy supplied hereunder will be three-phase, alternating current, at a nominal frequency of sixty (60) cycles per second.

B. DELIVERY OF ENERGY IN EXCESS OF CONTRACT OBLIGATION

The Contractor may from time to time, in the absence of objection by the contracting officer, use energy at rates greater than the contract rate of delivery in effect for each type of service provided for in this contract, but such greater use shall not be deemed to establish in the Contractor any right thereto and the Contractor shall cease any such greater use whenever and for the periods of time requested by the contracting officer.

C. CONTINUITY OF ELECTRIC SERVICE TO BE FURNISHED

The electric service, unless otherwise specified, will be furnished continuously except (1) for interruptions or reductions due to uncontrollable forces, as defined herein; (2) for interruptions or reductions due to operation of devices installed for power system protection; and (3) for temporary interruptions or reductions, which, in the opinion of the contracting officer, are necessary or desirable for the purposes of maintenance, repairs, replacements, installation of equipment, or investigation and inspection. The United States, except in case of emergency as determined by the contracting officer, will give the Contractor reasonable advance notice of such temporary interruptions or reductions and will remove the cause thereof with diligence.

D. MULTIPLE POINTS OF DELIVERY

When electric service is furnished at two or more points of delivery under the same schedule of rates, said schedule of rates shall apply separately to the service supplied at each point of delivery.

E. UNCONTROLLABLE FORCES

Neither party shall be considered to be in default in respect to any obligation hereunder, if prevented from fulfilling such obligation by reason of uncontrollable forces, the term uncontrollable forces being deemed for the purpose of this contract to mean any cause beyond the control of the party affected, including, but not limited to, failure of facilities, flood, earthquake, storm, fire, lightning, epidemic, war, riot, civil disturbance, labor disturbance, sabotage, and restraint by court or public authority, which by exercise of due diligence and foresight such party could not reasonably have been expected to avoid. Either party rendered unable to fulfill any obligation by reason of uncontrollable forces shall exercise due diligence to remove such inability with all reasonable dispatch.

F. MODIFICATION OF RATES

The rate schedule specified in this contract shall be subject to successive modification by the United States through the promulgation of superseding rate schedules. If at any time the United States promulgates a rate schedule superseding the rate schedule then in effect under this contract, it will promptly notify the Contractor thereof. Said superseding rate schedule, as of its effective date, shall become effective as to this contract unless the Contractor, by notice in writing given to the contracting officer within sixty (60) days after notice to it by the United States of promulgation of said superseding rate schedule, shall elect to terminate this contract effective as of such date not more than three (3) years subsequent thereto as the Contractor shall herein specify. In the event of such termination, said superseding rate schedule shall not be effective during the period of the remaining unexpired term of this contract or during a period of two years from the date of notice to the Contractor of the promulgation of said superseding rate schedule, whichever period is the shorter.

G. BILLINGS AND PAYMENTS

The United States will submit bills to the Contractor on or before the tenth day of each month for electric service furnished during the preceding month, and payments will be due and payable by the Contractor on the first day of the month immediately succeeding the date each bill is submitted.

H. NONPAYMENT OF BILLS

If the Contractor fails to pay any bill when due an interest charge of one per cent (1%) of the amount unpaid shall be added thereto as liquidated damages, and thereafter, as further liquidated damages, an additional interest charge of one-half of one per cent ($\frac{1}{2}\%$) of the principal sum unpaid shall be added on the first day of each succeeding calendar month until the amount due, including interest, is paid in full. The United States shall have the right upon not less than fifteen (15) days' advance written notice to discontinue furnishing electric service to the Contractor for nonpayment of bills and to refuse to resume same so long as any part of the amount due remains unpaid. Such a discontinuance of electric service will not relieve the Contractor of liability for the minimum charge during the time electric service is so discontinued. The rights given herein to the United States, either at law or in equity, for the breach of any of the provisions hereof.

I. ADJUSTMENTS FOR FRACTIONAL BILLING PERIOD

(a) For a fractional part of a billing period at the beginning or end of service, and for fractional periods due to withdrawals of service, the demand charge, the kilowatt-hour blocks of the energy charge, and the minimum bill shall each be proportionately adjusted in the ratio that the number of hours that electric service is furnished to the Contractor in such fractional billing period bears to the total number of hours in the billing period involved.

(b) Whenever irrigation and/or drainage pumping service is supplied under this contract, adjustments in the demand charge and in the kilowatthour blocks of the energy charge as applicable, and in the minimum charge of the rate schedule under which service is supplied, shall be made for the fractional part of the billing period at the beginning and end of pumping service in each year in like manner as is provided for in section (a) of this article. If pumping service is supplied in conjunction with a service for other purposes and is not metered separately, the billing demand for pumping service shall be considered to be the difference between the highest 30-minute integrated demand measured during the billing period and the contract rate of delivery for firm power.

J. ADJUSTMENTS FOR INTERRUPTIONS TO SERVICE

Should the delivery of electric energy be interrupted or curtailed because of conditions on the power system of the United States, which system for purpose of adjustments hereunder shall include transmission facilities utilized but not owned by the United States, below the contract rate of delivery for the affected type of service provided for in this contract or below the rate of delivery required by the Contractor at the time of such reduction, whichever is the lesser, for a period or periods of one (1) hour or longer in duration each, the total number of hours of curtailed service in any billing period shall be determined by adding the sum of the number of hours of interrupted service to the product of the number of hours of reduced service multiplied by the percentage of said reduction below said contract rate of delivery or below the rate of delivery required by the Contractor at the time of such reduction, whichever is the lesser. The demand charge, the kilowatthour blocks of the energy charge, and the minimum bill shall each be proportionately adjusted in the ratio that the total number of hours of such curtailed service as herein determined bears to the total number of hours in the billing period involved. The Contractor shall make written claim, within thirty (30) days after receiving the monthly bill, for adjustment on account of any curtailment to service, for a period or periods of one (1) hour or longer in duration each, alleged to have occurred and which is not reflected in such bill. Failure to make such written claim, within said thirty (30) day period, shall constitute a waiver thereof. All curtailments to service, for any reason whatsoever, which are due to conditions on the power system of the United States, shall be subject to the provisions of this article and the Contractor shall be limited in its remedy to the relief granted by this article.

K. MEASUREMENT OF ELECTRIC POWER AND ENERGY

The total electric power and energy delivered to the Contractor will be measured by metering equipment to be furnished and maintained by the United States. The meter or meters shall be sealed and the seals shall be broken only upon occasions when the meters are to be inspected, tested, or adjusted, and representatives of the Contractor shall be afforded reasonable opportunity to be present upon such occasions. The meter or meters shall be tested at least once each year by the United States and at any reasonable time upon request therefor by either party. Any metering equipment found to be defective or inaccurate shall be repaired and readjusted or replaced. Should any meter fail to register, the electric power and energy delivered during such period of failure to register shall, for billing purposes, be estimated by the contracting officer from the best information available.

L. CORRECTIONS FOR INACCURATE METERS

If any of the meter tests provided for herein discloses that the error of any meter or meters exceeds two per cent (2%), correction based upon the inaccuracy found shall be made of the records of electric service furnished since the beginning of the monthly billing period immediately preceding the billing period during which the test was made; *Provided*, That no correction shall be made for a longer period than such inaccuracy may be determined by the contracting officer to have existed. Any correction in billing resulting from such correction in meter records shall be made in the next monthly bill rendered by the United States to the Contractor, and such correction when made shall constitute full adjustment of any claim between the parties hereto arising out of such inaccuracy of meters.

M. POWER FACTOR

While the Contractor will normally be required to maintain the power factor as stated in the rate schedule then in effect under this contract, the Contractor will be permitted to operate at a lower power factor when conditions are such, as determined by the contracting officer, that a lower power factor will not prevent the United States from making full use of its available generating and transmission facilities.

N. COOPERATION OF CONTRACTING PARTIES

(a) If, in the maintenance of their respective power systems and/or electrical equipment and the utilization thereof for the purposes of this contract, it becomes necessary by reason of any emergency or extraordinary condition for either party to request the other to furnish personnel, materials, tools, and equipment for the accomplishment thereof, the party so requested shall cooperate with the other and render such assistance as the party so requested may determine to be available. The party making such request, upon receipt of properly itemized bills from the other party, shall reimburse the party rendering such assistance for all costs properly and reasonably incurred by it in such performance, including not to exceed ten per cent (10%) thereof for administrative and general expenses, such costs to be determined on the basis of current charges or rates used in its own operations by the party rendering assistance.

(b) No laborer or mechanic, in the employ of the Contractor, doing any part of the work contemplated by this article, shall be required or permitted to work more than eight hours in any one calendar day upon work at the site thereof, except upon the condition that compensation is paid to such laborer or mechanic in accordance with the provisions of this article. The wages of every laborer and mechanic employed by the Contractor in the performance of any part of the work contemplated by this article shall be computed on a basic day rate of eight hours per day and work in excess of eight hours per day is permitted only upon the condition that every such laborer and mechanic shall be compensated for all hours worked in excess of eight hours per day at not less than one and one-half times the basic rate of pay. For each violation of the requirements of this article a penalty of five dollars shall be imposed upon the Contractor for each laborer or mechanic for every calendar day in which such employee is required or permitted to labor more than eight hours upon said work without receiving compensation computed in accordance with this article, and all penalties thus imposed shall be withheld for the use and benefit of the United States; *Provided*, That this stipulation shall be subject in all respects to the exceptions and provisions of U.S. Code, title 40, sections 321, 324, 325, 325a, and 326 relating to hours of labor and to compensation for overtime.

O. PROVISIONS RELATIVE TO EMPLOYMENT

(a) The Contractor shall not discriminate against any employee or applicant for employment because of race, creed, color, or national origin, and shall require an identical provision to be included in all subcontracts; *Provided*, however, That this clause does not refer to, extend to or cover the business or activities of the Contractor which are not related to or involved in the performance of any part of the work contemplated by this contract.

(b) In the performance of any part of the work contemplated by this contract, the Contractor shall not employ any person undergoing sentence of imprisonment at hard labor.

P. TRANSFER OF INTEREST IN CONTRACT BY CONTRACTOR

No voluntary transfer of this contract or of the rights of the Contractor hereunder shall be made without the written approval of the Secretary of the Interior; *Provided*, That if the Contractor operates a project financed in whole or in part by the Rural Electrification Administration the Contractor may transfer or assign its interest in the contract to the Rural Electrification Administration or any other department or agency of the Federal Government without such written approval; *Provided further*, That any successor to or assignee of the rights of the Contractor, whether by voluntary transfer, judicial sale, foreclosure sale, or otherwise, shall be subject to all the provisions and conditions of this contract to the same extent as though such successor or assignee were the original Contractor hereunder; and *Provided further*, That the execution of a mortgage or trust deed, or judicial or foreclosure sales made thereunder, shall not be deemed voluntary transfers within the meaning of this article.

Q. ASSIGNMENT OF INDUSTRIAL CONTRACT BY THE UNITED STATES

When the Contractor hereunder is denominated an industrial customer, the United States may transfer and assign this contract at any time without the consent of the Contractor to any public body or cooperative engaged in the business of distributing electric power and energy purchased at wholesale from the United States if such assignee agrees to take over and assume all the rights, duties, and obligations of the United States under this contract. Whenever a transfer or assignment of this contract is made by the United States to a public body or cooperative pursuant hereto, such transfer or assignment shall be and constitute a novation and thereafter the United States shall be relieved of all liability under said contract and under said assignment and the Contractor shall look solely to the assignee for performance of this contract.

R. CONTRACT SUBJECT TO COLORADO RIVER COMPACT

Where the energy sold hereunder is generated from waters of the Colorado River system, this contract is made upon the express condition and with the express covenant that all rights hereunder shall be subject to and controlled by the Colorado River Compact approved by section 13(a) of the Boulder Canyon Project Act of December 21, 1928 (45 Stat. 1057) and the parties hereto shall observe and be subject to and controlled by said Colorado River Compact in the construction, management, and operation of the dams, reservoirs, and power plants from which electrical energy is to be furnished by the United States to the Contractor hereunder, and in the storage, diversion, delivery, and use of water for the generation of electrical energy to be delivered by the United States to the Contractor hereunder.

S. WAIVERS

Any waiver at any time by either party hereto of its rights with respect to a default or any other matter arising in connection with this contract shall not be deemed to be a waiver with respect to any subsequent default or matter.

T. NOTICES

Any notice, demand or request required or authorized by this contract shall be deemed properly given if mailed, postage prepaid, to the contracting officer at the address shown on the signature page hereof, on behalf of the United States, except where otherwise herein specifically provided, and to the officer signing for the Contractor at the address shown on the signature page hereof, on behalf of the Contractor. The designation of the person to be notified or the address of such person may be changed at any time by similar notice.

U. CONTINGENT UPON APPROPRIATIONS

Where the operations of this contract extend beyond the current fiscal year, the contract is made contingent upon Congress making the necessary appropriation for expenditures hereunder after such current year shall have expired. In case such appropriation as may be necessary to carry out this contract is not made, the Contractor hereby releases the United States from all liability due to the failure of Congress to make such appropriation.

V. OFFICIALS NOT TO BENEFIT

No Member of or Delegate to Congress or Resident Commissioner shall be admitted to any share or part of this contract or to any benefit that may arise herefrom, but this restriction shall not be construed to extend to this contract if made with a corporation or company for its general benefit.

W. COVENANT AGAINST CONTINGENT FEES

The Contractor warrants that it has not employed any person to solicit or secure this contract upon any agreement for a commission, percentage, brokerage, or contingent fee. Breach of this warranty shall give the United States the right to annul the contract or, in its discretion, to deduct from the contract price or consideration the amount of such commission, percentage, brokerage, or contingent fees. This warranty shall not apply to commissions payable by contractors upon contracts or sales secured or made through bona fide established commercial or selling agencies maintained by the Contractor for the purpose of securing business.

Mr. RUNNELS. Mr. Chairman, I would like to ask of the witness, Mr. Dillon, if he thinks it is most important, as the chairman has stated, that the language be added in section 4 so that he could go ahead and challenge the validity in a court case and there would be no misunderstanding?

Mr. DILLON. Right, yes.

Mr. RUNNELS. And evidently your SMUD ring is pretty heavy?

Mr. DILLON. Yes, it is.

Mr. RUNNELS. The \$1.7 million at 22 percent increase. Do you feel that the public was not given sufficient information as to why they made an increase of this magnitude?

Mr. DILLON. Absolutely, Mr. Runnels. As I said, it was a completely exparte hearing. There was no opportunity for anybody to present any evidence to the contrary.

Mr. RUNNELS. And you were not accorded the courtesy of questioning the witnesses; is that correct?

Mr. DILLON. That is correct; yes, sir.

Mr. RUNNELS. Sort of like a kangaroo court and they just told you what they were going to do?

Mr. DILLON. Almost.

Mr. RUNNELS. Thank you, Mr. Chairman.

Mr. JOHNSON. The gentleman from Nevada, Mr. Towell.

Mr. TOWELL. No questions, Mr. Chairman.

Mr. JOHNSON. Mr. Ketchum.

Mr. KETCHUM. No questions, Mr. Chairman.

Mr. JOHNSON. We thank you for your appearance here, and if you will furnish a contract with the Federal Government—

Mr. DILLON. I will do that.

Mr. JOHNSON. Our consultant, Mr. Casey, has some questions.

Mr. CASEY. We still have three other transcripts we have to elicit from somebody. I thought I might ask if the transcript of the July 10, 1973 hearing in Sacramento was available to you and, if so, would you be willing to furnish it for our file. It has already been ordered into the file. We just have to locate it.

Mr. DILLON. Fine. I will supply it.

Thank you, Mr. Chairman.

Mr. JOHNSON. Our next witness will be Hon. Gary Gillmor, mayor of the city of Santa Clara, Calif., and chairman of the Northern California Power Agency.

If you people will all want to come up as a panel; is that the way, or do you want to appear individually?

STATEMENT OF HON. GARY GILLMOR, MAYOR, CITY OF SANTA CLARA, CALIF., AND CHAIRMAN, NORTHERN CALIFORNIA POWER AGENCY, ACCOMPANIED BY ROBERT C. McDIARMID, SPECIAL COUNSEL, NORTHERN CALIFORNIA POWER CO., AND HERBERT WESTFALL, MANAGING PARTNER, R. W. BECK & ASSOCIATES

Mayor GILLMOR. We could come as a panel.

Mr. JOHNSON. We have Mr. Herbert C. Westfall, managing partner of R. W. Beck & Associates, and we have Mr. McDiarmid.

You may proceed.

Mayor GILLMOR. Thank you. On behalf of the Northern California Power Agency we endorse the implementation of H.R. 14221.

My name is Gary Gillmor and I appear here as chairman of the Northern California Power Agency, which represents over 400,000 citizens of California residing and working in the cities of Redding, Roseville, Biggs, Alameda, Gridley, Ukiah, Healdsburg, Lodi, Lompoc, Palo Alto, the Plumas-Sierra Rural Electric Cooperative, and Santa Clara, the city of which I am the mayor.

We believe this bill H.R. 14221, should be enacted and become the law.

Why should it be enacted? There is an old saying that can be paraphrased as follows: If one forgets history, then one can be expected to repeat its mistakes.

The history of the rate increases proposed by the Secretary of the Interior provides a path that we must remember so that we do not forget.

The first announcements of this proposed rate increase also stated that public meetings would be held. Those who traveled to Sacramento, Calif. that day remember Mr. J. Robert Hammond, the assistant regional director, start the meeting with the expression, "We will not answer any questions."

We remember difficulties in getting information, unless we asked for specific information.

We remember not obtaining load curves upon which the amount of preference power available is established.

We remember being denied allocations of preference power while large amounts of capacity and energy flows to a private investor-owned utility.

We remember being denied the fruits of the surplus energies due to the conservation efforts of our citizens, because Reclamation said it was not possible for this power to flow to preference agencies.

We recall congressional subcommittee hearings in January when we were told why no public hearings were held. We were told and let me quote, "There is an old saying in Interior that you don't get into a (expletive deleted) contest with a skunk."

Finally we recall letters from Deputy Assistant Secretary Wilson, dated April 18, 1974, and Assistant Secretary Horton, dated March 14, 1974, in which they state they are considering possible modification of a second step rate increase in 1977.

But we also remember the report of the Comptroller General that points out that some of these very issues that they wish to charge for now and study later do not comply with the congressional intent or department directives.

This cavalier treatment of the people's money is uncalled for and unwarranted. Rate increases should be based on fact and the facts presented to date show that this rate increase is exorbitant and has not yet been justified.

Interior would study while we pay, yes; we pay \$6 million.

This history illustrates the cogent facts: An urgent review of the facts of this rate increase is needed by some impartial body—this bill does this.

The public must be afforded the right in future similar situations to full public disclosure.

Gentlemen, I commend the sponsors for introducing this needed legislation and urge your support. Further testimony will be given—but I would like to add as an elected official that you people are the ones we look to. I don't think that you, based on your obligations as a Congressman would try to tell your constituents something if in fact you have not had due process in regard to listening to the facts and conditions necessary so that you could report back to your constituents. I find it very embarrassing for me as a mayor of 100,000 people to serve the people and their utility needs when we have to go to them and state that the Secretary has promulgated these rates. We cannot understand all of the unique features of these rates because we were told in our first so-called public hearing that we will not answer any questions directed to the Federal Government. I cannot tolerate this as a locally elected official. I feel I have an obligation to due process when I have to make decisions on a local level. I feel Congressmen have the same obligation and I think the Interior Department and the Bureau does also.

In closing, I am a small businessman as well and I look upon this similar to a real estate venture whereby you have a shopping center or commercial complex and in this shopping center or commercial complex you usually find a situation where the major tenant gets the most favorable conditions. He gets the lesser rent and he gets all of the types of situations which makes his lease more profitable. I look at this type of promulgation of the rates and the situation with Interior where we find some of the majors in regard to this situation are getting the favorable treatment a-la Centralia power and the sale of power to the privately-owned utility and let's find these in a less favorable situation like in a shopping center where the satellite store must pay the higher rent and not get the favorable situation. Cities that are in a situation whereby we look at this rate increase, had they been preference customers or not, a city like Roseville or Redding. I think we should also enjoy some of the fringe benefits available in the Centralia project and not always bear the brunt of it like we are in this 50-odd percent if it is fully achieved if it becomes a reality in the late 1970's. This more than doubles the rate increase of some of the cities. I hope you people will pass this on.

HR 14221 we endorse highly, the 400,000 people in our utility district, as well as the 100,000 people in Santa Clara.

Thank you for allowing me to participate.

Mr. JOHNSON. Thank you, mayor.

I know you have followed this from the start, as I have. It does concern many people. It is very hard on an area that is subject to this increase and have it passed on to the consumer in the electric bill. I, too, am very much concerned about the amount of the increase. I am not opposed to a proper increase due to the inflation on maintenance, operation, and replacement. But when you get into the other matters of concern that were used to establish this rate, I think there is room for concern. Certainly we want to have the proper consideration given to any rate increase that is really needed to make these projects whole over their repayment period. I think we ought to face up to the fact that they should be self-supporting and that there is repaid to the Federal Government their just cost, but nothing extra and nothing to accumulate a surplus at the end of the trail.

I presume there are others here who have statements. We might as well hear all three of you before we put questions to the three of you. Who wants to go next?

Mr. McDIARMID. I will, if I may.

I am Robert C. McDiarmid. I have a statement of my partner, George Spiegel. At 7:30 this morning, it developed that he was too sick to make it into the office. Consequently I wound up with it.

As Mayor Gillmor has said, we strongly support and endorse this bill.

Mr. JOHNSON. Just a moment. Your full statement will appear in the record and you may summarize.

[The above referred to statement follows:]

STATEMENT OF ROBERT C. McDIARMID, SPECIAL COUNSEL TO THE NORTHERN CALIFORNIA POWER AGENCY, AND THE CITIES OF BIGGS, GRIDLEY, PALO ALTO, REDDING, ROSEVILLE, AND SANTA CLARA, CALIF., AND THE PLUMAS-SIERRA RURAL ELECTRIC COOPERATIVE, INC.

As Mayor Gillmor has noted, the Northern California Power Agency ("NCPA") and its members which are preference customers of the Bureau of Reclamation's Central Valley Project strongly support and endorse the bill under consideration. That bill will provide NCPA and its members the due process which they were denied in connection with the Department of the Interior's consideration of rate increases which were proposed on May 28, 1973 and which were announced on November 1, 1973. The rates to preference customers were increased by 25 percent effective April 1, 1974, and will be increased again beginning January 1, 1977 for a total increase of 50 percent above pre-existing rates. NCPA's members will bear a large share (approximately 30 percent or \$11 million per year) of the increase.

Prior to the Interior Department's announcement of rate increases, members of Congress and NCPA and its members urged that formal procedures be adopted which would provide for public hearings and an opportunity for affected persons to present a full case, including the presentation and cross-examination of witnesses. In my prepared written statement presented on January 22, 1974 to the Conservation and Natural Resources Subcommittee of the House Committee on Government Operations¹ I described the inadequacy of the procedures employed by the Interior Department. We have never been given a satisfactory explanation of why the Interior Department denied us our basic due process right to a hearing. The only reason we have seen set forth by the Interior Department was that it perceived "no need for the expense, delay, and rigidities that more formal proceedings with such features as sworn testimony, cross-examination, rules of evidence, and written briefs would entail."²

Rather than attempting to find some middle ground that would accord interested persons the essential ingredients of due process while at the same time streamlining procedures to minimize "expense, delay and rigidities", the Department of the Interior decided to limit customer input to the submission of written comments. The Department and the Bureau went so far as to refuse to answer questions at the one public conference held on the proposed increase on July 10, 1973. For example, the Bureau representatives at that meeting would not even answer the question of whether CVP rates to Pacific Gas and Electric Company were being increased.³ When the matter of the refusal to answer questions was brought up at the House CVP hearing, no one from the Department or the Bureau could indicate who made the decision or why no discretion was accorded government officials to respond to certain questions at the July 10 meeting. The only thing that is clear from the discussion at the House CVP Hearing was that the instruction not to answer questions was received by the Sacramento regional office of the Bureau from the Office of the Commissioner of Reclamation. This

¹ Hearing on Interior Department's Power Rate Increase for Customers of the Central Valley Project in California (hereinafter referred to as "House CVP Hearing").

² Letter of June 21, 1973 from Assistant Secretary of the Interior Jack Horton to Honorable Henry S. Reuss.

³ See Official Report of Proceedings Before the Bureau of Reclamation in the Matter of Mid-Pacific Region Open Hearing on Federal Power Rate Adjustments, July 10, 1973, transcript pp. 93-96.

instruction was not discussed with the Department's Solicitor's office, it does not reflect Department policy, the official of the Commissioner's office who relayed the instruction did not make the decision, and the official of the Interior Department who could have overruled the determination not to answer questions did not do so.⁴ It is evident now that the decision not to hold hearings did not minimize costs, but rather, has increased costs because of the necessity for detailed Congressional review of the manner in which the rate increases were determined and of the Interior Department's basis for the rate increases. As Congress McCloskey observed at the House CVP Hearing (transcript p. 136): "I cannot conceive of more expense than has been incurred in the preparation for these hearings and what we are conducting today, and I think I can assure you that in the future, any rate increase of this kind where you do not fully disclose every aspect of it . . . [to] the public is going to result in a complaint which this Committee will inquire into."

The Bureau's refusal to answer questions at the July 10, 1973 public meeting in Sacramento is only one of the basic elements of due process which was denied the CVP preference customers. Very little of the information and data underlying and needed to evaluate the original rate increase proposal was made available prior to the July 10 meeting, although we had requested such information and data well in advance. Our requests for a postponement of that meeting were denied and we were forced to go forward and make presentations on the basis of incomplete data and information. Although we were given a subsequent opportunity to make further submittals, the time allowed for such submittals was unreasonably short in light of the magnitude and complexity of the issues. Also, we were handicapped in preparing the further submittals by the unavailability to us of some of the information and data related to CVP questions which was needed for a full study of the basis for CVP rates to preference customers.

Despite not having all the information and data needed for a full study and despite being compelled to prepare our study within an unreasonably short period of time, R. W. Beck and Associates, the engineering consultants to NCPA, were able to complete a study showing that no rate increase to preference customers were justified.⁵ Testimony with respect to that study plus testimony dealing with other matters related to the proposed rate increase was presented by NCPA and its members together with accompanying affidavits, and we offered to make our witnesses available for cross-examination by the Bureau and others. In contrast, the Bureau did not offer testimony under oath in support of its rate increase proposal and refused to tender testimony under oath and to make witnesses available for questioning and cross-examination. There are a number of significant factual issues and significant issues of engineering and business judgment which underlie the difference in conclusions and rate recommendations as between the Bureau and NCPA and its members. The only way in which these matters can be resolved satisfactorily is through the process of questioning and testing the bases for such differences. Yet, we were denied any opportunity to question witnesses for the Bureau on a public record.

Not only were we denied the right to have the record before the Department based on a public record with sworn testimony and cross-examination, we were not given an opportunity to see the Bureau's comments on our submittals so that we could at least submit written comments in reply thereto. Following the Department's announcement of the rate increase on November 1, 1973, we were provided with copies of comments by the Bureau and found that inadequate consideration was given to our study and other presentations. Of course, by that time it was too late for us to present any comments to the Secretary of the Interior since the rate increases had already been announced.

It is clear that the rate increase determination is not based on a complete record since the Interior Department and the Bureau of Reclamation refused to permit procedures which would have enabled development of a full record. Under the circumstances involved in the rate increases in question, the opportunity for written comments is inadequate for the development of a record which would enable a fully informed decision to be made. The reasons for the kinds of procedures we had requested, and which were refused, are highlighted in the following passage from a decision issued last year by the U. S. Court of Appeals for the District of Columbia Circuit:⁶

Informal comments simply cannot create a record that satisfies the sub-

⁴ Transcript of House CVP Hearing, pp. 146-158.

⁵ That study was also prepared for the Sacramento Municipal Utility District.

⁶ *Mobil Oil Corporation v. Federal Power Commission*, 483 F. 2d 1238, 1260.

stantial evidence test. Even if controverting information is submitted in the form of comments by adverse parties, the procedure employed cannot be relied upon as adequate. A "whole record," as that phrase is used in this context, does not consist merely of the raw data introduced by the parties. It includes the process of testing and illumination ordinarily associated with adversary, adjudicative procedures. Without this critical element, informal comments even by adverse parties, are two halves that do not make a whole. Thus, it is adversary procedural devices which permit testing and elucidation that raise information from the level of mere inconsistent data to evidence "substantial" enough to support rates.

We presented comments and studies and sought to have procedures employed which would enable the development of a "whole record" on which the basis for CVP's revenue requirements and preference customer rates could be determined. The Interior Department, however, demonstrated no interest in having a "whole record" and prevented the development thereof.

In addition to failing to develop a "whole record", the Interior Department has set forth no determinations or findings in support of the announced rate increases. There is thus no way in which the underlying bases can be determined except by further probing such as was done by the Subcommittee on Conservation and Natural Resources of the House Committee on Government Operations or such as could be done at hearings before the Federal Power Commission as contemplated by H.R. 14221.

NCPA and its members support the proposed legislation because it would provide for evaluation of the current rate increases by an agency independent of the Interior Department. We consider this feature to be very important because of Interior's demonstrated unwillingness to let due process considerations interfere with its resolve to impose exorbitant rate increases on CVP preference customers. We feel that, unless the decision-making responsibility as to these increases is removed from the Interior Department, preference customers will continue to be stonewalled from having their views considered. Hopefully, as to future rate increases, the Interior Department will accord the public due process of law and it would be unnecessary for such rate increases to be heard by the Federal Power Commission. Therefore, we support H.R. 14221 as proposed which contemplates that future rate increases would be determined by the Secretary of the Interior after adequate public hearings and with a written decision on the record. If, however, the sorry history of the current rate increases repeats itself in the future we would deem it advisable at that time to consider transferring the ratemaking function permanently to the Federal Power Commission. It should be recognized that Federal Power Commission review of Interior Department power rates is not a novel concept. Indeed, the Bureau of Reclamation is in a sense an anachronism in this regard since other Interior Department marketing agencies—Bonneville Power Administration, Southeastern Power Administration, and Southwestern Power Administration—have their rates reviewed by the Federal Power Commission.

A further reason supporting Federal Power Commission review of the current rate increases is the issue which has been raised as to whether the Bureau of Reclamation can presently increase its rates for power sold to Pacific Gas and Electric Company ("PG&E"). The submittals on behalf of NCPA to the Department of the Interior demonstrated that the principal reason for the rate increase is the refusal of Interior to raise the rates the Bureau charges PG&E to a level which would recover its costs of serving PG&E. While it is not clear what rate changes have been established for sales to PG&E, it is clear that until at least April 1, 1976, PG&E will continue to pay pre-existing rates for power coming from sources other than CVP's own generation and apparently the rates for such power are assumed in the Bureau's studies to be increased to the level of the preference customer rates at that time.⁷ Yet, as reflected in the submittals made on behalf of NCPA, the non-Project power being sold to PG&E has been, and will continue to be, sold at substantial losses thereby resulting in an enormous subsidy to PG&E. The amount of subsidy for capacity sales of such power during the period from 1974 through 1994 would accumulate to more than \$92 million. The General Accounting Office, in its report on the reasonableness of the contentions made by NCPA and others, estimated that the loss from sales of non-Project capacity to PG&E would amount to \$116 million.⁸ The principal

⁷ There has been no indication by the Secretary of the Interior, however, that the rate for non-Project power will be increased at that time and we know of no rate increase proposal having been made in this regard.

⁸ "California's Central Valley Project—Proposed Power Rate Increase" (B-125042), dated November 19, 1973.

excuse advanced by the Bureau and the Department for failing to increase rates to PG&E for non-Project power is the determination that the Bureau's contract with PG&E (Contract No. 14-06-200-2948A) precludes any rate increase for such power prior to April 1, 1976. We disagree with this determination and believe the matter requires prompt resolution. That contract is on file with the Federal Power Commission and is subject to its jurisdiction; accordingly, the FPC is an appropriate forum to consider the disputed matter of contract interpretation. Moreover, the Bureau and PG&E have agreed in that contract (Article 32 thereof) that when they are unable to agree on a change of any rate or charge, "the matter shall be submitted to the Federal Power Commission for final decision." If the fully allocated cost of the non-Project power being sold to PG&E were recovered from PG&E there would be no need for a rate increase to preference customers.

Another aspect of the rate increase which is particularly appropriate for Federal Power Commission consideration, because it relates to the Bureau-PG&E contract, is whether the Bureau is making more free capacity available to PG&E than is required under the contract. This gift to PG&E of free capacity results in less capacity being sold to preference customers than could be sold, which in turn results in less revenue to the Bureau. Although the Bureau-PG&E contract provides that the preference customer load which may be served is 985,000 kilowatts prior to January 1, 1975 and up to 1,050,000 kilowatts in 1980 and each year thereafter (Article 14(a)(2)), the Bureau and PG&E are interpreting the contract in such a manner as to permit service to preference customers up to a peak of only 925,000 kilowatts for one hour and, when that load level is exceeded, sales to preference customers are withdrawn permanently by an equivalent amount. We find no basis under the contract or under federal reclamation law for withdrawals of this type and believe that preference customer loads up to 985,000 kilowatts should be served at this time. This issue should be resolved by someone other than the Interior Department which apparently has acquiesced in PG&E's interpretation of the contract to limit the availability of preference power to preference customers. In this regard we note that the Federal Power Commission has instituted an investigation to determine whether certain of PG&E's contracts, including its contract with the Bureau of Reclamation contain anticompetitive features;⁹ thus, the matter of limiting sales to preference customers could be appropriately considered in that proceeding in parallel with a rate review proceeding as contemplated by H.R. 14221.

There are a number of questions in addition to the matters related to rates to PG&E and the limitations imposed by PG&E which have been raised by NCPA's consultants which merit consideration. Most of these matters were considered in the GAO Report (identified *supra* at p. 11, fn. 8) and GAO generally agreed with the conclusions of NCPA's consultants. The Secretary of the Interior has never made any finding with respect to the matters raised by NCPA and we do not know the basis for the refusal to accept the evaluations, judgments, conclusions and recommendations set forth by NCPA's experts. Among the more important of these issues are the following:

(a) NCPA's consultants disagree with the appropriateness of the novel criterion, never previously imposed by the Bureau, that the rate to be established must be high enough to cover all costs, including costs for future projects, in each and every year beginning in 1977 until the year 2031, regardless of whether any costs in a given year are unusual or non-recurring. This criterion was inconsistent with applicable Bureau instructions and with reclamation laws.

(b) NCPA presented evidence indicating that hydroelectric data used by the Bureau is invalid and that the amount of available energy and the related revenues were understated. Although the rates announced on November 1, 1973 are based on an upward adjustment for hydrology to the data originally used by the Bureau in its May 28, 1973 rate proposal, the full adjustment recommended by NCPA was not adopted.

(c) NCPA offered expert testimony that the rates are based on accounting for replacements in a manner which is contrary to Bureau instructions and inconsistent with sound engineering, accounting and economic principles.

(d) NCPA offered expert testimony that the rates improperly, and contrary to sound business principles, are inflated because of a failure to capitalize properly interest on new plants during the period of reservoir filling prior to the time they are fully useful to produce revenues.

(e) NCPA's consultants indicated that it was unreasonable for the Bureau to assume a drastic change in CVP power marketing after the year 2004.

⁹ "Order Granting Motion for Extraordinary Relief and Instituting Investigation", *Pacific Gas and Electric Company*, FPC Docket No. E-7777, issued March 14, 1974.

(f) The rates as proposed, according to the Bureau's own studies, would produce a surplus of \$579 million over the repayment period studied. Such a huge surplus is unprecedented, unwarranted, and contrary to reclamation laws.

These substantial issues all merit careful attention by an independent body, such as the Federal Power Commission, which would evaluate the testimony of witnesses presented by NCPA and others versus testimony which would be required, for the first time, from Bureau of Reclamation and Interior Department personnel.

Mr. McDIARMID. Thank you.

As you all have heard in the past, the problem is really one of due process. There is very little quite as complicated as a major rate increase of an electrical system. We appeared at the so-called public hearing in Sacramento, of which you will be receiving a transcript, prepared to ask questions, prepared with a rather detailed case of our own. We are told that, no, they would listen to what we had to say, maybe, but we couldn't ask them any questions to find out what in fact they had assumed.

Now, we have never found out why it is the Interior doesn't believe we are entitled to the ordinary requisites of a hearing. Interior has never said, although there has been a good deal of discussion around the subject. The problem is that a rate increase this major for cities of this size is really the sort of thing that must be justified to the customers or the citizens of these cities who will eventually pay this bill. It is very hard, as Mayor Gillmor has pointed out, to tell them Interior says this is what we should pay, and although we believe that is way over anything that is just or reasonable, Interior says it and we can't have a hearing and they won't listen to what we have to say and that is just basically what it comes down to.

For this reason we are strongly in support of this bill. The Federal Power Commission deals with issues of this sort every day. It deals slowly, but eventually it gets around to it. It is a place where there is expertise. It is a place where there is at least a provision for a hearing and a place where we can put on our testimony and cross-examine the Bureau's witnesses. We don't object, obviously, to paying a rate increase that is justified. All costs vary. Sometimes they go up, sometimes they go down. We do not object to paying a higher rate if the costs haven't gone up if it can be justified on any kind of a fair basis. We don't think that is the case here. Mr. Westfall, the engineer for the power agency in the cities, will testify in a little more detail about why it is that we don't think these rates can be justified.

Now, the sum and substance of it all really is that there must be a way in which a proposal of this nature can be tested, and really the hearing procedure, a fair hearing procedure, is the only mechanism which is available to that end, the mechanism which Congress has determined in 1935 to be applied to electric utility sales for wholesale in the Federal Power Act. It is a method which Congress decided in 1938 would be applied to gas pipeline transmission rates in the Natural Gas Act.

It really is the only method which appears to be fair, and which can be turned to in a situation like this where there are numerous questions of fact, and for that matter, a few of interpretations of law as well. If you can't have a hearing you are left where the fate of the cities and their citizens really hangs in the balance and in the hands of unnamed persons in the Department of the Interior. This is why we believe this bill is an appropriate means for a resolution of this problem at this time.

Now, section 6 of the bill goes on to provide that in the future for future rate increases the Secretary shall develop procedures for a hearing mechanism for determining rates. We think that would be a perfectly acceptable means for resolving the problem. We agree with Mr. Richter it should be clear if it is not clear now, that there be review in court of the decision which the Secretary would make, and if it turns out that the decisions which the Secretary makes are in the nature of the decisions which he has made so far, which we think are unjustifiable and certainly unwarranted on the basis of the process which he has afforded to the customers, we would then think it might be appropriate to make the Federal Power Commission's review into a permanent kind of thing.

Thank you.

Mr. JOHNSON. Well, thank you for your summary of your statement. I see your statement is quite complete with many references to matters of great concern to all of us. Naturally we will go through your statement very carefully as well as having it printed in the record. But I think you have covered pretty near everything in there.

Now, as I understand you to say, the method that was used as far as the Government was concerned in offering hearings on the matter was not adequate because there was no chance to ask any questions nor cross-examine the witnesses, is that right?

Mr. McDIARMID. Mr. Chairman, I should say that the only really adequate kind of a hearing in the contentions that is under by all lawyers I guess is that there be some knowledge in advance of what the other side's basic position is and that there be some method for eliciting the truth, especially when it is a question of fact that are at the issue. The basic assumptions underlying the result that what the opposing party comes out with are frequently most important. We have never been able to find out what many of these basic assumptions are. There has been no opportunity for cross-examination or really for questioning of any kind. The "hearing," in quotes, which has been offered, was nothing like a hearing that any lawyer would recognize.

Mr. JOHNSON. Well, I think you will admit this being a very technical matter, it takes very technical people to participate in a proper hearing, both from the standpoint of engineering as well as financial experts. In any type of rate hearing, both sides are heard and cross-examined. Finally they arrive at a just increase to be allowed. In your opinion this was not done?

Mr. McDIARMID. Not at all. We tendered our witnesses for cross-examination but were unable to obtain cross-examination of the Secretary's witnesses.

We did, I should say, present a quite substantial case at that time in view of the fact that we didn't know very much about what the Secretary was doing and were unable to find out very much about what his assumptions were. We did present a fairly substantial case at that time. We have since that time supplemented it, but we have been unable to obtain anything like what we presented from the Secretary. It is rather difficult to find out.

Mr. JOHNSON. Well, we want to thank you for your participation. You will remain for questions.

Our next person is Mr. Westfall, the managing partner from R. W. Beck & Associates who are under contract with the Northern California Power Co.

Mr. WESTFALL. Mr. Chairman, members of the committee, my name is Herbert Westfall and I appear here in behalf of the Northern California Power Agency (NCPA). I am managing partner of the consulting engineering firm of R. W. Beck & Associates. Our firm has been retained by NCPA and by cities in northern California who are members of NCPA, to advise and perform studies with respect to power supply and other matters.

My statement is in two parts, a detailed statement and a summary which I will excerpt into the record with your permission, Mr. Chairman.

Mr. JOHNSON. Your full statement will appear in the record as submitted, both one and two, and you may summarize one and two.

Mr. WESTFALL. Thank you.

I might say, Mr. Chairman, that Mr. Norman Hill, my associate and engineer also, who has worked with me on the northern California agency studies, is here, and both of us will be available for questions should you so desire.

We have reviewed all data made available to us by the Bureau and have undertaken detailed independent studies with respect to the rate increase to Central Valley project preference customers. Based upon our detailed review and studies and upon advice of counsel to NCPA with respect to certain matters, it is my opinion that, if the Bureau can recover the full allocated cost of Centralia capacity being sold to P.G. & E. under rates charged to P.G. & E., no rate increase to Central Valley project preference customers is required or can be justified at this time. Our studies indicate that an increase of approximately 14.5 percent may be required in 1977. If I might digress, Mr. Chairman, a copy of the detailed report has been made available to the staff for its review and for the files of the committee. It is quite an extensive report, and I have left a copy with the staff for its further study.

The Central Valley project is in a strong financial position. As of June 30, 1973, the total Federal investment chargeable to power was \$236,830,000. Of this amount, nearly \$205 million, or 87 percent, has already been repaid and the remaining 13 percent is not required to be repaid until 2023. Notwithstanding this excellent financial condition, Interior has increased rates to its preference customers by more than 50 percent. The increase is a two-step increase, the first step which became effective April 1, 1974, was approximately 25 percent, or about \$6 million annually. Beginning January 1, 1977, the increase is to become more than \$13 million annually. The Bureau studies which purportedly provide the basis for the increase are based upon criteria which are not consistent with those used for other Federal power-marketing agencies and, in fact, are not consistent with the Bureau's own adopted guidelines:

1. The Central Valley project study proposals would subsidize the cost of power sold to P.G. & E. through increased rates to preference customers.
2. Bureau criteria for Central Valley project, that the rate now established must be high enough to cover all costs, including costs for future projects, in each and every year from 1977 through 2031, are not consistent with applicable Bureau instructions and are inconsistent with reclamation laws.
3. The stated need for \$579 million surplus has not been and cannot be justified.

4. Accounting for the cost of replacements is contrary to Bureau instructions.

5. Full interest charges for certain Central Valley project additions prior to their full operation unrealistically inflate the amount of the rate increase as now proposed by Interior.

The rate increase which was placed in effect April 1, 1974, serves only the purpose of collecting from one class of customers—the Central Valley project preference customers—for losses on sales to another customer—Pacific Gas & Electric Co.

The loss in power sold to P.G. & E. during 1974, 1975, and 1976 will be about \$19,373,000 and the increase, which Interior would impose on its preference customers during that same period is nearly \$14 million.

The criteria used by the Bureau in its studies to the effect that the rates must be sufficient in each and every year to cover all cost of the Central Valley project, including interest costs assignable to existing projects and for new projects, is not consistent with accepted rate-making principles.

The “pinch-point” year of 1982 used in the Bureau repayment schedules for the rate increase to preference customers includes, as operating costs and/or deductions from net revenues, items which have been arbitrarily added and for which alternative assumptions and criteria could have been used which would result in lower revenue requirements in 1982 than those shown on the Bureau repayment schedule.

The Bureau repayment schedule reflects full interest charges for the New Melones, the Auburn, and the Marysville projects beginning as of the date construction is completed; however, the full output—and, therefore, the full revenue-producing capability—is not realized for a number of years while the reservoirs are being filled.

If interest is charged in each year only in direct proportion to the percentage of project output actually realized and the remainder is capitalized—a procedure commonly used by utilities—the 1982 “pinch-point year” revenue requirements could be reduced by \$3,568,000.

Interior issued instructions on August 2, 1972, directing Federal power agencies to capitalize replacement costs by June 30, 1973. The repayment schedule dated November 12, 1973, which reflects the promulgated rate increase, does not capitalize replacements. If replacements were capitalized, and interest charged thereupon, the 1982 “pinch-point year” revenue requirements could be reduced by \$341,000.

The assumption used by the Bureau in its studies that the Central Valley project will purchase Centralia power throughout the 1982 “pinch-point year,” arbitrarily and severely overstates the revenue requirements in that year. During the last 6 months of fiscal year 1982, the Bureau studies reflect a cost of approximately \$13,228,000 to purchase Northwest power. The present Centralia purchase arrangements will terminate on December 31, 1981, unless extended by mutual consent.

There is serious question as to the availability of power from the Northwest in 1982, and the Bureau has an alternative source available to it which is lower in cost. The Bureau can repurchase from the bank accounts established with P.G. & E. pursuant to contract No. 2948A. Had the Bureau assumed that it would repurchase from the bank ac-

counts in 1982 rather than purchase Centralia power, the 1982 "pinch-point year" revenue requirements would be reduced \$5,238,000.

In other words, the revenue requirements—and consequently, the rate level—used in the Bureau studies could have been reduced, by adopting alternative assumptions for the foregoing three criteria, by \$9,147,000 for the 1982 "Pinch-point year."

The foregoing are illustrative of the deficiencies in the Bureau studies which provided the basis for the rate increase to Central Valley project preference customers. Clearly proper review of the Central Valley project rates by the appropriate agency and opportunity for meaningful review and comment by the customers who are being asked to pay the increased rates is needed.

Further detail concerning this statement are included in the detailed statement that will be prepared to answer any question this committee may have.

Mr. Chairman, I thank you for the opportunity to make this statement.

Mr. JOHNSON. You have given us a very well documented summary of what we are confronted with.

Let me ask this: In arriving at the figures throughout the statement, were those figures gathered from information that has been made available to you by the Bureau of Reclamation or did you secure the information from outside sources?

Mr. WESTFALL. Largely from information obtained from the Bureau of Reclamation. We submitted numerous requests for specific information. When we made requests for specific information it was in most instances provided to us in a timely manner, but we had to make the requests for specific items of information.

Mr. JOHNSON. Now, in dealing with the Bureau of Reclamation did you have consultation with various officials representing the Bureau of Reclamation?

Mr. WESTFALL. Yes, we met with the Bureau officials on a number of occasions specifically for the purpose of soliciting and obtaining information. We discussed the conclusions which we reached with them, our report, a copy of which was made available to your staff dated August 31, was presented to the Bureau. We have not had meaningful discussions concerning our report with the staff. The report was submitted to the best of my knowledge. That has not been fully taken into consideration in the promulgation of the rate.

Mr. JOHNSON. Well, now, explain to me just a little bit about the pinch-point year of 1982. What does that relate to?

Mr. WESTFALL. One of the criteria, as I understand it from information supplied by the Bureau, I'm informed, for the Central Valley project, was that there should be no deficit in any year throughout payout period. They do show a deficit in their repayment schedules, those dated November 12, 1973. They show nominal deficits in 1974 and 1976. However, beginning in 1977, one of the criteria was, as I understand it, that there was to be no deficit of any costs, including interest costs, and that there would be some repayment of principal in every year throughout the repayment period extending to the year 2031. In the year 1982 the cumulative costs of all factors, including the repayment of full costs under the Auburn-Marysville project the New Malones project, plus the purchase of continued Centralia power

which they assume Northwest power purchases in 1982 cascading to a peaking of costs in that year. That year, then, was the year that was the most critical year from a revenue requirement standpoint and consequently was used as the basis for establishing the rate.

Mr. JOHNSON. Fine.

Now, in reality the New Malones project probably will not come on line until after 1982, and I would say the Auburn project will not come on line anywhere near 1982. And Marysville isn't off the ground yet. It was authorized in 1962 but has been in limbo ever since. There is very little activity on Marysville. So I would say that is a good 20 years away.

Now, as you said in your statement, it would be cheaper to buy power from other sources beyond 1982 as far as the Bureau of Reclamation is concerned. Where would you get that?

Mr. WESTFALL. Well, at the present time the CVP is banking substantial amounts of energy and it is banking very large amounts of capacity with Pacific Gas & Electric Co., under the provisions of the Centralia P.G. & E. contract. That contract provides for the repurchase by the Bureau of that energy from the bank under rates, terms, and conditions in the contract. The contract also provides in the event that after the complete removal of all the power that is in the bank that energy can be purchased from P.G. & E. to make up any needed energy requirements for preference customer loads.

The capacity that flows into the banks as our studies show and as testified to in other hearings, is never recovered. There is an excess of capacity in the banks. That capacity is never going to be used or required to meet the Bureau's preference customer loads throughout the term of the present contracts which extend to the year 2004. Our studies certainly assume that the project, New Melones, Auburn, would come on line under the schedules indicated by the Bureau. We had no information to indicate otherwise. I am sure these projects are sound projects and will contribute materially to the Central Valley project. My point was that in 1982 the assumption that the Bureau would purchase power from the Northwest at an annual cost of some \$26,420,000 for the 400,000 kilowatts of power which is actually substantially more power than required in that year. So we are continuing to bank, virtually the entire amount of capacity and a significant part of the energy in that year.

Mr. JOHNSON. I realize that, I watch the appropriations process. The rate that we are appropriating funds for the three projects, the target date of 1982 is not real at this particular time, I would say. I doubt whether any of the three of them will be on line by 1982.

Now, there is a remote possibility that Melones will come through and be on line. The main structure, the dam itself, is under contract. Again this year they did not or have not recommended appropriations to meet the contract capabilities. So this could string that out a little bit. Then the main item there at that project, the powerhouse has not been advertised nor awarded at the present time. That is the key to the success of that project. As it is a carryover reservoir, it might be sometime in filling in order to meet its capabilities. So I would say that New Melones is questionable. We are now confronted with another harassment out there, an initiative being proposed for the November ballot to halt construction again. The New Melones project has

gone through all the courts, the district court and the court of appeals and the Supreme Court. They have finally settled the issue that the environmental impact requirements have been met and the contractor is on the job at the present time. Now we have the initiative movement underway in California and what effect that will have on it is more than I can say at this time.

On the Auburn project we are in the courts now, as you people know. The same charge is being made that the environmental impact statement is not complete. The district judge has given the Bureau of Reclamation until November 9 or 10 to comply with certain requests for information involving the environmental impact statement. Hopefully the Bureau will be able to satisfy the judge's request for information.

But here again we are confronted with maybe an appeal to the circuit court of appeals and on to the Supreme Court. And if the other initiative movement is successful, Auburn faces the same thing.

We are just barely getting started. The bids were opened last Tuesday and they called for the coffer dams and Keyway excavations, which is just barely getting into the bottom of the river. Hopefully we will award that contract and order the contractor onto the job under the cloud of what may happen on September 9 or 10 and then they may go ahead. Here again the funding is inadequate to even allow that money to round out the start of the contract from the bottom of the river. It is deficient in the amount of recommended appropriations to allow that contractor to get started. We are hopeful that the Appropriations Committee of Congress will give us an add on to allow the necessary funds—to allow that contractor to go to work and have it funded out to meet his capabilities.

So the Auburn is delayed and delayed and delayed. I would say it is 6 years delayed now from its original start and I don't know how much more delay we will experience there. Then we go to Marysville and that has never gotten started. It is in a restudy stage now with a requirement that they meet the new discount rate and it is very questionable whether the project will have a favorable benefit-cost ratio. So I think the pinch-point of 1982, other than the Centralia considerations is not valid.

Now, it has been my thinking that the project is in pretty good financial condition now, that is the Central Valley project, and there could be an extended period of time with present rates. Later, if we are faced with certain increases, I think that proper study of those rates will show them to be much less than we now anticipate them to be.

These are hard things to come by, but looking at all of this, I agree with you people that the proper hearings were not held. I think some of the things that were taken into consideration by the Interior Department and Bureau of Reclamation were wrong. I would agree maybe there should be some increase somewhere along the line, but we have always been led to believe that the Central Valley project was pretty sound financially. Our people are unable to understand why we are faced with this increase by 1977.

Mayor GILLMOR. Mr. Chairman.

Mr. JOHNSON. Yes, Mayor.

MAYOR GILLMOR. Mr. Westfall has stated that about the gathering of information and what we came up against. I think if you return to that meeting in Sacramento which they called a hearing, and you are seeking the records of that, you will note at the end of the hearings when you look over the record I had asked what type of procedure would be used, where do we go and how do we react and we don't have all the information to react to. At that time Mr. Hammond stated he could not state policy from Washington, D.C. He did not know exactly what would follow. This left us in a situation we didn't know where to follow. We didn't know what to ask for. In turn we were in a situation where we were lost. That is totally ridiculous. Maybe some of our information might be erroneous and possibly that could be correct, but we went on good faith. We think all of our information, especially what our consultants have presented is correct, but I think the committee ought to totally realize that we did it, only not getting voluntary information, but information only given to us if we knew what we had to ask for, and again as an elected official I think this is totally ridiculous.

MR. JOHNSON. I might say in regards to your last statement there, we became involved with this when we were notified of the first inquiry. Many of us got into this and tried to do our level best to allow the preference customers and their representatives, both legal and engineering personnel, to have free flow of information, especially after the Sacramento hearings. We met and made our positions known to the Bureau of Reclamation and Department of Interior on two different occasions. I think finally there was a loosening of information upon request, and the materials were furnished. That is why I ask the question here, you people have received this information from the Bureau and you have had an opportunity to discuss the various matters of concern with the Bureau personnel. You said yes.

MAYOR GILLMOR. Well—

MR. JOHNSON. I was asking about what he has in his paper. That being particular matters of concern to you. Now, I know there are voluminous records and reports and decisions and information in the hands of the Bureau of Reclamation within the Department of Interior that you have not had an opportunity to review. As I understand it, your support for the legislation is to have this material placed on the record. Then whatever the record would show would be the agreed upon amounts to be charged; is that it?

MAYOR GILLMOR. We agree with everything you have stated, Mr. Chairman, with regards to reasonable increases, inflation, and other factors, but I think we have every right in the world to see the documentation. That is all we are requesting and that is all this bill as far as I see it—and I think candid discussion about Marysville and Auburn and others and how someone can key them on, we are supposed to come on on a certain date, we know it isn't going to come on. Also they are gearing in a rate for decades with regard to costs. With regards to one geothermal and the possibility of geothermal, Santa Clara went on record authorizing \$1 million to bid on Federal lands to integrate into the Centralia project and to get into the bid process, and cities are going to join with us to do that. There are so many changing situations and I don't see how you can be obligated for decades on the pinch-point after your candid discussion with regard

to Marysville and the other projects in California. I think we have to sit down and be reasonable men, expect reasonable increases, but also reasonable information so we justify our action and that of the Federal Government. This is why H.R. 14221 is extremely valuable to the people of California.

Mr. JOHNSON. The gentleman from New Mexico, Mr. Runnels.

Mr. RUNNELS. Thank you, Mr. Chairman.

I would like to request for the file that we receive a copy of the P.G. & E. Contract Number 2948A. The reason I make this request is that the Bureau can repurchase from the bank accounts established under this contract, and may I ask a question before the request is acted upon?

Mr. JOHNSON. Go right ahead.

Mr. RUNNELS. Was any reason given to you three gentlemen—and I want to congratulate all three of you on your testimony—as to why the preference customers were asked to underwrite the loss of the electricity to be sold to P.G. & E.? Is there any real concrete evidence as to why your customers in the preference category were asked to underwrite a loss of \$19 million?

Mr. WESTFALL. If I may, there is a representative from Pacific Gas & Electric Co., extremely familiar with that contract and they may wish to further answer.

It is my understanding that the principal reason why no increase was proposed to Pacific Gas & Electric Co., prior to April 1, 1976, was that their contract has a review provision in it—a 5-year review provision in the contract. The rates were subject to review in April 1971. No review was undertaken, or if at least so undertaken it was never made a matter of record and no change was made in 1971. It is my understanding that because no change was made in 1971 that the Bureau took the position that a change could not be made until April 1976. That is my understanding.

As I say, there is a gentleman from Pacific Gas & Electric Co., who may wish to comment further.

Mr. RUNNELS. May I ask a further question. Is there any connection between P.G. & E. and Pacific Power & Light Corp., as to who gets certain sources of any power that you know of?

Mr. WESTFALL. I would defer that question to the gentleman from Pacific Gas & Electric Co.

Mr. RUNNELS. All right, sir.

Mr. Chairman, the opening statement where it was stated that we will not answer questions, I fully can see the need to set up an orderly procedure. I have poured over their complete statement, and I still believe that this bill could be amended and be of great help not only to people of California, but the whole United States where people have their say in an orderly manner on time consuming information provided by the Bureau.

Mr. JOHNSON. Did you make that request for the contract?

Mr. RUNNELS. Yes.

Mr. JOHNSON. You have heard the request of the gentleman from New Mexico asking for a contract between the Pacific Gas & Electric Co., and the U.S. Government be made part of the files.

Is there objection?

Hearing none, so ordered.

Mr. McDIARMID. We can furnish that.

Mr. JOHNSON. The gentleman from New Mexico. Mr. Lujan.

Mr. LUJAN. No questions, Mr. Chairman.

Mr. JOHNSON. The gentleman from California, Mr. Ketchum.

Mr. KETCHUM. Thank you, Mr. Chairman.

Mr. Chairman, I am wondering if the witnesses have copies of the letter from the Department dated May 16, 1974 and from the Federal Power Commission dated May 16, 1974?

Mr. McDIARMID. We do now, sir.

Mr. KETCHUM. You will note in both instances the Federal Power Commission and the Department of the Interior are opposed to the bill. I can understand the Department of Interior's opposition which is probably somewhat parochial. The Federal Power's opposition does concern me.

I am wondering, Mr. Chairman, if perhaps these gentlemen could reply to this letter for the record or the file at some future point?

Mr. JOHNSON. You have heard the request of the gentleman from California. Is there objection?

Hearing none, so ordered.

If you will furnish that, gentlemen.

Mayor GILLMOR. Yes; we will.

Mr. KETCHUM. I really have no further statement, Mr. Chairman, or further questions, except to say that I, too, share the gentleman from New Mexico's concern and really these gentlemen's concern for open public hearings. Perhaps this bill is not the solution, but certainly some system has to be set up where public information or public questions, good, valid, reasonable questions can be interjected into any of these determinations. I further would like to state on behalf of Mr. Dillon—I didn't have the opportunity to do it earlier—I had the pleasure to reside in that area during the period of time I resided in the California legislature, and I heard many people complain from time to time about SMUD and I certainly hope some reference will be made in the local newspapers as to SMUD's efforts on behalf of their customers, because I think it is commendable on their part.

Mr. JOHNSON. The gentleman from New Mexico would like to pick up his time?

Mr. LUJAN. Yes, Mr. Chairman.

I would like to get back to the basic question that has prompted the introduction of this. I don't mean the specific rate increase, but perhaps the overall way of doing it. Your criticism is the same as we have heard, that you didn't get an opportunity to have input into it. Mr. Stamm from the Bureau of Reclamation stated that perhaps continuing in the same system but giving veto power to the Federal Power Commission might be an acceptable way of doing it; what is your opinion?

Mr. McDIARMID. Well, sir. I think our basic problem here, and you will pardon me for putting it this way, but I practice a great deal before the Federal Power Commission. We see problems of this kind of cost justification all the time. The basic problem here, I think, and what really is so appalling to the citizens of the cities here involved, is that under the procedure which has been set up at the Federal Power Commission, which works slowly but eventually works, you can get a lot more information, a lot more justification, from privately

owned utility companies which are in their very nature out to make a profit for their stockholders, a lot more rationale of a decision, and your views can be taken into account by the FPC. You get a lot more of that in that kind of a situation than we have gotten here with the Bureau, ostensibly a Government agency designed for supplying and working with these preference customers.

The problem, I think, is that the format which Interior has set up here of hearings that aren't hearings, of decisions but really a press release, are not in any way, shape, manner, or form, justified or attempted to be justified on their own terms.

Mr. LUJAN. What you are saying is that we need to go to the full-blown hearing before FPC rather than the veto power review and then subject to their approval?

Mr. McDIARMID. Basically, I think so, sir. It need not necessarily be before the FPC. Before you came in, I commented on section 6 which directs the Secretary to set up a procedure for hearings in the future. If there is a procedure for hearings on the record, and thereafter a procedure for judicial review, that really ought to be satisfactory if it is operated on in good faith.

Mr. LUJAN. You say not necessarily before the FPC. In your judgment, with the considerable experience that you have had, would it be better to set up a procedure within Interior or have it done before the Federal Power Commission?

Mr. McDIARMID. In terms of administrative feasibility, sir, I think it would probably be better to have it set up at the FPC. Now, we also don't want to ruffle too many feathers at Interior—

Mr. LUJAN. If you want to do it as efficiently as you possibly could, if you had to make that determination, where would you put it?

Mr. McDIARMID. Probably the FPC.

Mr. LUJAN. Thank you.

Mr. JOHNSON. Our consultant, Mr. Casey, has a question of the witnesses.

Mr. CASEY. Gentlemen, it seems to me we have two problems here. We have the one of how we will operate in the future, and we have the other one about what has already happened. There are two separate distinct problems, and they lend themselves to different statutory treatment.

Now, to allude back to Mr. Lujan's question and perhaps fill you in because you were not here on Friday when we had the executive branch with us in for lengthy testimony and questioning. Bearing in mind that this committee has more to overview than the Bureau of Reclamation, there may be some requirement for the committee to bring out a bill that would standardize Interior power marketing rather than diffusing it even more than it already is. Now, with that little preamble, I would call attention that the other marketing agencies operate under a law passed in 1944, that does convey a certain FPC overview. Are any of the gentlemen familiar with that?

Mr. McDIARMID. Your Honor—

Mr. CASEY. I am not a "your Honor."

Mr. McDIARMID. Everybody who sits on that side is "Your Honor."

I was assistant to the general counsel for a number of years for the FPC when the FPC did nothing under those statutes except watch occasional statutes go by. I am sure you are aware that there have

been a couple of court cases which have arisen out of that kind of perfunctory review, and have generally so far gone adversely to the Department of the Interior and the FPC. We are aware of the statute and the FPC's general inaction under that.

Mr. CASEY. Would a requirement of law that would submit the Bureau of Reclamation power ratemaking procedures to the same requirements that already exist with respect to Bonneville and the others, furnish you the security that you would like to have in this instance?

Mr. McDIARMID. It would be better than now exists. I would not think that would be totally desirable, because although the statute is written in such a fashion as to give the FPC the authority to provide the kind of review for which we have asked and are asking here, the history of the practice under that act has been that essentially the FPC watches it go by without taking into account protests or without giving any kind of hearing.

Mr. CASEY. That is very interesting, because you know the FPC does not come under the legislative overview of this committee.

Mr. McDIARMID. Yes.

Mr. CASEY. And we, therefore, are not aware of that. Perhaps the committee might better preserve its jurisdiction by establishing a totally new mechanism for this purpose instead of referring it to FPC. I gather you wouldn't consider that inappropriate?

Mr. McDIARMID. No, sir. There should be some mechanism.

Mr. CASEY. All right.

One other thing. Mr. Westfall, you estimated about \$9 million of revenues for the pinch-point year arising out of three bad assumptions, if we might call them that. Have you estimated the amount of rate increase that would have been justified if the pinch point would have been reduced by the first amount tabulated, that being \$3½ million reduction in interest requirements due to capitalization of power costs? Have you expressed that in terms of a rate increase?

Mr. WESTFALL. No, no I have not.

Mr. CASEY. Could you guess one for me?

Mr. WESTFALL. If the cost assignable to interest on Auburn-New Melones projects were deferred, and understand that the \$3½ million of reduction in revenue requirements relates to certain stage of reservoir filling for New Melones, for example, all of the project would have been completed, completed in 1969, start filling, and up to its capability by 1982, some very little deferred interest on the New Melones project. So that substantially all of it related to the Auburn-Marysville project.

Now, if both projects were delayed the figure would be above the \$3.5 million that I mentioned in my testimony, but relating the \$3.5 million to the roughly \$13 million total increase projected for the year 1981-82 as I recall from the Bureau's figures, that would indicate that roughly 25 or 30 percent of the rate increase, that would factor in at about 13 percent of the rate increase in 1982, could be alleviated by that one factor. In other words, the rate increase of roughly 50 percent would have been in the order of 35 to 37 percent.

Mr. CASEY. What I am toying with here is the practical problem of drafting statutory language that would mandate, perhaps, retroactive adoption of some of what you assume to be more reasonable

criteria. I am assuming that rolling it into the Federal Power Commission may or may not give you any relief, even if the bill is passed. There is no assurance of that in any sense of the word.

Thinking in those terms, just how many of these things might indeed be manageable in statutory terms. I want to get some feel for their absolute significance.

I thank you, Mr. Chairman.

Mr. WESTFALL. Mr. Chairman, may I comment on Mr. Casey's earlier question that was answered in part by Mr. McDiarmid?

Mr. JOHNSON. You may.

Mr. WESTFALL. Relating to specifically the references to Bonneville, I would suggest to the committee here that Bonneville works actually very effectively. I happen to live in the Northwest and am very much acquainted with the procedures used by Bonneville. They will promulgate a new rate and there will be substantial rate increase in Bonneville this fall. They have for the past year been meeting extensively with the customers. They had a full meeting of the Bonneville Regional Council of which I happen to be a member. There are perhaps 300 to 400 people throughout the Northwest in all segments of industry on that council. Bonneville historically has discussed its rate changes. That has gotten input. It has held hearings, but they have been very informal, but there has been a full communication. We did not see that in the instance of this rate increase. If we had assurances that that would take place then perhaps there would be merit to following that same procedure, but with the history we have had on it, I would strongly support Mr. McDiarmid. If you can get the information you can do the studies and communicate, but we had a difficult time getting it.

Mr. JOHNSON. Thank you for your appearance here, gentlemen, and your responses to the questions.

[Mr. Westfall's statement in full follows:]

STATEMENT IN BEHALF OF NORTHERN CALIFORNIA POWER AGENCY,
BY HERBERT C. WESTFALL

The statement presented herein summarizes data and conclusions developed by R. W. Beck and Associates in behalf of Northern California Power Agency (NCPA) in the matter of the power rate increase promulgated by the Department of the Interior (Interior), Bureau of Reclamation (Bureau) for the Central Valley Project, California (CVP). These data and conclusions and testimony related thereto were also presented in the response submitted on January 22, 1974 to the Conservation and Natural Resources Subcommittee of the House Committee on Government Operations in connection with its Hearing on the above-referenced rate increase. I respectfully refer the committee to the testimony and response, including our "Report on Central Valley Project June 1973 Power Rate Adjustment Study" which was submitted to the Bureau on August 31, 1973.

The firm of R. W. Beck and Associates has been retained from time to time since 1965 by certain cities in northern California, who are members of NCPA, and by NCPA to advise and perform studies with respect to power supply and other matters. The firm is presently retained by NCPA to advise and assist in behalf of NCPA members—Palo Alto, Santa Clara, Redding, Roseville, Biggs and Plumas-Sierra Rural Electric Cooperative—in the matter of the proposed CVP wholesale rate increase. We have analyzed the rate proposals in this proceeding and presented evidence to the Bureau.

R. W. Beck and Associates is a firm of professional consulting engineers, planners, economists and analysts providing a complete range of professional services to utilities throughout the United States and abroad. The firm was

founded in 1942 at Seattle, Wash., and continues to maintain its general offices at Seattle with additional offices at Denver, Colo., Phoenix, Ariz., Columbus, Nebr., Orlando, Fla., Boston, Mass., and Indianapolis, Ind.

My personal professional qualifications are attached hereto as Exhibit A. These qualifications enable me to offer the facts, opinions and conclusions herein set forth in behalf of NCPA.

INTRODUCTION

The Central Valley Project is a multipurpose water reclamation project serving California's Central Valley which is administered by the U.S. Bureau of Reclamation, Department of the Interior. Its facilities are used to supply water, control floods, protect and enhance river fisheries, deliver low cost electric power, provide recreational opportunities, maintain navigation, and protect water quality. Among the project's major facilities are nine electric generating plants which have a capability of 1,471.2 megawatts (based upon information furnished to us by the Bureau). In addition, the project imports 400 megawatts (less losses) of power from the Pacific Northwest area from the Centralia coal-fired steam-electric plant at Centralia, Wash., under a unit power contract with the owners of that plant. That power is transmitted over the Northwest-Southwest Intertie using capacity reserved for the Bureau.

In 1972, commercial power sales from the CVP totalled 6,863,265 megawatt-hours while the project itself used 1,005,497 megawatt-hours. Of the energy sold in 1972, 5,256,345 megawatt-hours were sold to preference customers and 1,606,920 megawatt-hours (23.4% of total sales) were sold to Pacific Gas and Electric Company (PG&E). Total revenue from sales of power was \$31,696,721 in 1972. As of June 30, 1973, the total federal investment in the CVP chargeable to commercial power was \$236,830,000 of which \$204,909,710 has already been repaid, leaving an unpaid balance of only \$31,920,290. In other words, 87% of the investment has been repaid, and the remaining 13% is not required to be repaid until the year 2023. Notwithstanding this excellent financial position, Interior proposes to increase its rates to preference customers by more than 50%. In its proposal announced on May 28, 1973, the Bureau proposed a single step rate increase of 51.6% effective January 1, 1974 to preference customers based upon studies presented in its June brochure (June CVP Study). The rate increase, as announced by Interior on November 1, 1973, is a two-step increase. The first step, which became effective on April 1, 1974, was to increase rates to preference customers by about \$6 million, or approximately 25%. Beginning January 1, 1977, that increase is to become more than \$13 million annually, or essentially the same 50% increase which Interior proposed in June. In other words, the proposal announced by Interior on November 1, 1973 did not materially change the earlier proposal except that a portion of the increase would be delayed until January 1, 1977. However, even during the period in which some relief was accorded (April 1, 1974 to January 1, 1977), the rate increases to preference customers would amount to more than \$16.8 million. During substantially all of this same period (to April 1, 1976), PG&E will not pay any increase according to the Bureau's own study (November CVP Study). At the same time, PG&E receives a substantial amount of project capacity for which it pays nothing.

CVP has present capability of more than 1,800 megawatts. Of this capability only 925 megawatts is currently being made available to preference customers. Some of the remaining capability is used to supply CVP pumping requirements and the balance is available to PG&E.

Based upon our detailed studies and upon advice of counsel to NCPA with respect to certain matters, it is my conclusion that, if the Bureau can recover the full allocated cost of Centralia capacity being sold to PG&E under rates charged to PG&E, no rate increase to CVP preference customers is required or can be justified at this time.

Both the June CVP Study and the November CVP Study are based upon criteria which are not consistent with adopted Bureau guidelines, contractual requirements and conditions now existing or which may be expected to exist on the CVP system in the following respects:

1. The CVP study proposals would subsidize the cost of power sold to PG&E through increased rates to preference customers.
2. Bureau criteria for CVP, that the rate now established must be high enough to cover all costs, including costs for future projects, in each and every year from 1977 through 2031, are not consistent with applicable Bureau instructions and are inconsistent with reclamation laws.

3. The stated need for \$496 million surplus in the June CVP Study and the even greater \$579 million surplus in the November CVP Study has not been and cannot be justified.

4. Accounting for the cost of replacements is contrary to Bureau instructions and is not consistent with sound engineering, accounting and economic principles.

5. Energy output of the CVP system, understated by approximately 10% in the June CVP Study, continues to be understated in the November CVP Study, but by a lesser amount.

6. The CVP studies undervalue CVP output after 2004.

7. Full interest charges for certain CVP additions prior to their full operation unrealistically inflate the amount of the rate increase as now proposed by Interior.

Interior has promulgated rates which are based on criteria, as above noted and as more fully discussed hereinafter, which are arbitrary and are not consistent with accepted rate-making principles used for other federal projects. The preference customers of CVP, upon whom the rate increase is imposed, have strenuously objected to the rate increase and have pointed out the deficiencies in the Bureau studies. Their objections and the data presented in support thereof were not given reasonable consideration by Interior prior to its adoption of the rate increase. A complete and independent review of the CVP rate increase is essential if the interests of the preference customers and the federal government are to be fully protected.

FINANCIAL POSITION OF THE CENTRAL VALLEY PROJECT

The unpaid balance of the CVP at the end of fiscal year 1973, was \$31,920,290 on the total federal investment charged to commercial power of \$236,830,000 (as shown in columns 30 and 31, respectively, on the payout schedule in the June CVP Study), which clearly demonstrates that the CVP is in good financial condition. This federal investment has been paid off much more rapidly than is required under established payback procedures for federal projects. Almost 87% of the current investment has been paid and the remaining balance is not required to be paid until the year 2023.

The calculation of a \$1.3 billion deficit with rates existing prior to April 1, 1974 appears on page 20 of the June CVP Study and is described as the "accumulated results of a repayment study ending in 2031 based on the current rate". The reference to a deficiency of \$1.3 billion within the 50-year repayment period is in error under the conditions of the June CVP Study and is grossly misleading insofar as the financial position of the CVP is concerned. Interest charges of \$1.1 billion can only be obtained by compounding interest upon interest and by disregarding investment already repaid. In this regard, it is noted that the unpaid electric investment of \$436,194,000 supporting its claim of a \$1.3 billion deficit represents the total plant investment over the full 87-year period of the June CVP Study and is added as part of the computed deficit; however, this figure is meaningless since \$204,909,710 of the total investment has already been paid, leaving an unpaid balance of only \$31,920,290 in 1973.

There are established requirements for payback of the federal investment in the CVP. The general provisions are that the investment in each capital component be recovered 50 years after the respective components are placed into service. As subsequent capital additions are added, including renewals and replacements, a required payment schedule is created in which the required payments are due 50 years after the additions. Such a required payment schedule is presented, but not used, as column 35 on the rate and repayment schedule in the June CVP Study labeled "Allowable Unpaid Balance—Commercial Electric Plant". The actual required payments are indicated in column 35 as the reductions of the Allowable Unpaid Balance in each year. Inspection of column 35 shows that the first such reduction, or first required payment, occurs in 1994, which is 50 years after the beginning of the CVP in 1944.

The established procedures, used by the Bonneville Power Administration and by other Bureau regions, for determining the need for a rate increase is to compare the projected unpaid balance, column 30 on the CVP payout schedule, with the allowable unpaid balance, column 35. A rate increase is justified only if the projected unpaid balance exceeds the allowable unpaid balance. In the case of the CVP, the Bureau has abandoned this established procedure by imposing the pinch-point criterion which requires higher revenues and results in the commercial power component of the federal investment being completely paid in 1999, 32 years before it is required to be paid. The pinch-point criterion, which

is a significant factor underlying the Bureau's claim for the need for a rate increase, was pointedly criticized in the report by the Controller General of the United States dated November 19, 1973 (GAO Report) as inconsistent with proper repayment criteria.

RATE INCREASE EFFECTIVE APRIL 1974-JANUARY 1977

The basis for the power rate increase, as announced on November 1, 1973 by Interior, contains the same deficiencies as the June CVP Study. The Bureau has promulgated a total rate increase of approximately 50% to preference customers, a major part of which would be to subsidize sales of Northwest (Centralia) power to PG&E. Under the current rate proposal, the increase in rates to preference customers during the fiscal years 1974, 1975 and 1976 is totally for the purpose of subsidizing the loss on Centralia capacity sold to PG&E. The following tabulation shows the loss, computed by the methods detailed on page II-21 in the August 31 R. W. Beck and Associates Report, and the proposed increase which Interior would impose upon preference customers in 1974, 1975 and 1976 as contained in the November CVP Study:

Fiscal year:	Increase from preference customers	Loss on centralia capacity sold to P.G.&E.
1974.....	\$1,515,000	\$6,679,000
1975.....	6,098,000	6,517,000
1976.....	6,136,000	6,177,000
Total.....	13,749,000	19,373,000

¹ Increase is applied for only 3 months ending June 30, 1974.

CENTRALIA PURCHASES

The greatest single reason for the claimed need for a rate increase is the increased cost of purchased power from the Centralia power plant in the Pacific Northwest. A substantial amount of the capacity and energy from Centralia is being sold to PG&E at a price substantially less than its cost to CVP. The CVP studies indicate that the Bureau will sell and bill no project capacity or energy to PG&E during this period; thus, all power being sold and billed to PG&E is clearly Centralia power. (Substantial amounts of capacity have been made available to PG&E free of charge in addition to the Centralia power for which it is billed.) The CVP studies reflect no rate increase to PG&E for this power prior to April 1, 1976, and the rate increase to PG&E projected to become effective April 1, 1976 to the level of the preference customer rates will not, as the CVP studies clearly demonstrate, be sufficient even then to recover the projected costs of Centralia power sold to PG&E.

The amount by which Centralia costs exceed revenues from capacity sales to PG&E from Centralia accumulates to a total of \$92,795,000 in the period from 1974 through 1994 (the dates to which Centralia purchases are assumed in the Bureau studies) under the conditions of the November CVP Study.

Interior and the Bureau have taken the position that the sales to PG&E below cost now will result in an overall savings to the CVP on the premise that the Bureau can repurchase the capacity and energy in the future at the same price at which it sold plus an assumed 14% service charge. NCPA disagrees with this position:

1. Bureau backup data for the CVP studies show that there is no expected need to repurchase Centralia capacity in any year, thus there is no possible benefit, present or future, in selling such capacity to PG&E at less than cost. In other words, the Bureau is selling this capacity to PG&E at a substantial loss.

2. The future cost of energy repurchased by CVP from the bank is not clear. PG&E has stated that neither the service charge nor the purchase price for energy that is withdrawn (repurchased) from Energy Bank Account No. 2 is specified under the terms of the Bureau-PG&E Contract No. 14-06-200-2948A (Contract No. 2948A), stating further, in substance, that the 14% service charge

assumed by the Bureau is too low and that the future price of energy sold to CVP would be adjusted to reflect the appropriate cost of energy generation on the PG&E system at that time.

3. Even if PG&E were agreeable to returning the energy at the price sold plus a service charge of 14%, the cost which the preference customers are now asked to pay, giving effect to the time value of money, is more than four times the benefit. This is so because each extra "subsidy" dollar paid to PG&E today could, if invested at 3% interest, produce interest income of over 65% (as compared to the 14%) if retained and invested over the 20-year average life of energy in the bank.

As discussed hereinbefore, the Bureau is not only intending for preference customers to subsidize the losses on sale of Northwest capacity and energy to PG&E, but the losses and subsidies are projected in the Bureau studies to continue beyond the 1981 termination date of the current contracts until approximately 1993. Other power supply alternatives are potentially available and need to be considered before raising rates to preference customers.

The terms of Contract No. 2948A with PG&E obligate PG&E to supply energy that is required to support the CVP firm customer load of 1,050 MW (after 1980) through the year 2004, so there is no question as to the availability of a source of energy for the Bureau's customers.

NCPA is actively pursuing development of geothermal generation and has proposed to the Bureau that NCPA would install 440 MW of geothermal capacity to replace and/or supplement Centralia supply. Such energy could be available through at least 1998 and capacity would be available through at least 2031. In addition, NCPA is interested in utilizing the Bureau's 400 MW Pacific Northwest-Southwest Intertie capacity if it becomes available for off-peak energy.

THE CVP STUDY CRITERIA ARE NOT CONSISTENT WITH CURRENTLY EFFECTIVE BUREAU GUIDELINES AND INSTRUCTIONS

According to information furnished by the Bureau, the current guidelines to be used in economic and rate analysis are:

1. Reclamation Instructions Part 583, Power Economic and Financial Studies, dated 5-17-56.
2. Reclamation Instructions Part 489, Depreciation and Replacement, dated 6-9-66 and 4-19-71.

Other specific guidelines have been issued by Interior from time to time with respect to procedures for rate and economic studies. These included instructions dated 8-2-72 to the Bureau from the Office of the Assistant Secretary, Water and Power Resources, of the Department of the Interior, pertaining to expenses for renewals and replacements.

The procedures used in the June CVP Study and the November CVP Study are totally inconsistent with the above guidelines in two important respects, as recognized in the GAO Report:

1. The current instructions clearly direct that expenses for renewals and replacements be considered as capital additions, not as deductions from current revenue as applied in the CVP studies.
2. The CVP studies are predicated upon the premise that the rates must be set high enough to cover all "revenue deductions" of every nature in each and every year from 1977 through 2031. These include all operating, maintenance, depreciation and interest expenses. The result is that the amount of the rate increase is determined by the one year, 1982 in which projected total revenue deductions are the highest (because of a non-recurring factor) even though revenues will exceed deductions in the earlier and later years so that there is a substantial cushion of earnings to absorb an individual year's deficit.

The guidelines for economic evaluation of federal projects clearly anticipate that deficits in operating results may occur under special circumstances. "In early years of project power system operations, the estimated net revenue may result in an annual deficit," (Section 10 of Reclamation Instructions Part 583 referenced above.) The crucial year, 1982, is the year after the anticipated completion of two large capital plant additions and four years after the anticipated completion of a third addition. Both the June and November CVP studies include 100% of the interest and operating costs of these additions as revenue deductions in 1982, notwithstanding the fact that the plant additions are expected to be capable of producing only about 18% of the full revenue that year. The backup data for the CVP studies indicate that the plant additions are not expected to produce full output (i.e., the reservoirs are not expected to be

full) until 1987. There is no basis for requiring CVP to meet all costs during 1982 or any other single year. The essential criterion is that the CVP repay to the Treasury the federal investment within the specified payment period. A method which would be appropriate during the period 1982 through 1987 would be to capitalize, proportionally, the interest and other fixed costs in relation to the percentage of project capability not yet being realized.

JUSTIFICATION FOR RATE INCREASE IS BASED ON ARBITRARY AND ERRONEOUS
ASSUMPTIONS AND CRITERIA

As discussed hereinbefore, the criteria used by the Bureau in its studies that the rates must be sufficient in each and every year to cover all cost of the CVP, including interest costs assignable to existing projects and for new projects, is not consistent with accepted rate-making principles.

The "pinch-point" year of 1982 used in the Bureau repayment schedules for the rate increase to preference customers includes, as operating costs and/or deductions from net revenues, items which have been arbitrarily added and for which alternative assumptions and criteria could have been used which would result in lower revenue requirements in 1982 than those shown on the Bureau repayment schedule.

Partial capitalization of interest on new projects prior to full output (during reservoir filling period)

The Bureau repayment schedule reflects full interest charges for the New Melones and the Auburn-Marysville projects beginning as of the date construction is completed; however, the full output (and, therefore, the full revenue-producing capability) is not realized for a number of years while the reservoirs are being filled. Based on information furnished by the Bureau, the percentages of full energy output which will be produced by each project during the reservoir filling period is as follows:

Year:	Percent of total output	
	New Melones	Auburn-Marysville
1979	49	
1980	66	
1981	85	
1982	97	18
1983	100	35
1984		55
1985		72
1986		88
1987		100

If interest is charged in each year only in direct proportion to the percentage of project output actually realized and the remainder is capitalized (a procedure commonly used by utilities), the amount of interest so capitalized and the net reduction in required revenue to meet the "pinch-point" criteria would be as follows:

[Dollars in thousands]

Year:	Interest capitalized			Interest on capitalized interest ¹	Net reduction in required revenue
	New Melones	Auburn-Marysville	Total		
1979	\$1,133		\$1,133	\$36	\$1,097
1980	755		755	61	694
1981	333		333	72	261
1982	67	\$3,694	3,761	193	3,568
1983	0	2,928	2,928	287	2,641
1984		2,027	2,027	353	1,674
1985		1,261	1,261	393	868
1986		541	541	411	130
1987		0	0	411	(411)

¹ At 3.225 percent.

In the 1982 "pinch-point" year, revenue requirements could be reduced by \$3,568,000 by using this accepted criterion of capitalizing a portion of interest prior to full output of a project.

Capitalizing replacements

Interior issued instructions on August 2, 1972, directing federal power agencies to capitalize replacement costs by June 30, 1973. The repayment schedule dated November 12, 1973, which reflects the promulgated rate increase, does *not* capitalize replacements. If replacements were capitalized, and interest charged thereon, the net reduction in required revenues would be as follows:

[In thousands]

Year:	Replacements capitalized ¹	Interest on capitalized replacements ²	Net reduction in required revenue
1974	\$621	0	\$621
1975	153	\$20	133
1976	159	25	134
1977	169	30	139
1978	289	36	253
1979	325	45	280
1980	386	55	331
1981	401	68	333
1982	422	81	341
1983	700	94	606
1984	710	117	593
1985	703	140	563
1986	683	162	521
1987	689	185	504
1988	855	207	648
1989	866	234	632

¹ Amount of replacements shown on Bureau, Nov. 12, 1973, repayment schedule.

² At 3.225 percent interest.

In the 1982 "pinch-point" year, revenue requirements could be reduced by \$341,000 by capitalizing replacements in accordance with Interior instructions of August 2, 1972.

Centralia purchases in 1982

The present Centralia purchase arrangements will terminate on December 31, 1981 unless extended by mutual consent. During the last six months of fiscal year 1982 (the pinch-point year), the Bureau studies reflect a cost of approximately \$13,228,000 to purchase about 191 MW-Yrs. and 1,347 million kWh of Northwest power. During this same six-month period, the Bureau studies indicate that the Bureau will require about 87 MW-Yrs. and 956 million kWh to supply the needs of the project and its customers.

There is serious question as to the availability of power from the Northwest in 1982, and the Bureau has an alternative source available to it which is lower in cost. The Bureau can repurchase from the bank accounts established with PG&E pursuant to Contract No. 2948A at substantial savings in 1982 (the pinch-point year). These savings, which can be shown as a reduction in required revenue, can be determined as follows:

Bureau studies:

Cost of purchased power from Northwest	\$13,228,000
Less: Revenue from sales to P.G. & E.	3,138,000
Net cost for Northwest purchases required for project and preference customer load requirements	10,090,000

Alternative source:

Cost of purchased power from P.G. & E. for project and preference customer load requirements:	
Capacity at \$21.44 per kilowatt hour ¹	1,865,000
Energy at 3.124 mills per kilowatt hour ²	2,987,000
Total	4,852,000

Cost penalty in 1982 due to bureau marketing assumption 5,238,000

¹ Based on \$18.18 per kilowatt hour (proposed 1977 rate without giving effect to lower cost capacity in bank prior to Apr. 1, 1976) plus 14 percent service charge.

² The highest rate assumed by the Bureau for purchases from Energy Account No. 2.

Summary

The revenue requirements (and, consequently, the rate level) used in the Bureau studies for the preceding three criteria could be reduced, by adopting alternative assumptions, by the following amounts for the 1982 "pinchpoint" year:

Possible reduction in required revenue, 1982

Criteria:

Capitalized partial interest during reservoir filling-----	\$3, 568, 000
Capitalized replacements-----	341, 000
Purchase power from P.G. & E. bank accounts-----	5, 238, 000
Total reduction-----	9, 147, 000

Based upon the results of detailed studies undertaken by R. W. Beck and Associates and presented in our "Report on Central Valley Project June 1973 Power Rate Adjustment Study," it was and continues to be our conclusion that no rate increase to CVP preference customers has been justified or is required at this time. Our studies indicated that a rate increase of approximately 14.5% may be required in 1977 in order for CVP to maintain financial integrity.

Subsequent to the preparation of our Report, we have conducted further studies which support our original conclusions.

As discussed hereinbefore, the rate increase which was placed in effect April 1, 1974 serves only the purpose of collecting from one class of customers—the CVP preference customers—for losses on sales to another customer—PG&E.

The increase to take effect in 1977, which when combined with the increase placed in effect on April 1, 1974 aggregates an increase in rates to preference customers of approximately 50%, has not been and cannot be justified on the basis of adopted Bureau guidelines for preparing repayment schedules, or with congressional statements, as to the concepts which should be used in preparing a rate and repayment study.

The major points which have been summarized hereinbefore are representative of the deficiencies in the CVP studies which have been submitted as justification for the CVP rate increase.

Clearly proper review by the appropriate agency and opportunity for review and comment by the customers who are being asked to pay the increased rates is needed.

EXHIBIT A**PERSONAL PROFESSIONAL QUALIFICATIONS OF HERBERT C. WESTFALL**

Herbert C. Westfall received a degree in engineering from the University of Colorado in 1949 and has served continuously as an engineer since that time.

From 1949 to 1950, he served as a resident construction engineer for the Oregon State Highway Department and from 1950 to 1952 as project design engineer with the firm of Stevens and Thompson, Portland, Oregon.

From 1952 to the present, he has served as a Consulting Engineer with the firm of R. W. Beck and Associates, whose 280 partners and employees serve the utility industry throughout the United States and in several foreign countries. He has been a Partner of the Firm since 1954 and its Managing Partner and Chief Engineer since 1968.

He is a registered professional engineer in 14 states, certified by the National Council of State Boards of Engineering Examiners, and has testified as an expert witness on several occasions before federal regulatory agencies or courts.

Mr. JOHNSON. Our next witness will be Mr. William B. Kuder, the assistant general counsel for Pacific Gas & Electric Co. We welcome you here, Mr. Kuder. We see that you have a very complete and comprehensive statement and submission of materials to be made to the committee's record. Your entire submission will be printed in the record as if read in full, and you may summarize it any way you see fit.

STATEMENT OF WILLIAM B. KUDER, ASSISTANT GENERAL
COUNSEL, PACIFIC GAS & ELECTRIC CO.

Mr. KUDER. Thank you, Mr. Chairman.
[Mr. Kuder's entire submission in full follows:]

STATEMENT BY WILLIAM B. KUDER, ASSISTANT GENERAL COUNSEL, PACIFIC GAS
AND ELECTRIC COMPANY

Pacific Gas and Electric Company (PG&E) purchases power from the Bureau of Reclamation's Central Valley Project under a Power Sale Interchange & Transmission Contract. Changes in rates under this contract would be subject to Federal Power Commission approval if H.R. 14221 is enacted.

In conjunction with hearings on proposed Central Valley Project rate adjustments held last January by the Subcommittee on Conservation and Natural Resources of the House Committee on Government Operations, several questions were asked concerning transactions under the Bureau-PG&E contract. We wish to submit for the record before your committee our answers to these questions and to point out some of the benefits to Central Valley Project preference power customers of the power support and "banking" provisions of the contract.

PG&E provides firming support which enables the Bureau to serve firm loads up to 985,000 kilowatts until 1975 and then up to 1,050,000 in 1980 and each year thereafter. According to Bureau studies, the Bureau could serve only half of this preference customer load without PG&E support.

With this support the Bureau can serve additional customer load at CVP rates. Assuming that both the proposed CVP average rate of 6 mills per kilowatt hour and the current PG&E wholesale average rate of 11 mills continued without change from 1974 to 2004, the Bureau customers would save about 5 mills, or more than \$450 million during the remaining life of the contract, by being able to purchase power from the Bureau instead of from PG&E.

Under two "banking" provisions, capacity and energy sold by the Bureau to the Company can be repurchased by the Bureau whenever it is needed for preference customers. The repurchase price is the price the Company paid plus or minus the difference in cost to the Company of producing power in Company plants between the time power was purchased by the Company and the time power is sold back to the Bureau and plus a reasonable service charge. Thus, the rate for the sale of power to PG&E is directly reflected in a low price for repurchase of power by the Bureau.

Under a third "banking" provision, the Company is obligated to sell nearly 15 billion kilowatt hours of energy to the Bureau for at least \$70 million less than the Company's present cost of producing it, and the amount of this loss will undoubtedly become greater with time.¹

Several Bureau preference customers have complained of a provision in the contract under which the Bureau loses money on sales of Centralia power to the Company. During the period FY 1972 through FY 1976, the Bureau will sell this power, not only to PG&E but also to the Bureau's preference customers, for less than the Bureau paid for it. The Bureau will lose \$30.7 million from sales to preference customers and \$18.8 million from sales to the Company.²

Preference customers which complain of a loss to the Bureau from the sale of Centralia power to PG&E have overlooked the greater loss the Bureau incurs from sale of this power to these customers. They also have ignored the substantial benefits they receive from other provisions in the contract and have failed to recognize that the Company is required to sell power to the Bureau at less than cost under the same contract. On balance, more benefits from these transactions accrue to the preference customers than to the Company.

¹ Please see pages 132-133.

² Please see pages 129-130.

In this statement, we answer some of the questions submitted to us, and include other discussion which we believe pertinent to the matter under consideration.

SUBCOMMITTEE ON CONSERVATION AND NATURAL RESOURCES, QUESTIONS OF
NOVEMBER 12, 1973 AND PG&E ANSWERS

Question 1. Article 32 of the contract (No. 14-06-200-2948A) between the Bureau of Reclamation and PG&E provides that all rates and charges (except project-generated power sold to PG&E and energy sold to the Government from Energy Account No. 1) "shall, together with service charges, be jointly reviewed by the Bureau and PG&E and adjusted as appropriate" on April 1, 1971, and "every five years thereafter."

An August 30, 1973 PG&E statement notes that "PG&E considered the possibility of a joint review and adjustment of rates." The statement, however, speculates that "if a joint review of rates had been made in 1971, any benefit to the Bureau that might have resulted from an increase in the rate for Northwest Power would have been offset by other rate adjustments required to make all rates fair and equitable to both parties . . ."

Question. (a) Isn't the purpose of this mandatory joint review provision to avoid the type of speculation mentioned above and to ascertain the facts in order that both parties can determine if an adjustment is, in fact, "appropriate."

Answer. (a) A joint review is not mandatory unless one of the parties deems it necessary or desirable. The purpose of the review is to ascertain the facts in order that both parties can determine if an adjustment is appropriate.

Question. (b) If the answer to (a) is yes, please explain why no such review was conducted.

Answer. (b) The Bureau did not request a review because it believed "There was no firm basis for negotiating in early 1971, an increase in charges for Centralia power to the bank account."³ As long as the Bureau did not desire to raise the Centralia rate, PG&E was willing to postpone review and adjustment of other rates in the contract until 1975.

Question. (c) If the answer (a) is no, please explain what is the purpose of this mandatory provision?

Answer. (c) See Answer 1(a) above.

Question. (d) How long should such a review take?

Answer. (d) From about six months to two or more years depending on available manpower, assignment of work priorities and the extent to which the rates need adjusting.

Question. (e) Shouldn't that review be undertaken in advance of any rate increase?

Answer. (e) If either party to the contract anticipates that a rate adjustment as provided in Article 32 will be necessary or desirable on one of the specified dates, a review should be made in advance of the anticipated adjustment.

Question 2. In a September 24, 1973 letter to the attorneys representing some CVP customers, Acting Deputy Assistant Secretary of the Interior Wilson stated:

"There is also the consideration that under the contract the Government has the right to buy back the capacity and energy sold to PG&E at the rate at which it is sold plus a service charge, which means that a lower rate for such sale today means a lower repurchase rate in the future."

We understand as follows: Article 22 of the contract obligates PG&E to sell back to the Government the following:

A. From Energy Account No. 1 (which involved CVP hydropower sold to today means a lower repurchase rate in the future.)

B. From the Capacity Account (which involves capacity sold by CVP to PG&E after July 31, 1967)—capacity at a rate computed on the price PG&E paid to CVP "plus a service charge equal to 14 percent";

C. From Energy Account No. 2 (which involves energy, including that from Centralia, sold by CVP to PG&E after July 31, 1967)—energy at a rate computed on the price PG&E paid to CVP "plus a service charge."

However, Article 32 of the contract specifies that "rates and charges for energy sold to the United States from Energy Account No. 2 . . . shall be adjusted

³ Comment on CVP Issue 9 of Issue Papers submitted by the Commissioner of Reclamation to Assistant Secretary of the Interior—Land and Water Resources.

monthly to reflect the changes in costs" of "new thermal generating units" add to PG&E's system "during the preceding 5-year period." Thus, it is evident that the Government's right to buy back the capacity and energy (except from Energy Account No. 1) which CVP sold to PG&E is not tied to the price "at which it is sold" by CVP to PG&E.

Question. (a) Do you agree with our understanding of the contract?

Answer. (a) We agree with point A of your understanding: ⁴ We do not fully agree with your points B or C.

The rate for capacity from the Capacity Account is based on the average price PG&E paid for capacity sold to the Company on and after January 1, 1965, plus a 14 percent service charge. However, both the average price and the service charge are subject to adjustments which may result from the periodic review provided for in Article 32.

The rate for energy from Energy Account No. 2 is to be the average price paid by PG&E for energy sold to the Company plus a service charge; however, Article 22(c) (2) (ii) provides that both the average rate and the service charge are to be modified to reflect any adjustment made under Article 32. Article 32 provides that rate adjustments shall reflect any applicable change in the costs of construction and production and that the charge for energy from Energy Account No. 2 shall be adjusted monthly to reflect the cost of energy generation from thermal generation units installed during the preceding five year period. This provision was designed to permit the Bureau customers to share in the benefits of the latest technological developments in generating units on the PG&E system when determining the adjustment to the average cost of energy in Account No. 2.

The operation of Energy Account No. 2 is illustrated by the following example.

Required

Price for energy from Energy Account No. 2 in January 1985.

Assume

(a) The average sale price to PG&E of all energy in the Account as of January 1985, is 3.0 mills/kwh.

(b) PG&E's average cost of energy production from its thermal units when the energy was banked was 7.0 mills/kwh.

(c) PG&E's average cost of energy production from its thermal units in January 1985 is 9.0 mills/kwh.

Under these assumed conditions, the energy would be sold back to the Bureau at a rate equal to the 3.0 mills price paid by PG&E adjusted upward by 2.0 mills for changes in the cost of production, plus the service charge. Thus, although the cost to the Company of producing the energy was 9.0 mills, the Bureau would pay only 5.0 mills, plus the service charge. It can be seen from the illustration that the price of energy sold to PG&E during the time energy was banked is the primary component of the price for energy to be sold to the Bureau from Energy Account No. 2. Thus, the price for energy from Energy Account No. 2 is in fact tied to and substantially controlled by the price initially paid by PG&E.

Question. (b) In view of the foregoing, and the fact that PG&E's power generating costs will probably be higher than the price PG&E is presently paying for Centralia power, do you agree with Mr. Wilson's assertion that "a lower rate for such sale today means a lower repurchase rate in the future?"

Answer. (b) Yes.

Question 3. We understand that the Bureau's current rate assumes that the Bureau will pay "14 percent" service charges on its future repurchases from Energy Account No. 2. Although there is a "24 percent" provision in the Capacity Account (Article 22(c) (1) (i)), there is no such provision in Articles 22 and 32, or elsewhere in the contract, relating to repurchases of energy from Energy Account No. 2.

PG&E's August 30 statement indicates that this service charge estimate "is too low."

(a) Is that still PG&E's opinion?

Answer (a) Yes. PG&E's administrative and general expenses increased more than 90% in the five years 1967-1972 and may reasonably be expected to escalate in the future.

⁴ Please see pages 132-133.

SUBCOMMITTEE ON CONSERVATION AND NATURAL RESOURCES, REQUESTS OF
NOVEMBER 20, 1973 AND PG&E RESPONSES

Request

The load curve data for the PG&E system in 1967 on the basis of which the Project Dependable Capacity of the CVP system was determined under the 1967 Bureau-PG&E Contract:

Response

Project Dependable Capacity specified in the contract was not based on 1967 load curve data. Plant capacity factors were originally established in the 1951 Bureau-PG&E contract. These were modified in the 1955 and 1963 amendments to that contract. Load curve data used in calculating these capacity factors were not retained in our files. In Article 11(b)(2) of the 1967 contract, the parties agreed that the capacity factors used in the 1963 amendment to the 1951 contract would be continued in the new contract and applied to then existing project plants in all future redeterminations of Project Dependable Capacity.

Request

A statement as to the extent to which PG&E and the Bureau have endeavored to redetermine the Project Dependable Capacity of the CVP system on the basis of the more recent load curve data.

Response

We are currently conducting a redetermination of Project Dependable Capacity. In this process, we are considering recent load curve data in determining the capacity factors to be applied to the San Luis Plant, which was added to the CVP after 1967. This is a pumped-storage plant which does not contribute to the total energy output of the CVP. Therefore, the addition of San Luis is expected to have very little effect on the place which total project generation occupies on the area load curve. The effect of the contract between the State of California and the Bureau for coordinated operation of San Luis must also be evaluated.

Request

The PG&E statement on the proposed Central Valley Project Power Rate Adjustment says on page 6:

"PG&E provides firming support, which enables the Bureau to serve firm loads up to 985,000 kilowatts until 1975. . . ."

We understand that in August 1971, in June 1972, and in May and June, 1973, the total demand of the project preference customers reached 925 mw and in those months there were withdrawn from the customers 47.75 mw, 3.55 mw, 16.35 mw and 3.35 mw, respectively. However, we note that Article 14(a)(2) of the Bureau-PG&E contract (14-06-200-2948A) states that "... after April 1, 1971, the load level may gradually increase each year coincident with customer load growth . . . up to approximately 985,000 kilowatts prior to January 1, 1975."

Please advise us why PG&E bills CVP project preference customers when their integrated demand exceeds 925 mw and is less than 985 mw?

Response

PG&E bills CVP project preference customers only for power they receive from the Company in excess of the power they buy from the CVP. The amount of CVP power sold by the Bureau to a customer is determined by the Bureau's contract with the customer. 925 MW is the current load level which requires support under the contract because that is the load level "indicated by the information given by the United States" to PG&E as provided by Article 14(a)(2). We understand that the Bureau has withdrawn CVP power allocations, when the total integrated demand exceeds 925 MW, from certain customers to assure that the firming support levels will coincide with the load growth of other customers with firm power allocations selected by the Secretary of the Interior in accordance with the federal power marketing policy reported to and endorsed by the Congress in 1964. (See Senate Appropriations Committee print, Department of the Interior "Report to the Appropriations Committee of the Congress of the United States Recommending a Plan of Construction and Ownership of EHV Electric Interties Between the Pacific Northwest and Pacific Southwest" (1964), p. 45; See S. Rept. No. 1326, 88th Cong., 2d Session 33,

37-38 (1964), and H.R. Rept. No. 1794, 88th Cong., 2d Session 42 (1964); see also 16 U.S.C. Section 837g, Pub. L. 88-552, Section 8, August 31, 1964, 78 Stat. 758, Pub. L. 88-511, August 30, 1964, 78 Stat. 689.)

VIEWES AND COMMENTS ON GENERAL ACCOUNTING OFFICE REPORT B-125042
OF NOVEMBER 19, 1973

Chapter 1: Introduction

PG&E has no basic disagreements with the statements of fact contained in Chapter 1 of the report.

PG&E is not in a position to comment on statements concerning the Bureau's policies in establishing its rates.

Chapter 2: Contentions by Opponents of Proposed Power Rate Increase

Contentions 1 and 5.—The loss to the Bureau from sales of Centralia capacity and energy to PG&E and to preference customers, reported at pages 10-12 of the GAO report, is calculated on the assumption made in the Bureau's Rate Adjustment Study that nearly all Centralia capacity is to be sold to PG&E. Of course, this assumption has no material effect on calculation of total CVP revenues, as long as all Bureau power is sold on a single rate schedule. However, since the issue of proper allocation of CVP Centralia losses has now been raised it becomes important to account for these losses in accordance with the Bureau-PG&E contract and actual operation of the CVP. In fact, less than half of the Centralia capacity will be sold to PG&E and all the rest will be sold to preference customers.

Article 22(a) (3) of the Power Sale Interchange and Transmission Contract between the Bureau of Reclamation and PG&E provides that:

In determining the amounts of capacity and energy for which Contractor shall pay the United States in any month . . . it shall be deemed that capacity required for maximum Demand of Firm Load and energy required for Firm Load were first furnished from Project generation.

Project generation operates at capacity factors lower than the load factors of the Bureau's preference customers. Consequently, these customers require Centralia capacity and energy to make up the deficiency. The only capacity and energy sold to PG&E for banking are the capacity and energy from CVP plants and Centralia which are not required to serve preference customer loads.

All power sold by the Bureau is a mix of Centralia thermal capacity and energy and CVP hydro plant capacity and energy. Centralia power is delivered at 80% capacity factor and is needed to meet operating requirements of the CVP. This is because CVP hydro plants have an average year capacity factor of about 46% and a dry year capacity factor of only 35%, whereas preference customer loads require a capacity factor of about 60%.

These facts lead to the results that capacity and energy sold from CVP plants and Centralia to preference customers, and to PG&E for banking, during the period FY-1972-1976 will be as follows:

BUREAU CAPACITY DISPOSITION

[In megawatt years]

	Sold to CVP customers		Sold to P. G. & E. for banking	
	CVP capacity	Centralia capacity	CVP capacity	Centralia capacity
Fiscal year—				
1972 ¹	810	115	115	76
1973 ¹	784	141	141	241
1974 ²	658	267	241	115
1975 ²	654	271	220	111
1976 ²	654	271	154	111
Subtotal	3,560	1,065	871	654
Total	4,625		1,525	

¹ Actual.

² Estimated on basis of energy disposition in bureau rate adjustment study.

BUREAU ENERGY DISPOSITION

[10⁶ KWh]

Fiscal year	Sold to CVP customers		Sold to P.G. & E. for banking	
	CVP ¹ energy	Centralia energy	CVP ¹ energy	Centralia energy
1972 ²	4,394	798	1,027	523
1973 ²	4,336	1,013	167	1,723
1974 ³	3,525	1,885	0	808
1975 ³	3,533	1,912	0	781
1976 ³	3,567	1,912	0	781
Subtotal	19,355	7,520	1,194	4,616
Total	26,875		5,810	

¹ Includes Northwest energy other than from Centralia.² Actual.³ Estimated on basis of energy disposition in Bureau rate adjustment study.

The Bureau's actual costs of Centralia capacity and energy were 6.92 mills/kwh in FY 1972 and 6.79 in FY 1973. The Bureau estimates these costs will increase to 8.76, 8.79 and 9.01 mills in FY 1974, 1975 and 1976 respectively. The Bureau currently is selling this capacity and energy to its preference customers and to PG&E at a rate of about 3.74 mills/kwh. This rate will change to about 4.72 mills on April 1, 1974 for sales to preference customers. The Bureau assumes that that rate will become effective on April 1, 1976 for Centralia sales to PG&E.

It appears from the foregoing data on disposition, costs and rates, that, from FY 1972 through FY 1976, the Bureau will lose \$30.7 million from the sale of Centralia capacity and energy to preference customers and \$18.8 million from the sale of Centralia capacity and energy to PG&E.

Inasmuch as 1) more CVP plant capacity will be banked than estimated by GAO and 2) PG&E will pay the increased rate for this capacity and associated energy beginning on April 1, 1974, the revenue to the Bureau from PG&E for capacity and energy, 1972-1976, will be \$0.5 million more than estimated by GAO.

Updated Bureau hydrology studies indicate that there will be about 8% more energy from CVP plants than estimated in the Repayment Study. If the Repayment Study were modified to reflect this increase and a corresponding decrease in the need for Northwest power, it would show that from July 1972 through FY 1999, the Bureau would sell (bank) to PG&E 9257 MW years of CVP and Northwest capacity. If the Repayment Study were further corrected to reflect the Northwest capacity used by preference customers, it would show that the amount of Northwest capacity sold to PG&E would be only 2472 MW years and not 8271 as stated at page 13 of the GAO report.

The estimated effect of this transaction on the Repayment Study is a hypothetical loss of \$40 million to CVP, and not \$116 million as stated at page 13 of the GAO report. Of course, this "loss" would occur only if CVP did not repurchase the capacity banked with PG&E.

In view of increasing needs for surface water supplies in central California, we believe that it is reasonable to assume that future additions of project canals and pumping plants will be authorized by Congress. These facilities will require additional CVP power for operating project pumps. In that event, capacity from the bank may well be needed to augment the power supply of CVP so that it can meet the demands of its customers. Moreover, it is possible that the Bureau will not be able to continue to purchase Northwest capacity throughout the term of the contract and therefore will require capacity from the bank for preference customer loads.

If the capacity bank will not be used, PG&E should be relieved of the obligation of maintaining it. In that event, the CVP rate readjustment in 1976 should take this factor into consideration. Moreover, the one mill wheeling rate and the capacity and energy charges for PG&E power sold to the Bureau

should also be adjusted so that all rates and charges under the contract will continue to be fair and equitable as required by Article 32 after taking into account the benefits to preference customers pointed out at pages 1, 2, 7, 8, 29-31.

We concur in the conclusion at page 15 of the GAO report that it is impossible to state at this time what rate will be negotiated with PG&E in 1976 and that the assumption of the opponents that CVP "could purchase the energy it needs from PG&E for substantially less than CVP pays for Northwest power" seems to be "highly speculative", particularly in view of current capital and fuel cost trends.

Mr. Arthur Simon⁵ alleges that the Beck estimate⁶ of a 5.35 mills per kwh cost of fuel for energy sold by PG&E after the energy accounts are exhausted is a more accurate estimate than PG&E's estimate of 9 mills. In these days of rapidly rising fuel costs, it is difficult to predict what PG&E's cost of fuel will be after the energy accounts are exhausted. The 9 mill cost represents an average cost for energy from \$6.00/bbl. oil. PG&E has recently purchased fuel oil at \$7.00/bbl., an equivalent of over 10 mills/kwh. Such costs are higher today⁷ and are expected to rise even more in the future. The 5.35 mill estimate by Beck is based on an assumption that 25% of the fossil fuel used by PG&E will be natural gas. PG&E estimates that virtually no natural gas will be available for generation after 1974.

Contention 2.—PG&E agrees that 1922-71 is a reasonable hydrology period for projecting average energy production from the CVP. Although we have not attempted to calculate the amount of increase, we agree that the 1922-71 hydrology period would yield a higher average energy production than the 1922-54 period. However, use of this expanded period would not change Project Dependable Capacity.

Contention 4.—We generally concur with the conclusion that the report reaches on this contention. Capacity is made available to PG&E without charge from time to time on a short term unpredictable basis. The Company more than compensates the Bureau for use of this capacity by providing integrated operation and reserve backup as discussed at pages 30-31.

Contention 6.—Please see our comment on Contention 10.

Contention 7.—PG&E's accounting practice is that replacement costs are capitalized within the calendar year that they occur.

Contention 8.—We do not have enough information to evaluate Reclamation instructions and therefore have no reason to question the validity of GAO's conclusions regarding Contention 8.

Contention 9.—If the Bureau did not have the type of support provided under the PG&E contract after the year 2004, the amount of power that the Bureau would be able to sell to its customers would be substantially reduced. We doubt whether the reduction in revenues would be offset by reduction in the expenses of purchased power to an extent sufficient "to lessen rather than increase the need for a power rate increase."

Contention 10.—In our opinion it is a good business practice to plan for no deficit financing in any year. Moreover, application of this policy to the repayment of federal Reclamation projects will, to the extent it produces a surplus, relieve federal taxpayers of the burden that would otherwise be imposed on them to finance new federal projects or additions to existing projects.

Contention 11.—PG&E follows the practice of capitalizing interest during construction until a plant is placed in commercial operation. To be in commercial operation a PG&E hydro plant both must complete its acceptance tests and its reservoir must be full or substantially full to allow operation in the following year should that year be dry. The reservoirs operated by the CVP present a more difficult problem in that they typically are multipurpose in nature and the time required to fill them is normally longer than for PG&E reservoirs. PG&E does not take a position as to what would be appropriate practice under the particular circumstances of the CVP facilities.

⁵ Arthur Simon Comments, October 11, 1973.

⁶ R. W. Beck Study, August 31, 1973.

⁷ As of November 1973; please see footnote at page 133.

CONGRESSMAN M'CLOSKEY'S QUESTIONS OF FEBRUARY 25, 1974, AND P.G. & E.
ANSWERS

Question 1. What has PG&E paid, and at what rates, for the energy in Bank Account No. 1? What are the total amounts and dollar figures involved by year?

Answer 1. PG&E paid the R2-F2 rates for the energy accounted for in Energy Account No. 1: 4 mills per kwh for the first 130 kwh per kw of capacity each month, 3 mills per kwh for the next 130 kwh per kw of capacity each month and 2 mills per kwh for all additional energy, discounted 5 percent for delivery at voltages exceeding 44 kv. The following table shows the total amounts, and dollar figures involved by year. We also list the balance on July 31, 1967, which was the last day energy was credited to Energy Account No. 1, and the balance as of January 1, 1974.

Year	Energy purchased by P.G. & E. (10 ⁶ kWh)	Total cost (thousands)
1951	46	\$149
1952	2,382	6,140
1953	1,870	5,003
1954	1,544	3,699
1955	575	1,417
1956	1,448	3,486
1957	1,072	2,602
1958	1,795	4,147
1959	565	1,333
1960	313	662
1961	411	870
1962	420	914
1963	1,061	2,353
1964	919	2,400
1965	1,281	3,213
1966	709	1,606
1967	762	1,589
Total purchases	17,173	41,583
Less U.S.B.R. purchases 1951 through July 31, 1967	2,280	
Energy account No. 1 balance as of July 31, 1967	14,893	
U.S.B.R. purchases August 1967 through December 1973	2,461	
Energy account No. 1 balance as of Jan. 1, 1974	12,432	

Question 2. What is the average time such energy remains in the bank until it is repurchased?

Answer 2. The energy was purchased by PGandE during the period from December 1951 through July 1967. We estimate the Energy Account No. 1 balance will be reduced to zero some time between 1986 and 1996. This would give an average time period of about twenty to twenty five years between the time PGandE bought the energy and the time PGandE resold energy to the Bureau.

Question 3. At what rates has this energy been resold to PGandE's customers? What are the total amounts and dollar figures involved by year?

Answer 3. All energy produced or purchased by PGandE is comingled and sold at rates regulated by the California Public Utilities Commission (retail) and the Federal Power Commission (wholesale). The dollar amounts received depend upon the class of customer and the demand of each member of each class. There is no way to trace each kilowatt-hour purchased from CVP by PGandE and delivered for ultimate consumption by, for example, an industry, commercial establishment, or a residential user. Therefore, the total amounts of energy and dollar figures requested cannot be determined.

However, if the purpose of the question is to determine whether PGandE makes a profit from the energy it buys from CVP and sells to PGandE customers, the answer is that there is no profit to the company from this transaction. Under utility regulation, the company is allowed a rate of return only on capital it has prudently invested in facilities used or useful to provide reliable service. Payment for purchased power is not a capital outlay; it is an operating expense and, like cost of fuel, wages, and other operating expenses, the cost is passed on to the customer. Under California regulation, the cost of purchased power as well as any other operating expense must be included for rate making purposes without any margin, mark-up, or profit. Where the cost of purchased

power is less than the cost of fuel for producing a like amount in company thermal plants, the saving is passed on to the customer in the form of rates lower than they would otherwise have been.

Question 4. If the accumulated and compounded interest on the investment represented by the stored energy is added to the price of the energy sold by PGandE back to Bureau of Reclamation, does PGandE not find the energy bank operation extremely profitable, even despite the present 9 mill cost.

Answer 4. No. No profit has accrued or will accrue to PGandE from the energy bank account. The energy was purchased by PGandE and, as explained in Answer 3, resold to its customers without any margin, mark-up or profit. The dollar benefit to our customers from this transaction can be determined. Between 1951-1967 the average price paid by the Company for CVP energy was 2.44 mills per kilowatt hour. During this same period, the Company's average cost of thermal generation was 2.77 mills. Thus, customers saved, on the average, 0.33 mills, or a total of about \$5 million during the entire period. It cannot be supposed that those customers set this amount aside and invested it at compound interest, and it would be very unrealistic to make such an assumption.

On the other hand, if the contract is not amended, it is entirely clear that PGandE customers will bear a loss in the cost of energy resold to the Bureau from Energy Account No. 1. The question assumes a present cost of 9 mills per kilowatt hour on such resale. Against that cost, there would be a credit of 0.33 mills (the amount the PGandE customers saved initially) and 2.81 mills (the present contract rate for sales to CVP). Thus the net loss to PGandE customers on resale to the Bureau would be 9 mills less 3.14 mills, or 5.86 mills. On sales of the remaining 12.4 billion kilowatt hours in Energy Account No. 1, the loss would be about \$73 million. If the cost of oil raises the cost of energy above 9 mills, then the loss would be greater.⁸

Question 5. For Energy Bank Account No. 2, assuming that present purchases will be sold back in 1992-2004, and assuming the 14% service charge, what is the interest rate which could be said to be applicable to this loan of public assets to PGandE?

Answer 5. There is no loan of public assets to PGandE. PGandE customers may benefit as explained in Answers 3 and 4. The energy is not "stored"; it flows through immediately to PGandE customers. Thus this energy does not represent an investment in a fund of either energy or money on which PGandE could or would be permitted to earn a return or an interest component. The service charge is, for ratemaking purposes, treated as an offset to PGandE system operating expenses. The receipt by the company of this energy and its resale to PGandE customers results only in an obligation on PGandE to make future sales to the Bureau in amounts and at rates based on the amount and cost of the original receipts. In the interval between a receipt from the USBR and a subsequent corresponding sale to the Bureau, there is no loan of public assets to PGandE in any form.

Question 6. Did PGandE initiate or suggest the new capacity allocation of Centralia output to the Bureau of Reclamation?

Answer 6. PGandE pointed out to the Bureau that CVP plants did not produce enough energy to meet preference customer requirements and that a large amount of energy sold by CVP to these customers was generated by Centralia capacity. The company therefore told the Bureau that, in accordance with Article 22(a)(3) of the Power Sale Interchange & Transmission Contract between the Bureau of Reclamation and PGandE, Centralia capacity should be allocated to Bureau preference customers on the basis of their end use of the energy it produced. This was not a new concept inasmuch as the Bureau had used it in early November 1973 in preparing its answer to the Subcommittee's letter of October 24, 1973, Question 1(d)(i), concerning the Bureau's cost of Centralia power sold to PGandE.

Question 7. When the concept of capacity charges first discussed, and between which representatives of PGandE and the Bureau?

Answer 7. The concept of allocating Centralia capacity on the basis described in answer 6 was first discussed with the Bureau at its Sacramento Office on November 21, 1973. Present were: J. E. Heller, W. B. Kuder, and W. C. Travis for PGandE and R. L. Barta, G. R. Estes, and Rita Singer for the Bureau.

⁸ In the second quarter of 1974, oil to replace that being used from storage has cost about \$15.00 per bbl. or 23 mills per kwh.

Question 8. If the Bureau now charges PGandE for Centralia capacity, should PGandE pay for past allocations of such capacity as well?

Answer 8. The Bureau has billed and PGandE has paid for all Centralia capacity allocated to PGandE by the Bureau through January 1974.

Question 9. Did PGandE initiate or suggest the new capacity allocation of Centralia output to the Bureau of Reclamation?

Answer 9. Please see the answer to question 6.

Question 10. On what basis is the resale rate set at the industrial rate? Does this not have an impact adverse to small municipal utilities?

Answer 10. PGandE resale rates are not set at the PGandE industrial rate level. They are based on cost of service.

PGandE resale rates are subject to Federal Power Commission jurisdiction. Industrial service rates are subject to the jurisdiction of the California Public Utilities Commission. Each of these two regulatory agencies carries out its rate-making procedures independently of the other. However, since each agency determines the PGandE rates under its jurisdiction on a foundation of PGandE's total system cost of service, for loads of similar size and character the rates under each of the two jurisdictions would, in the long run, be expected to be comparable. Because of differences in the timing of rate proceedings before the two agencies, the relationship between these rates will, of course, vary from time to time.

To the extent that cost-based resale and industrial service rates are comparable for customers of comparable size and character, resale customers are not adversely affected. A resale customer serving two or more ultimate users is serving customers smaller than itself. Even if a relatively small resale customer were to establish service to a relatively large industrial customer, the resale customer would remain larger than any single load it serves. The resale customer always has the advantage of buying in larger bulk than would be possible for any of its customers. The presence of load diversity among its customers increases that advantage.

Question 11. In view of today's energy problems, does PGandE still feel that CVP sources of generating capacity should come only from hydro or federal sources?

Answer 11. CVP sources of generating capacity and energy made available for integrated operation of the CVP and PGandE systems should be (1) CVP plants; (2) surplus generation of northwest plants; and (3) hydro electric plants of the United States and other sources as agreed upon by the parties pursuant to paragraphs (f) and (g) of Article 19 of the Power Sale Interchange & Transmission Contract between the Bureau of Reclamation and PGandE.

Question 12. In addition to Centralia capacity, does PGandE receive any other capacity from CVP at no charge? (The difference between plant capacity and CVP load and the ratchet capacity above an annual customer support level of 925 MW.) What value does PGandE assign in plant costs to this capacity?

Answer 12. A. Centralia Capacity.—PGandE pays for all the Bureau's Centralia capacity not used to serve the Bureau's preference customers.

B. CVP Plant Capacity.—A project dependable capacity rating for the CVP plants as a group has been established by studies conducted jointly by the Bureau and PGandE. This rating is now 925 MW. Assuming no outages, the project dependable capacity represents the amount of capacity supported by energy that is available from the project under historical dry cycle water supply conditions after deducting the capacity used for CVP pumping loads and CVP electrical losses. The Bureau receives full payment for this project capacity even though at times some of the Bureau generating units are out of service for overhaul. When this occurs, PGandE provides the replacement capacity needed by Bureau customers at no additional charge to the Bureau. During average or wet years some additional capacity may become available from time to time as a result of the increased water supply. This capacity is available to PGandE at no additional charge.

C. Ratchet.—The present customer load level, measured at the time of annual peak demand, is 925 megawatts. In months when the demand of customer loads is less than the annual peak demand, PGandE may use the capacity represented by the difference in demand without additional charge.

D. Value.—The CVP plant capacity in excess of project dependable capacity has no value for planning purposes because it is not known to be available far enough in advance to permit deferral of investment by the company in other capacity.

Once the investment in company capacity has been made, the CVP excess capacity has value only to the limited extent that it allows additional flexibility in the integrated operation of the company and CVP systems. At times of

abnormal CVP water supply or seasonal declines in CVP customer load, these same conditions ordinarily prevail on the PGandE system. Area capacity made available to PGandE as a result of such conditions is primarily to use in releasing generating capability for overhaul. The share of such capacity provided by CVP is not fully usable to PGandE because of uncertainties in scheduling and forecasting as well as lack of need. To the extent such capacity is usable it represents a benefit to PGandE that partially offsets corresponding benefits provided by PGandE to the Bureau without charge such as reserves for overhaul and forced outages.

Question 13. Is there excess non-firm energy in the CVP system which flows to PGandE? If so, what price is paid for it?

Answer 13. PGandE purchases for banking all CVP firm and non-firm energy in excess of that used to serve project and preference customer loads. Such purchases are made at the prevailing CVP customer rate which, until April 1, 1974 was:

4.0 mills/kwh for the first 130 kwh/kw each month; 3.0 mills/kwh for the next 130 kwh/kw each month; and 2.0 mills/kwh for all remaining energy.

The Bureau has announced that this rate will become 3.0 mills/kwh for all energy on April 1, 1974. PGandE receives a 5% discount on all energy because it is received at voltages exceeding 44 KV.

Question 14. Does PGandE oppose public financing of generation by municipal utilities or groups of such utilities? If so, on what basis, and what actions has PGandE taken to oppose the financing of such generation?

Answer 14. PGandE has appeared before committees of the California Legislature and opposed passage of bills which would allow city councils to authorize issuance of revenue bonds to finance electric generation. The company's opposition was based on the ground that the bills did not adequately provide (and in some versions had no provision) for a vote of the citizens of these municipalities to show whether or not they approved the issuance of bonds for that purpose.

CONCLUSION

At the House Government Operations Subcommittee hearing on January 23, 1974, Mr. McCloskey expressed concern about the effect on taxpayers of CVP power rates. Attached is a report by National Economic Research Associates, Inc. on the "Subsidy Received by Government-Owned and/or Financed Electric Utilities."

The report concludes that government-owned and government financed power systems are subsidized by the government—or by the taxpayers—because (1) they do not pay federal or state income taxes as do investor-owned electric companies; (2) their debt securities are issued by government entities with the result that the interest thereon is free from the payment of income taxes at both federal and state levels; and (3) there is a capital cost benefit as a result of the risk reduction which occurs when government substitutes its capital raising ability for that of the electric utilities themselves.

The report estimates that the total subsidy amounted to over \$1.6 billion in the year 1967 and in 1980 will be over \$4.2 billion.

Any review of federal electric power rates should take into account this increasing burden on taxpayers who do not share in the benefits of government power sold at less than its true cost. Moreover, the need for conservation of energy which will be with us during the foreseeable future should justify elimination of any subsidy which encourages increased demand for electric power.

May 20, 1974.

SUBSIDY RECEIVED BY GOVERNMENT-OWNED AND/OR FINANCED ELECTRIC UTILITIES

(A Report by National Economic Research Associates, Inc. to the Edison Electric Institute)

SUMMARY

The National Economic Research Associates (NERA) is an independent consulting firm specializing in economic studies and forecasting. They were retained by the Edison Electric Institute to estimate the total subsidy currently received by government-owned and government-financed electric power systems. All data in the report are for the year 1967 as being the latest year for which complete information was available at the time of preparation of the report.

In 1967, there was about 3,150 electric utility systems owned and operated by federal agencies, municipal governments, rural electric cooperatives, power districts and state agencies. This sector generated 23.5 percent of the total utility industry output, with federal power agencies accounting for 13.4 percent; municipal governments for 4.8 percent; power districts and state projects for 4.4 percent; and rural electric cooperatives for 1.0 percent. Because of a lack of adequate data, the study excludes consideration of some federal projects and some municipal electric systems; consequently the following figures are understated in the total subsidy received.

Because investor-owned electric utilities are regulated by government, NERA believes that, as a whole, the gross earnings rate of all investor-owned electric utilities is a measure of the minimum return required by society for the investment of capital in electric power systems. Thus, the degree of subsidy provided to the tax-exempt sector may be measured by the difference between the gross rate of return of these systems and the gross rate of return of the investor-owned electric utilities.

The report concludes that government-owned and government-financed power systems are subsidized by the government—or by the taxpayers—because 1) they do not pay federal or state income taxes as do investor-owned electric companies; 2) their debt securities are issued by government entities with the result that the interest thereon is free from the payment of income taxes at both federal and state levels; and 3) there is a capital cost benefit as a result of the risk reduction which occurs when government substitutes its capital raising ability for that of the electric utilities themselves.

The NERA report estimates that the total federal, state and local government subsidy to those tax-exempt electric systems amounted to over \$1.6 billion in the year 1967. The following breakdown shows this subsidy:

	State, district, and municipal	Rural electric cooperatives	Federal projects	Total
Federal subsidy.....	\$430,767,000	\$263,811,000	\$560,411,000	\$1,254,989,000
State and local subsidy.....	64,899,000	98,045,000	229,129,000	392,073,000
Total subsidy.....	495,666,000	361,856,000	789,540,000	1,647,062,000

In addition, the report makes an estimate of the subsidy involved to these government-owned and government-financed systems for the year 1980. The report assumes that the distribution of the load among the various ownership sectors will conform generally to the present distribution which has been stable for a number of years. The report concludes that the total subsidy to be received in 1980 by government-owned and government-financed electric utilities will be about \$4,228,733,000. Of this total, the federal government will provide \$3,222,109,000 with state and local governments providing the remaining \$1,006,624,000.

NOTE.—This summary was prepared by the Edison Electric Institute.

SUBSIDY RECEIVED BY GOVERNMENT-OWNED AND/OR FINANCED ELECTRIC UTILITIES

1. INTRODUCTION

The purpose of this report is to estimate the total subsidy currently received by the government-owned and/or financed sector of the electric power industry and to discuss the effect of the subsidy on resource allocation. It should be emphasized at the outset that no attempt is made to judge whether the subsidy currently granted to this sector is justified from a public policy standpoint. Under certain circumstances, for both economic and non-economic reasons, subsidies may be desirable. However, in order to properly formulate public policy, it is necessary to recognize the extent of the subsidy and its effects on the allocation of resources.

The government-owned and/or financed sector of the electric power industry is comprised of approximately 3,150 electric utility systems owned and operated by federal agencies, municipal governments, REA cooperatives, power districts and state agencies. In 1967 this sector generated 23.5 per cent of the electric utility industry's total output, with federal agencies accounting for 13.4 per cent; municipal governments for 4.8 per cent; power districts and state projects for

4.4 per cent; and REA cooperatives for 1.0 per cent.¹ Because of a lack of adequate data, this study excludes consideration of some federal projects and some municipal electric systems. As a result, the total subsidy received by government-owned and/or financed electric utilities is probably underestimated.²

It has long been recognized that the government-owned and/or financed sector of the electric power industry is subsidized by the general taxpaying public. The subsidy arises from two sources. First, these electric utilities have special advantages that enable them to obtain capital at a cost lower than that available in the market to investor-owned enterprises. Federal projects other than the Tennessee Valley Authority obtain capital directly from the U.S. Treasury. Such projects benefit, therefore, to the extent that the government's cost of borrowing is less than the cost to private enterprise. Similarly, REA cooperatives obtain capital directly from the federal government and benefit even further in that their interest costs are fixed by law at 2 per cent, regardless of the Treasury's borrowing costs. The Tennessee Valley Authority (TVA) is a special case. Since 1961 TVA has been permitted to issue taxable revenue bonds to finance the construction of new facilities. No subsidy is involved in capital so raised, except to the extent that TVA's position as an agency of the federal government may reduce its interest costs as well as eliminate the necessity for raising high-cost equity capital. Further, the TVA continues to benefit from the fact that the charges imposed on its pre-1961 capital derived from appropriations are equal only to the average interest rate paid by the U.S. Treasury and that capital derived from retained earnings is available without charge. Municipals are able to raise capital at rates below those prevailing for private firms because no federal income tax is imposed on municipal bond interest. Essentially, this permits a municipal power system to pay its bondholders only the net rate of return they demand, while a private utility must pay a higher interest rate that would yield this net return requirement after payment of the bondholders' personal income tax.

The second major source of subsidy to the government-owned and/or financed sector is their freedom from direct taxation. These electric power supply systems normally pay no federal or state corporate income taxes and no property taxes, although some payments in lieu of local property taxes are made.

The findings of this study are that the total 1967 subsidy to the government-owned and/or financed sector of the electric power industry was \$1,647,062,000. Of this amount, the federal government provided \$1,254,989,000 (76 per cent), with the remainder provided by state and local governments. The total subsidy is expected to increase to \$4,228,733,000 by 1980. The analysis employed to derive these estimates is discussed in detail in the next three sections.

The subsidy provided to government-owned and/or financed systems by artificially reducing the cost of capital to such systems tends to encourage overinvestment in electric power facilities. It is clear that in an economic analysis of the desirability of a particular investment, comparisons should be made on the basis of real investment costs to the economy. The use of a rate of return that is arbitrarily determined by a legislative or executive decision and which, therefore, ignores the market evaluation of capital, results in a misallocation of resources.³

II. THE TOTAL SUBSIDY

The degree of subsidy provided to government-owned and/or financed power supply systems may be measured by the difference between the gross rate of return of these systems and the gross return of the investor-owned electric utilities. Much regulatory effort is aimed at discovering the true cost of capital to investor-owned electric utilities and then setting rates so that actual earnings will approach this cost. Assuming that, as a whole, regulatory commissions are reasonably successful in their efforts, then we may take the gross earnings rate of all investor-owned electric utilities as a measure of the minimum return required

¹ Edison Electric Institute, *Statistical Yearbook of the Electric Utility Industry for 1968*, p. 18. In the same year, this sector accounted for 24.4 per cent of the industry's installed generating capacity and made 23.6 per cent of all kilowatt-hour sales to ultimate customers. *Ibid.*, pp. 6 and 31. At the time of this report, 1967 was the most recent year for which complete data were available. 1968 data are being published and coverage should soon be complete.

² Those excluded own 2.1 per cent of the electric power industry's installed generating capacity, and make only 2.7 per cent of the total electricity sales to ultimate customers. Thus, those excluded own 8.9 per cent of the total government-owned and/or financed electric utilities' installed generating capacity and make 13.0 per cent of that sector's sales to ultimate customers.

³ This point is widely recognized. See, *Interest Rate Guidelines for Federal Decision-making*, Hearing before the Subcommittee on Economy in Government of the Joint Economic Committee, Congress of the United States, January 29, 1968, pp. 4-10; and *The Financial and Economic Obligations of the Nationalised Industries*, presented to Parliament by the Chancellor of the Exchequer by Command of Her Majesty, London, April 1961, p. 6.

by society for the investment of capital in electric power systems. The difference between this return and the actual rate of return earned by government-owned and/or financed systems must therefore be a measure of the subsidy received by such systems. Put another way, the difference between the gross earnings of this sector and the investor-owned electric power systems (per dollar of investment) must go to one of two sources: (1) taxes paid by the investor-owned firms but not by the government-owned and/or financed enterprises; and (2) differences in the net earnings required by investors. The net earnings required by investors will, in turn, differ because of differences in tax treatment (freedom of municipal bond interest from federal income tax), investment risks (investors tend to view government enterprises as less risky, all else equal) or because of direct subsidy (permitting REA cooperatives to borrow at a 2 per cent of interest). These are precisely the components of the total subsidy that we wish to measure.

In order to calculate the total subsidy provided to the government-owned and/or financed sector, it is necessary to compare the actual gross earnings of this sector with the level that would be required if the earnings rate were equivalent to that of the investor-owned sector. The 1967 earnings equivalent was arrived at in the following manner. Total capitalization applicable to electric operations (total capitalization multiplied by the ratio of net electric plant to total net plant and investment) and gross electric utility income (net electric operating income plus taxes and tax equivalents) were computed for both the investor-owned and government-owned and/or financed sectors of the industry.⁴ For the investor-owned electric utilities, gross electric income as a per cent of electric capitalization was 13.8 per cent, with net operating income representing 7.3 per cent and taxes 6.5 per cent. Comparable percentages for the government-owned and/or financed sector (shown in Table 1) were 5.1, 4.5 and 0.6, respectively. The percentages computed for the investor-owned electric utilities were then applied to the electric capitalization figures of the various government-owned and/or financed facilities to arrive at the latter's computed gross electric utility income net operating income and tax equivalents.

REVENUE AND TAX DATA—INVESTOR-OWNED AND GOVERNMENT-OWNED AND/OR FINANCED ELECTRIC POWER SYSTEMS, 1967¹

[Dollar amounts in thousands]

	Investor-owned class A and B companies	Government owned and/or financed				Total ³
		Municipals	REA Coops	PASNY	Federal projects ²	
Total electric capitalization (TEC).....	\$48,559,186	\$6,636,150	\$4,121,740	\$1,116,511	\$7,194,601	\$19,069,002
Gross electric income.....	\$6,689,293	\$511,154	\$205,955	\$61,187	\$201,587	\$979,883
Percent of TEC.....	13.78	7.70	5.00	5.48	2.80	5.14
Net electric income.....	\$3,552,384	\$451,163	\$164,314	\$61,187	\$186,892	\$863,556
Percent of TEC.....	7.32	6.80	3.99	5.48	2.60	4.53
Taxes or equivalent paid.....	\$3,136,909	\$59,991	\$41,641	0	\$14,695	\$116,327
Percent of TEC.....	6.46	90	1.01	0	.20	.61
Federal income tax.....	\$1,491,185	0	0	0	0	0
Percent of TEC.....	3.07	0	0	0	0	0
Other tax.....	\$1,645,724	\$59,991	\$41,641	0	\$14,695	\$116,327
Percent of TEC.....	3.39	.90	1.01	0	.20	.61

¹ For Federal projects included in the Southeastern Federal power program, only 1966 data are available and such data were used throughout this report. For all others, balance sheet items are 1966-67 average.

² In deriving figures for Tennessee Valley Authority, short-term interest of \$12,735,000 was expensed out.

³ Capitalization figures for the U.S. Bureau of Reclamation projects are unavailable and therefore average net plant figures were used instead.

Note: Totals may not add, due to rounding.

Source: FPC, Statistics of Privately Owned Electric Utilities in the United States, 1967. FPC, Statistics of Publicly Owned Electric Utilities in the United States, 1966 and 1967. U.S. Department of Agriculture, Rural Electrification Administration, 1967 Annual Statistical Report, Rural Electrification Borrowers. (REA Bulletin 1-1.) U.S. Department of the Interior, 1967 Annual Report of the U.S. Columbia River Power System. U.S. Department of the Interior, Bureau of Reclamation, Power Systems, Average Rate and Repayment Studies, fiscal years 1966, 1967 and 1968. U.S. General Accounting Office, Comptroller General of the United States, Examination of Financial Statements of Southeastern Federal Power Program, Fiscal Year 1966. U.S. General Accounting Office, Comptroller General of the United States, Examination of Financial Statements, Southwestern Federal Power System, fiscal year 1967.

⁴ Capitalization data for federal projects were available only for the Columbia River, the Southeastern, the Southwestern and the Tennessee Valley Authority power systems. For others, the figure used was net electric plant. This ignores working capital requirements and thus leads to some understatement of the subsidy provided to such projects. In the case of the Power Authority of the State of New York (PASNY), net plant figures were unavailable as PASNY does not calculate depreciation. Both annual depreciation expense and accumulated depreciation were therefore estimated assuming a 50 year life for production plant and a 45 year life for transmission plant. Given this, net electric plant and comparable income figures for PASNY were calculated.

If the government-owned and/or financed sector had earned a gross rate of return equivalent to that earned by investor-owned firms (calculated as explained above), their 1967 gross earnings would have amounted to \$2,626,945,000, as compared with their actual income of \$979,883,000. (See Table 2.) The total deficiency (that is, the difference between actual and computed gross income) thus amounted to \$1,647,062,000. Of this total, \$1,115,530,000 is due to the direct tax deficiency and \$531,532,000 is due to the net operating income deficiency. Of the 1967 direct tax subsidy, \$585,609,000 was a federal income tax deficiency and \$529,921,000 was a deficiency in other taxes, chiefly property taxes.

The total subsidy as a percentage of total electric operating revenue amounted to 24.5 percent for the municipals, 34.1 per cent for the REA cooperatives, 98.8 per cent for the Power Authority of the State of New York and 125.8 per cent for federal projects. Stated another way, the total deficiency per kilowatt-hour sold in 1967 amounted to 2.83 mills for the municipals, 7.92 mills for the REA cooperatives, 4.69 mills for PASNY and 5.02 mills for the federal projects.

TABLE 2.—NET ELECTRIC INCOME AND TAX DEFICIENCY, GOVERNMENT-OWNED AND/OR FINANCED ELECTRIC UTILITIES, 1967

	[Dollar amounts in thousands]				
	Municipals	REA coops	PASNY	Federal projects	Total
Gross electric income:					
Computed.....	\$914, 196	\$567, 811	\$153, 811	\$991, 127	\$2, 626, 945
Actual.....	511, 154	205, 995	61, 187	201, 587	979, 883
Deficiency.....	403, 042	361, 856	92, 624	789, 540	1, 647, 062
Net electric operating income:					
Computed.....	485, 501	301, 546	81, 684	526, 357	1, 395, 088
Actual.....	451, 163	164, 314	61, 187	186, 892	863, 556
Deficiency.....	34, 338	137, 232	20, 497	339, 465	531, 532
Total taxes:					
Computed.....	428, 695	266, 264	72, 127	464, 771	1, 231, 857
Actual.....	59, 991	41, 641	0	14, 695	116, 327
Deficiency.....	368, 704	224, 623	72, 127	450, 076	1, 115, 530
Federal income taxes:					
Computed.....	203, 796	126, 579	34, 288	220, 946	585, 609
Actual.....	0	0	0	0	0
Deficiency.....	203, 796	126, 579	34, 288	220, 946	585, 609
Other taxes:					
Computed.....	224, 899	139, 686	37, 839	243, 824	646, 248
Actual.....	59, 991	41, 641	0	14, 695	161, 327
Deficiency.....	164, 908	98, 045	37, 839	229, 129	529, 921

Note: Totals may not add, due to rounding.

Source: FPC, "Statistics of Privately Owned Electric Utilities in the United States, 1967." FPC, "Statistics of Publicly Owned Electric Utilities in the United States, 1966 and 1967." U.S. Department of Agriculture, Rural Electrification Administration, "1967 Annual Statistical Report, Rural Electrification Borrowers." (REA Bulletin 1-1.) U.S. Department of the Interior, "1967 Annual Report of the U.S. Columbia River Power System." U.S. Department of the Interior, Bureau of Reclamation "Power Systems, Average Rate and Repayment Studies, Fiscal year 1966, 1967, and 1968." U.S. General Accounting Office, Comptroller General of the United States, "Examination of Financial Statements of Southeastern Federal Power Program, Fiscal Year 1966." U.S. General Accounting Office, Comptroller General of the United States, "Examination of Financial Statements, Southwestern Federal Power System, Fiscal Year 1967."

III. THE SUBSIDY PROVIDED BY FEDERAL AND BY STATE AND LOCAL GOVERNMENTS

In this section, we attempt to identify more specifically the sources of the total subsidy to government-owned and/or financed electric power systems by analyzing the components of that subsidy. The data available for such a breakdown are in many cases quite limited; therefore, many simplifying assumptions are employed. Despite this data limitation, we believe that the analysis does yield reasonable approximations to the actual figures.

We begin by attempting to identify the total costs that government-owned and/or financed electric utilities impose on the U. S. Government. The costs fall into four categories: (1) federal income taxes directly foregone; (2) federal income taxes foregone on debt and equity owner's income (referred to here as taxes indirectly foregone); (3) capital charges applicable to the U. S. Government's investment in federal projects and REA cooperatives; and (4) for the same projects, risk reduction costs. Computation of the first two cost components was relatively simple. Federal income taxes directly foregone were computed as before by applying the 1967 ratio of federal income tax paid to total electric capitalization of the investor-owned electric utilities to the electric capitalization of the government-owned and/or financed electric power systems. The results (shown on line 1 of Table 3) indicate a total of \$585,609,000 direct federal income taxes foregone. The net operating income that the government-owned and/or

financed sector would have required in order to earn a rate of return equivalent to investor-owned electric utilities was calculated in the same manner. In order to compute the federal income tax foregone on potential debt and equity holders' income, it is necessary to estimate the tax rate applicable to such income. We know that the net electric operating income of a given firm is distributed among interest payments, dividends and changes in retained earnings which becomes capital gains or losses to equity holders. In 1967, on average, investor-owned electric utilities paid out 78.8 per cent of their income before interest to debt and equity holders, while retaining 21.2 per cent. The tax rate assumed applicable to the income paid out is 38 per cent.⁵ In effect, we are assuming the personal income of potential electric utility debt and equity holders to be roughly the average for the total stockholding population in both level and distribution. Further, we assume the tax rate applicable to the change in retained earnings to be 19 per cent, thus reflecting the fact that the tax rate applied to capital gains is one-half the regular rate (up to a maximum of 25 per cent).

TABLE 3.—FEDERAL GOVERNMENT SUBSIDY TO GOVERNMENT-OWNED AND/OR FINANCED ELECTRIC POWER SYSTEMS, 1967

	[Dollar amounts in thousands]				
	Municipals	REA coops	PASNY	Federal projects	Total
COSTS					
(1) Federal income taxes directly foregone.....	\$203,796	\$126,579	\$34,288	\$220,946	\$585,609
(2) Federal income taxes indirectly foregone.....	164,934	102,441	27,749	178,813	473,937
(3) Capital costs.....		110,081		225,479	335,560
(4) Total monetary costs.....	368,730	339,101	62,037	625,238	1,395,106
BENEFITS					
(5) Federal income tax benefit.....		41,831		88,315	130,146
(6) Interest paid to Federal Government.....		64,039		152,723	216,762
(7) Net revenues after interest earned on Federal investment.....				27,244	27,244
(8) Total, monetary benefits.....		105,870		268,282	374,152
SUBSIDY					
(9) Net monetary subsidy (4)–(8).....	368,730	233,231	62,037	356,956	1,020,954
(10) Risk reduction cost.....		30,580		203,455	234,035
(11) Net Federal subsidy.....	368,730	263,811	62,037	560,411	1,254,989
(12) Percentage of total net Federal subsidy.....	29.38	21.02	4.94	44.65	100

Note: Totals may not add, due to rounding.

To summarize, federal income taxes indirectly foregone were computed by multiplying 78.8 per cent of the government-owned and/or financed sector's net operating income equivalent by an assumed 38 per cent personal income tax rate, with the remaining 21.2 per cent multiplied by a 19 per cent tax rate. The results of these calculations (shown on line 2 of Table 3) indicate federal income taxes indirectly foregone of \$473,937,000.

Capital charges applicable to the federal government's investment in federal power projects and REA cooperatives were calculated in the following way. First,

⁵ This was determined by relating dividends reported for 1967 to the taxable income of the recipients and then to the marginal tax rate applicable to such income levels. The analysis was based entirely on personal tax returns and thus ignores any corporate profit tax imposed on dividend income. This is partially offset by ignoring the fact that the first \$100 of dividends received by an individual are not subject to income tax. See, U.S. Department of the Treasury, Internal Revenue Service, *Statistics of Income 1967, Individual Income Tax Returns*, Washington, D.C., pp. 12, 58 and 222.

the government's 1967 net investment in each of these projects was determined. This was found to be \$7,014,601,000 for the federal projects and \$3,354,090,000 for REA cooperatives.⁶ Second, the interest rate appropriate to monies so invested was calculated. This involved ascertaining the timing of government investment in these projects and the rate of interest prevailing on U.S. Treasury long-term obligations at the relevant times. For example, over 44 per cent of the federal government's investment in the TVA occurred between 1951 and 1961, another 32 per cent occurred between 1941 and 1951, with the remainder occurring between 1941 and the initiation of TVA (1933).⁷ Further, we know that the average yields on long-term U.S. Government bonds were, respectively for these three periods, 3.265 per cent, 2.334 per cent and 2.270 per cent.⁸ With this information, the overall average interest rate applicable to the federal government's 1967 investment in the TVA was estimated at 2.785 per cent. This rate was then applied to the 1967 investment of \$1,780,092,000 to yield total capital charges to the government of \$49,576,000. Similar computations were performed for all federal projects and for REA cooperatives to arrive at the \$225,479,000 and \$110,081,000 figures shown on line 3 of Table 3.⁹

The last element of cost imposed on the federal government by government-owned and/or financed electric power systems is the risk reduction cost. We refer here to the capital cost savings made available to federal power projects and REA cooperatives as a result of the risk reduction which occurs when the federal government substitutes its capital-raising ability for that of the electric utilities themselves. To the extent that investors consider U.S. Government obligations less risky than the obligations of private electric utilities and will, therefore, accept a lower net return on investment, when the federal government raises capital on behalf of an electric power supply system, a benefit is conferred on that system. In effect, the government shifts to the general taxpaying public part of the risk associated with investing in an electric power system. Although no monetary outlay is involved, the value of this benefit can be estimated. This is so because the return demanded by a given investor must be used for two purposes: first, to pay his personal income taxes on that return; and second, to satisfy his net investment return requirement. At any given time, the latter, in turn, will be a function of the risk associated with various investments. Thus, risk differentials can be approximated by observing differences in net investment return requirements. These differences were computed as follows: (1) The ratio of net operating income to total electric capitalization for investor-owned firms was applied to the total electric capitalization of the REA cooperatives and the federal power projects to arrive at the net operating income equivalents for these systems. (2) From this, federal income taxes indirectly foregone were subtracted to yield computed net investment return required. (3) From the computed net investment return, actual net investment costs (U.S. Government's capital costs plus interest paid by TVA on publicly held long-term debt plus net profits on patronage capital earned by REA cooperatives minus federal income taxes levied on government capital cost payments and interest paid out by TVA) were subtracted to yield our final estimates.¹⁰ The federal government risk reduction costs, thus calculated, came to \$234,035,000 in 1967.

⁶ For the TVA, Columbia River, Southeastern and Southwestern projects, the figures used are net appropriations plus property transferred to power systems plus accumulated surplus. For Bureau of Reclamation projects, the figure used is net electric plant. For REA cooperatives, the figure is long-term debt owed by the cooperatives. Data for the Southeastern Power System are for 1966. For all others, data are 1966 and 1967 average.

⁷ Derived from data found in *Moody's Public Utility Manual*, various years.

⁸ *Standard and Poor's Trade and Securities Statistics, Security Price Index Record*, 1968, p. 213; 1942 data are the earliest available and therefore the 1942 rate was used for all pre-1942 calculations.

⁹ The timing of investment in REA cooperatives was determined by comparing "total funds advanced to all REA borrowers" at 10 year intervals beginning in 1937. The computed relevant interest rate is 3.28 per cent. Columbia River data are extremely poor. The specific timing of government investment prior to 1957 could not be determined, thus an interest rate of 2.5 per cent (roughly the 1942-1957 average) was assumed applicable to this period. The government's interest cost of Columbia River investment was thus estimated at 3.15 per cent. The timing of investment in Bureau of Reclamation projects and the Southeastern and Southwestern federal power projects was determined by comparing the balance of commercial power project costs to be repaid at 5 year intervals beginning in 1942. The interest costs thus calculated were 3.56 per cent for Bureau of Reclamation projects and 3.35 and 3.65 per cent respectively for the Southeastern and Southwestern federal power projects. It should be noted that this ignores any debt refinancing and thus probably underestimates the true capital costs.

¹⁰ The calculation of the last two items, federal income taxes levied on government capital cost payments and interest paid out by the TVA, is explained in the benefits discussion which follows.

Benefits flowing to the U.S. Government from government-owned and/or financed electric power supply systems originate from one of the following three sources: (1) federal income taxes levied on interest income generated by the Treasury's financing of federal power projects and REA cooperatives (and by TVA bonds); (2) interest payments to the government by government-owned and/or financed electric utilities; and (3) the net revenues after interest earned by federal power projects.

The first source of benefit to the U.S. Government is easily calculated. The total interest paid out to bondholders (capital charges) by the government in order to finance federal power projects and REA cooperatives has already been estimated. The total figure was \$335,560,000. All that remains then is to estimate the personal income tax derived from this interest income. To do this, we simply retain our assumption that, in the aggregate, a marginal tax rate of 38 per cent is applicable to bondholders. Applying this rate to the total interest paid yields a computed income tax benefit to the U.S. Treasury of \$127,514,000. Furthermore, in 1967 to TVA paid out \$6,925,000 in long-term interest. This we calculate to have yielded another \$2,632,000 in personal income taxes. Therefore, the total computed income tax benefit to the U.S. Government is \$130,146,000. Individual figures for the federal power projects and REA cooperatives are given on line 5 of Table 3.

The last two sources of benefit to the federal government can be taken directly from published sources. Long-term interest paid to the federal government by the REA cooperatives in 1967 was \$64,039,000. For the federal power projects the figure was \$152,723,000, while no long-term interest was paid to the federal government by municipalities. The final source of benefit to the government is the net revenues after interest earned by federal power projects. In 1967 this came to \$27,244,000. These figures are shown on lines 6 and 7 of Table 3.

The net subsidy provided by the federal government to government-owned and/or financed electric power systems can now be computed. The total monetary cost of such systems to the U.S. Government in 1967 was \$1,395,106,000; the contrasting benefit amounted to \$374,152,000. Therefore, the net monetary subsidy provided by the federal government to government-owned and/or financed electric power systems was \$1,020,954,000. When the non-monetary risk reduction subsidy is added in, the total subsidy is found to be \$1,254,989,000. Of this total, 29.4 per cent went to municipalities, 21.0 per cent went to REA cooperatives, 4.9 per cent went to PASNY and 44.7 per cent went to the federal power projects.

The tasks of computing the subsidy provided to government-owned and/or financed electric power systems by state and local governments remains. One simplifying assumption is made at the outset: state and local taxes on personal income are ignored. This is because such taxes vary widely on a regional basis and, in the aggregate, are not currently of major importance. Accounting for such taxes may, of course, become more important in the future if the trend toward increasing the scope and significance of non-federal income taxes continues. However, given this assumption, it is unnecessary to go through the process of computing indirectly foregone state and local taxes. Therefore, as calculated here, the only subsidy provided by state and local governments to federal power projects and REA cooperatives is the net local taxes foregone (strictly speaking: "taxes other than federal income taxes"). This tax deficiency has already been calculated in section II of this report (see Table 2). To repeat, the net state and local taxes foregone in 1967 were \$98,045,000 for the REA cooperatives and \$229,129,000 for the federal power projects. This, then, constitutes the total subsidy provided by state and local governments to these projects.

The computation of state and local subsidy provided to municipalities and to PASNY is more complex. The costs of these systems include not only net state and local taxes foregone (\$202,747,000), but capital costs and risk reduction costs as well. The capital costs were calculated in the following way. The average long-term interest rate paid by municipal electric utilities in 1967 was computed at 3.278 per cent. It was assumed that this rate accurately reflects the capital charges on state and local government proprietary investment in municipal systems—i.e., that proprietary investment grew at the same rate as the long-term debt of municipal systems and that, at any given time, the true

cost of such funds to state and local governments is the same as the cost of debt capital to municipal electric systems. Thus, the total annual capital charges imposed on state and local governments by municipal electric systems were calculated at 3.278 per cent of proprietary investment in electric operations (investment of municipality plus surplus multiplied by the ratio of net electric plant to total net plant plus investments). The local figure of \$107,449,000 is shown in Table 4. Similar assumptions were made for PASNY. The calculated relevant interest rate for PASNY was 3.78 per cent and the total computed capital cost came to \$6,439,000.

TABLE 4.—STATE AND LOCAL GOVERNMENT SUBSIDY TO GOVERNMENT-OWNED AND/OR FINANCED ELECTRIC POWER SYSTEMS, 1967

[Dollar amounts in thousands]

	Municipals	REA coops	PASNY	Federal projects	Total
COSTS					
(1) Net local taxes foregone.....	\$164,908	\$98,045	\$37,839	\$229,129	\$529,921
(2) Capital costs.....	107,449	-----	6,439	-----	113,888
(3) Total, monetary costs.....	272,357	98,045	44,278	229,129	643,809
BENEFITS					
(4) Net revenues after interest earned on State and local government investment.....	341,048	-----	23,336	-----	364,384
(5) Total, monetary benefits.....	341,048	-----	23,336	-----	364,384
SUBSIDY					
(6) Net monetary subsidy (3) — (5).....	(68,691)	98,045	20,942	229,129	279,425
(7) Risk reduction cost.....	103,003	-----	9,645	-----	112,648
(8) Net State and local subsidy.....	34,312	98,045	30,587	229,129	392,073
(9) Percentage of total net State and local subsidy.....	8.75	25.01	7.80	58.44	100

Note: Totals may not add, due to rounding.

The risk reduction costs imposed on state and local governments by municipal systems and by PASNY were calculated in the same basic manner as that used earlier to estimate federal risk reduction costs. The actual net investment return requirements of municipal electric utilities and of PASNY (state and local government capital costs plus interest paid on long-term debt utilized in electric operations) were subtracted from computed investor-owned utility equivalent net investment requirements (computed net income equivalent minus federal income taxes foregone). The reduction costs thus calculated amounted to \$112,648,000 in 1967. Thus, the sum of the costs imposed on state and local governments by municipal electric systems and by PASNY totals \$429,283,000, of which \$316,635,000 is a direct monetary cost.

Government-owned and/or financed electric power systems yield only one offsetting benefit to state and local governments—the net revenues after interest earned by municipal electric systems and PASNY.²¹ In 1967 this figure (electric utility operating income minus long-term interest paid multiplied by the ratio of net electric plant to total net plant plus investment) was \$364,384,000. When this is taken into account, it is found that State and local governments provided no monetary subsidy to municipal electric systems in 1967. In fact, in monetary terms, they benefited by \$68,691,000. In the case of PASNY, net revenues after interest were \$23,336,000 and the calculated net monetary subsidy provided by state and local governments was \$20,942,000. When the cost imposed on state and local governments by REA cooperatives and federal projects is taken into account, the total monetary subsidy is calculated at \$279,425,000. The inclusion of risk reduction costs brings the total subsidy figure up to \$392,073,000.

²¹ Additional benefits may be derived in the form of services such as free street lighting and free electric service rendered to state and local governments by municipal electric systems. In the FPC statistics, the value of most such services are credited to the appropriate revenue account and to this extent, these benefits are reflected in this report.

The following is a summary of the findings of this section. The federal government provided over 76 per cent of the total \$1,647,062,000 subsidy given to government-owned and/or financed electric power systems, with state and local governments providing the remainder. Translated into direct monetary losses, this amounted to \$1,020,954,000 by the federal government and \$279,425,000 by state and local governments. The greatest portion of both federal and state and local subsidies went to federal systems. Municipals received the second largest amount, the REA cooperatives received the third largest amount, while the least was received by PASNY. The total subsidy was divided among government-owned and/or financed systems in the following way: 47.9 per cent to federal projects, 24.5 per cent to municipals, 22.0 per cent to the REA cooperatives and 5.6 per cent to the Power Authority of the State of New York. These figures are summarized in Table 5.

TABLE 5.—FEDERAL, STATE, AND LOCAL GOVERNMENT SUBSIDY TO GOVERNMENT-OWNED AND/OR FINANCED ELECTRIC POWER SYSTEMS, 1967

[Dollar amounts in thousands]

	Municipals	REA co-ops	PASNY	Federal projects	Total
Net Federal subsidy.....	\$368, 730	\$263, 811	\$62, 037	\$560, 411	\$1, 254, 989
Net State and local subsidy.....	34, 312	98, 045	30, 587	229, 129	392, 073
Total subsidy.....	403, 042	361, 856	92, 624	789, 540	1, 647, 062
Percentage of total net Government subsidy.....	24.47	21.97	5.62	47.94	100

Note: Totals may not add, due to rounding.

IV. PROJECTIONS FOR 1980

According to recent estimates by the Federal Power Commission, the total peak load of the United States will reach 556 million kilowatts in 1980.¹² This contrasts with the 1967 peak of 217 million kilowatts.¹³ The projected 1980 peak is thus approximately 2.6 times the 1967 level. We have assumed that the distribution of this peak among the various sectors of the electric utility industry will generally conform to the present distribution, which has itself been stable for a number of years.

In order to simplify the projection of subsidies to 1980, it was assumed that the 1967 relationship between total electric capitalization and peak loads will be maintained. This implies either that there will be no technical change or price inflation, or, more reasonably, that these two elements will be offsetting. It follows that, if in reality, price inflation is dominant so that future capacity additions require increasingly greater capital outlays, then our capitalization estimates will be too low. Further, we assume that the association between capitalization and income, taxes and the like will remain stable.

Given these admittedly restrictive assumptions we estimate that the total subsidy received in 1980 by government-owned and/or financed electric utilities will be \$4,228,733,000. Of the total, the federal government will provide \$3,222,109,000, with state and local governments providing the remaining \$1,006,624,000. The 1980 projections are presented in Table 6.

TABLE 6.—FEDERAL, STATE, AND LOCAL GOVERNMENT SUBSIDY TO GOVERNMENT-OWNED AND/OR FINANCED ELECTRIC POWER SYSTEMS, PROJECTED TO 1980

[In thousands of dollars]

	Municipals	REA co-ops	PASNY	Federal projects	Total
Net Federal subsidy.....	946, 692	677, 319	159, 276	1, 438, 822	3, 222, 109
Net State and local subsidy.....	88, 094	251, 725	78, 530	588, 275	1, 006, 624
Total subsidy.....	1, 034, 786	929, 044	237, 807	2, 027, 097	4, 228, 733

Note: Totals may not add, due to rounding.

¹² U.S. Federal Power Commission, News Release No. 16323, September 24, 1969, Table 1.
¹³ Edison Electric Institute, *Statistical Yearbook of the Electric Utility Industry for 1968*, Table 6S. To achieve greater comparability with more complete FPC data, the 1967 EEI figure was adjusted upward to 216, 649 megawatts.

V. THE ECONOMIC EFFECTS OF SUBSIDIZING GOVERNMENT-OWNED AND/OR FINANCED ELECTRIC POWER SYSTEMS

The subsidy that is provided to government-owned and/or financed electric power systems, by making capital available below its true social cost (i.e., the minimum rate of return that investors will accept, including the funds necessary to pay all taxes normally levied on earnings), has clear effects upon the proper allocation of resources in the economy. Simply stated, artificially low capital charges induce overinvestment in the electric power industry. This may result in one of two basic ways: (1) by affecting utility decisions regarding how to satisfy a given demand for electricity; or (2) by influencing the level of demand for electricity. These effects are discussed below.

1. Given that there are differences in the rate of gross earnings required on capital, those firms with the lower capital costs (due to subsidy) will be encouraged to undertake uneconomical capital investment in order to realize operating cost savings. A few examples are illustrative.

First, assume that in designing a power plant, it is possible through the addition of capital to reduce fuel requirements by 100 Btu per kilowatt-hour. Further assume that 100 Btu have a value of .02 mills, and that 7,000 kilowatt-hours are produced annually by a kilowatt of capacity. Then the total yearly savings made available by the substitution of capital for fuel will be 14 cents per kilowatt of capacity. If carrying charges (capital costs plus depreciation) are 14 per cent per year, a firm would find it worth spending up to one additional dollar per kilowatt of capacity to achieve the savings. However, if the carrying charge is 5 per cent, the firm will find it worth spending up to 2.80 additional dollars per kilowatt of capacity to achieve the same savings.¹⁴ If the actual cost, therefore, lies between \$1.00 and \$2.80, the subsidized firm will make the economically undesirable additional investment. The results will be inefficient because the true social cost of capital will exceed the 14 cents saved per kilowatt of capacity.

An analogous case is the inefficient substitution of capital for labor. If the annual cost of one worker, say \$14,000, could be saved by additional plant-investment, the firm with the 14 per cent carrying charge would be willing to spend up to \$100,000 additional to achieve the saving, while the second firm would be willing to spend up to \$280,000 for the same saving.

Another example of the potential substitution of capital for operating expenses by government-owned and/or financed electric utilities concerns the decision to generate power or to purchase power. Assume that an investor-owned utility with 14 percent carrying charges has a 1,000 megawatt plant which was built at a cost of \$140 per kilowatt of capacity. Annual carrying charges are, therefore, \$19.60 per kilowatt of capacity or, assuming an annual output of 7,000 kilowatt-hours per kilowatt of capacity, 2.80 mills per kilowatt-hour. The wholesale rate charged by the investor-owned utility must cover this 2.80 mills plus other relevant costs. Assuming other costs equal, rather than pay this rate, a subsidized utility with a carrying charge of 5 percent per year will favor construction of a 50 megawatt plant at a cost of \$200 per kilowatt. Because of lower capital charges, the annual carrying charge per kilowatt-hour resulting from building the smaller plant will be only 1.43 mills (\$200 times 5 percent divided by 7,000). Thus, the subsidized utility will tend to build a 50 megawatt plant at a social cost of \$200 per kilowatt, rather than purchase a share of the output of the 1,000 megawatt plant which costs society only \$140 per kilowatt.

Artificially low capital charges will tend not only to encourage uneconomical investment in lieu of operating costs, but will tend as well to encourage electric power system investment at the expense of other social investments. This can be illustrated by an example from a Federal Power Commission report regarding development of the Chippewa River Basin.¹⁵ In this report, the Federal Power Commission, using identical total investment costs for the same project, arrives at the following annual costs:

By private financing-----	\$4, 442, 000
Financing by the Federal Government-----	1, 507, 000
Financing by the Rural Electrification Administration-----	1, 370, 000

¹⁴ In 1967 gross electric operating income averaged 13.8 per cent of total electric capitalization for the investor-owned electric utilities and only 5.1 per cent for the government-owned and/or financed sector. (See Table 1.) If we assume that these are the rates of earnings required by investors and further assume a depreciation rate of 3 per cent annually, then computed carrying charges for investor-owned public utilities averaged 16.8 per cent in 1967. The corresponding figure for the government-owned and/or financed sector was 8.1 per cent.

The Rural Electrification Administration obtains its funds from the federal government at a fixed interest rate of two per cent, irrespective of the cost to the federal government of borrowing such funds. In this particular case, the cost of the federal government financing was based on an interest rate of 3.125 per cent, while for private financing, 6.25 per cent was the rate of interest used. In the case of the federal government, no cost representing taxes foregone was included. For the Rural Electrification Administration, 0.5 per cent was allowed for taxes or payments in lieu of taxes. For private financing, 5.72 per cent was included for federal and other taxes. In all cases, the computed annual benefits were the same—\$2,648,000. Thus, the benefit-cost ratios were: for REA financing 1.93; for federal financing 1.76; and for private financing 0.60. This computation indicated that, on the basis of private financing, the project was economically infeasible. Indeed, it indicates the paradoxical result that with REA financing the project has greater feasibility than if the project were carried out by the federal government from which the REA obtains its funds. Thus, with exactly the same installation, the same use of real resources, and the same benefits, the calculated economic desirability of the project varied not only in degree, but even to the extent of changing it to undesirable, depending upon the financing source (i.e., the level of subsidy) which was contemplated.

2. The second major way in which excessive electric utility investment may be encouraged by artificially low capital charges is through influences on the demand for electricity. The effect of lower electric rates made possible by low net capital costs and freedom from taxes is to encourage greater use of electricity relative to other goods and services in the economy. This occurs directly to the extent that the low-rate utility's customers may be induced to substitute electric power for other energy sources. Further, however, energy intensive firms in the low-rate area obtain a competitive advantage, by virtue of their location, which enables such firms to offer their product on better terms. As the sales of these firms increase, their corresponding demand for electricity increases. To meet increased demands for electricity, it is necessary to overinvest in electric power facilities. Again, the additional investment is uneconomical in that the rates charged are not sufficient to cover all the true costs of production.

Along this same line, it is clear that the existence of a subsidized government-owned and/or financed electric power sector discriminates in favor of retail customers located in the areas served by the subsidized utilities and in favor of the ultimate consumers of the output of power intensive industries so located. Furthermore, it is clear that the subsidy provided to a given customer is proportional to his level of use. Thus, high use, and, therefore, high income customers tend to benefit most as a result of the subsidy.

Mr. KUDER. Before I get to the statement I would like to make one comment on the bill here. I would ask you to turn to page 4 of the bill, line 18. That is in section 3 that provides for judicial review. Line 18 reads, "this shall include the customers of projects referred to in this act."

Now, if you will please look at page 2 of the bill, lines 3 to 5, the bill mentions public agency customers, and I would request that utility companies be included, specifically included as customers. That could be done by striking the word "aa" at the end of line 4. I think that is a typographical error, and amending line 5 to read, "State and Federal agencies and utility companies;" that would clear up what may be an ambiguity in the bill about the right of a utility company customer under the bill to have judicial review.

Mr. JOHNSON. That is a good suggested amendment.

Mr. KUDER. What I would like to do, Mr. Chairman, in the interest of time is to read only the first two and a half pages of my statement.

Mr. JOHNSON. Very well, sir. I hope you will read—we don't have any amplification in here and you are a long ways from us. If you would read just a little loud if you do so, we could hear what you have to say.

Mr. KUDER. All right.

Pacific Gas & Electric Co. (P.G. & E.) purchases power from the Bureau of Reclamation's Central Valley project under a power sale interchange and transmission contract. Changes in rates under this contract would be subject to Federal Power Commission approval if H.R. 14221 is enacted.

In connection with hearings on proposed Central Valley project rate adjustments held last January by the Subcommittee on Conservation and Natural Resources of the House Committee on Government Operations, several questions were asked concerning transactions under the Bureau-P.G. & E. contract. We wish to submit for the record before your committee our answers to these questions and to point out some of the benefits to Central Valley project preference power customers of the power support and "banking" provisions of the contract.

P.G. & E. provides firming support which enables the Bureau to serve firm loads up to 985,000 kilowatts until 1975 and then up to 1,050,000 in 1980 and each year thereafter. According to Bureau studies, the Bureau could serve only about half of this preference customer load without P.G. & E. support.

With this support the Bureau can serve additional customer load at CVP rates. Assuming that both the proposed CVP average rate of 6 mills per kilowatt hour and the current P.G. & E. wholesale average rate of 11 mills continued without change from 1974 to 2004, the Bureau customers would save about 5 mills, or more than \$450 million during the remaining life of the contract, by being able to purchase power from the Bureau instead of from P.G. & E.

Under two "banking" provisions, capacity and energy sold by the Bureau to the company can be repurchased by the Bureau whenever it is needed for preference customers. The repurchase price is the price the company paid plus or minus the difference in cost to the company of producing power in company plants between the time power was purchased by the company and the time power is sold back to the Bureau and plus a reasonable service charge. Thus, the rate for the sale of power to P.G. & E. is directly reflected in a low price for repurchase of power by the Bureau.

Under a third "banking" provision, the company is obligated to sell nearly 15 billion kilowatt hours of energy to the Bureau for at least \$70 million less than the company's present cost of producing it, and the amount of this loss will undoubtedly become greater with time.

Several Bureau preference customers have complained of a provision in the contract under which the Bureau loses money on sales of Centralia power to the company. During the period fiscal year 1972 through fiscal year 1976, the Bureau will sell this power, not only to P.G. & E. but also to the Bureau's preference customers, for less than the Bureau paid for it. The Bureau will lose \$30.7 million from sales to preference customers and \$18.8 million from sales to the company.

Preference customers which complain of a loss to the Bureau from the sale of Centralia power to P.G. & E. have overlooked the greater loss the Bureau incurs from sale of this power to these customers. They also have ignored the substantial benefits they receive from other provisions in the contract and have failed to recognize that the company is required to sell power to the Bureau at less than cost under the same contract. On balance, more benefits from these transactions accrue to the preference customers than to the company.

In the last half hour I have listened to statements of Mr. Gillmor and Mr. McDiarmid and Mr. Westfall. I would like to touch on some of the points they have raised plus some other points the committee is interested in, but also I request permission, if it appears to be necessary, to file a written response after I have had a chance to review their comments.

Mr. JOHNSON. I might say, Mr. Kuder, the record will be open for additional comments for a certain period of time, and therefore any witnesses that have appeared here this morning who want to revise and extend their remarks, there will be an opportunity to do so and they will be received and printed in the record.

Mr. KUDER. Thank you, Mr. Chairman.

I have these statements here, and have underscored some of the points that were made just at random. I would like to take the statement of Mr. Spiegel, which Mr. McDiarmid read, and go to page 10 of his statement at the bottom where he says that power will be sold by the Bureau to P.G. & E. "at substantial losses, thereby resulting in an enormous subsidy to P.G. & E."

P.G. & E. buys power from the Bureau at the Bureau rates, and it buys energy from the Bureau at the Bureau rates, but it doesn't make any profit on reselling that power and energy to its customers. The cost of purchased power is an operating expense just like the cost of fuel or the cost of wages or any other operating expense, and under public utility regulation in California that cost is passed on to the customer without any margin or markup or profit. Whenever the company buys energy, we will say, from the Bureau at less than it would cost the company to produce the same energy in its plants that benefit is passed on to the P.G. & E. customers in the form of rates lower than they would otherwise have been. And I refer you, please, to pages 22 to 25 of my long statement. This is where we point out that there isn't any profit to the company from purchase of this subsidized Federal energy.

At page 24 of my statement we come to a second point which I would like to make, and that has to do with the rate at which the company sells energy back to the Bureau from an energy account No. 1. That energy account was established some years ago, and what it is is all the kilowatt hours that were surplus to the needs of preference customers beginning in 1951, in December of 1951. Thereafter for several years the Bureau had more energy than it could sell to those preference customers and it sold the energy to P.G. & E. Those sales were made at low Bureau rates, about 2.4 mills. During that period of years the cost of producing the same amount of energy in the company plants was more. It wasn't much more, but there was a saving there of about .33 mills on each kilowatt hour. That surplus built up over the years and right now there are over 12 billion kilowatt hours in that account. During that period of time, because the customers of P.G. & E. got this energy with a saving of .33 mills they saved a total of about \$5 million. However, the contract requires the company, whenever the Bureau wants the energy, to sell it back and the price is established at 2.81 mills.

Now, let's move for a moment to the increased cost of Centralia. Centralia costs more now than anybody thought it would in 1967 when the contract was executed, or, indeed, in 1970-71 when the question arose that the Bureau might want to have a review of the rate. No one

knew that the cost of coal-fired power at Centralia was going to more than double, which it has done, and that is why you have these losses to the Bureau from the sale of Centralia power.

Also, in 1967, no one had any idea that the cost of oil was going to have a dramatic rise. As a consequence, although there has been a difference in the price that P.G. & E. pays for Centralia and the cost of Centralia, there has been a much wider difference in the price at which P.G. & E. sells this energy at 2.81 mills and the cost of oil to produce it.

Now, I filed some answers, which are in my statement. They were prepared last November. In estimating the difference in cost between the 2.81 mills and the equivalent cost of oil at that time I used a figure of 9 mills. It cost the company 9 mills to generate this energy to sell back. That was based on a cost of oil at \$6 a barrel.

Shortly after I filed those answers the oil costs, as you well know, began to rise. Just last week when I was putting together this material I asked our engineers what the latest cost of oil was, and I have a footnote here, page 25 of my statement, that during this present quarter of 1974, the oil we now buy to replace oil in storage that is being used to generate power is \$15 a barrel, and that is the equivalent of about 23 mills per kilowatt hour.

So, when you look at the difference in cost of Centralia and what it sold for—I respectfully ask you to look also at the difference in cost between what P.G. & E. has to sell this energy for, 2.81 mills, and goodness knows what the cost is going to be over a period of years. I would suggest that probably 9 mills is too low. I would certainly hope that 23 mills is too high. But somewhere in that range there will be a difference, by the time all the energy is sold from that account, of something over, perhaps a lot over, a \$100 million.

So this loss from sales of P.G. & E. energy to the Bureau should be taken into account when you consider what the Bureau's Centralia losses are, and it far more than outweighs and outbalances those losses.

As Mr. Westfall pointed out, under this contract, and you will get a copy of it from Mr. Westfall, if there is any disagreement between the company and the Bureau on these rates, it goes to the Federal Power Commission. So this matter that I am talking about briefly this morning, and all the matters that Mr. Westfall is talking about, will be, I am sure, as far as the contract is concerned, subject to review and modification by the Federal Power Commission. I am not in a position to litigate the issues before this committee this morning, and I assume you don't want me to.

Now, again, looking at some of the statements we have here, I glanced at Mr. Westfall's summary statement. At the bottom of page 4 he points out or says that there are serious questions as to the availability of power from the Northwest in 1982, and the Bureau has an alternative source available to it which is lower in cost. And he says the source is P.G. & E.

Well, without going into it, I would like to say that our engineers disagree with his figures, and again, without reading it, I would ask you to look at our comments on our long statement at the top of page 18. One of the points, and goodness knows, Mr. Westfall has many others which I can't even address in the time allowed this morning, is, or was at least, that Mr. Westfall was using the figure of 5.35 mills in

his estimates, and he also assumed that 25 percent of the fossil fuel used by P.G. & E. in the sale of this power will be natural gas. Well, I have already gone into the uncertainty of oil prices. We think we don't have any natural gas available for power generation after this year. So that shouldn't be a factor in these figures.

Now, there is always, and there was before the other committee, too, and Mr. Westfall brought it up this morning, a question of this bank account and whether it would ever be used. When the contract——

Mr. JOHNSON. Sorry. You have about 4 minutes to get it into the record because we have to leave and adjourn because the House is now called into session.

Mr. KUDER. I better stop.

Mr. JOHNSON. Well, you can submit——

Mr. KUDER. I will be happy to discuss any of these things I am competent on with you—about the bank account, one or two words.

The thought was in the Pacific intent when we built these several hundred million dollars of lines, the Federal Government, P.G. & E., and other companies joined together to connect with the Northwest, there would be other additions to the Central Valley project. I am not talking about Auburn or New Melones or Marysville. What I am talking about is the East Side Canal and the East Side system.

Mr. JOHNSON. That is further away than the other two projects. You can forget them for the next 20 years as far as the East Side Canal.

Mr. KUDER. This is history, Mr. Johnson. The purpose of the bank account was to take care of these future additions.

If it is decided that they are not going to be made, or if it is decided that the Bureau doesn't need the bank account, of course the company should be relieved of the obligation of maintaining it. That is all I am going to say.

The reason, as I understand it, that the bank account was ignored in the present rate adjustment study of the Bureau was that they were only looking at authorized projects and the East Side is not authorized.

I am sure I missed many important points here, Mr. Chairman. Is there something you particularly wish that I address?

Mr. JOHNSON. Well, you have the right to prepare and submit to the committee, and it will appear in the record, any other statement that you want to make. I am very sorry, but we have to go and answer the bell and make the quorum and on Monday it is very necessary to show up because we just barely have a quorum on Mondays. You being an expert witness here with many things in here that possibly we would like to have more time with, but I am sure our consultant here will go over this very carefully and it will be printed for many other experts to take a look at.

Mr. KUDER. Some of the other committee members, in the Reuss committee, did send questions to us and we answered those questions. They are in here. Your committee may wish to do the same thing.

Mr. JOHNSON. We probably will if we have need for further questions to be put we will put them to the proper witnesses appearing before this subcommittee.

As I say, anyone who has testified here, you have a perfect right to submit written rebuttal to anything that was said here or anything further you would like to say and it will be made a part of the record but we should have it within 10 days.

Mr. KUDER. We will attempt to answer any questions you submit to us within 10 days.

Mr. JOHNSON. There is a lot we would like to go into, but not being as much of an expert as the people who testified here, it is kind of hard for a layperson to get hold of this thing. But certainly the contracts that were made and are now in effect and agreed to by parties, namely, the Pacific Gas & Electric Co. that you referred to, the Bureau of Reclamation as it related to your contract with Centralia as well as the contract with the Central Valley system, and as you stated these were subject to review and were reviewed by the Federal Power Commission. As far as I know, the reviews were held and the agreements were made between you and the Bureau of Reclamation, and I don't know whether there was formal Federal Power Commission hearings held where everyone had an opportunity to participate or not. They may have reviewed the results of your negotiations with the Bureau and the company. I am not sure of this. I don't know.

Mr. KUDER. Well, Mr. Johnson, hearings were not held, but the reviews—

Mr. JOHNSON. We have to go. This is our second one.

We are going to adjourn the hearing because we have another committee that has to take over here right after they get released from the House floor.

We are very sorry we have to break this up, because as I say, there is lots to this that a layperson has a hard time understanding.

[The statement of Mr. Armstrong plus letter from George Spiegel, special counsel to the Northern California Power Agency, to Hon. Harold T. Johnson, with rebuttal statement of Northern California Power Agency to statement by William B. Kuder, Pacific Gas & Electric Co., and a letter from William B. Kuder, to Hon. Harold T. Johnson, with Pacific Gas & Electric Co.'s answer, follow:]

STATEMENT OF RICHARD T. ARMSTRONG, GENERAL MANAGER, PLAINS
ELECTRIC GENERATION AND TRANSMISSION COOPERATIVE, INC.

My name is Richard T. Armstrong and I am General Manager of Plains Electric Generation and Transmission Cooperative, Inc.

Plains is a wholesale supplier of electric power and energy to eleven distribution cooperatives centered in New Mexico and to the Salt River Project of Phoenix, Arizona.

Plains headquarters is at 2401 Aztec Rd. N.E., Albuquerque, New Mexico and Plains consumers in New Mexico occupy approximately 75% of the New Mexico area and comprise approximately one-third of the New Mexico population.

The service areas of our members in New Mexico vary between rich grass lands for cattle to semi-desert areas in which economic activity is severely limited. Our members serve ultimate consumers ranging from some of America's largest corporations to the economically depressed.

Many of our members systems make little or no margin (profit). The net depreciated value of Plains Electric plant is \$13,992,439.80 and our outstanding indebtedness is \$14,152,542.54.

Plains is facing the problem of meeting the ever expanding energy requirements of its members, faced by the problems of unavailability of full governmental loans, inflation and environmental concerns.

The cost of power is vital to the financial integrity of our system. The cost of power is a necessity to the economical development of our members reasonably priced power. Inded the economically distressed areas of our state, which many of our members serve, are living laboratories of the beneficial effects of reasonably priced electricity upon the every day lives of New Mexicans and their social and economical betterment.

On behalf of Plains, its members and the future of New Mexicans served by its members I have viewed with great concern the increase in contract rates for

electric power sold to customers of the Bureau of Reclamation, Colorado River Storage and Rio Grande Projects. In connection there with Plains appeared before Bureau purported hearings and has raised objections substantially the same as you have heard by other consumers during the hours of these hearings. On behalf of my organization and those that it directly and indirectly services I heartily endorse HR 14221. This bill we feel offers a sensible and practical approach to solving a problem of unreasonable rate increases, unreasonably determined.

Thank you for the opportunity to appear before your committee.

POSITION STATEMENT OF PLAINS ELECTRIC GENERATION AND TRANSMISSION
COOPERATIVE, INC.

We believe the Bureau of Reclamation has failed to present sufficient evidence to justify this inflationary increase in a commodity as basic to the economy of the Plains area in New Mexico as electric power.

We believe that the time between the announcement of the proposed increase and implementation of the increase was woefully inadequate for determination by Plains and of other preference customers of the Bureau to make a determination of the justification for the Bureau action. There was also insufficient time to make an indepth study of the economic affect on the people of New Mexico.

We believe that the assignment of investments and payback schedules for electric generation, water, irrigation management, and recreational functions do not now reflect a proper distribution of investments. We feel that the Environmental Department of Fish and Game should bear a portion of the project costs. We feel that the users of basic needs, such as electric facilities, can no longer afford to bear this maladjustment of assigned capital and operating costs.

The costing criteria includes facilities planned far into the future. We feel that the Preference Customers should be presented several comprehensive studies. These studies must include the cost allocation of facilities now in existence; the feasibility and cost allocation of both facilities presently authorized and funded; and those facilities authorized, but not funded; and, their relationship to the repayment schedule.

We believe that the proposed 500% penalty charge for overruns on contract rate of delivery is both arbitrary and excessively punitive. We appreciate the Bureau's need to encourage its customers to arrange supplemental power sources, but, we believe this 500% penalty is a form of financial overkill.

Since ultimately the burden of this proposed increase will be borne by the individual power consumers, we believe that their representatives in Congress should carefully evaluate the impact of this and future increases on the rural, municipal, and urban power consumers and the economy, as a whole, of the people of New Mexico.

SPIEGEL & McDIARMID,
Washington, D.C., June 6, 1974.

Hon. HAROLD T. JOHNSON,
Chairman, Subcommittee on Water and Power Resources, Committee on Interior and Insular Affairs, U.S. House of Representatives, Washington, D.C.

DEAR CHAIRMAN JOHNSON: Enclosed is the Rebuttal of Northern California Power Agency to the Statement by William B. Kuder, Assistant General Counsel, Pacific Gas and Electric Company, Before the Subcommittee on Water and Power Resources of the House Committee on Interior and Insular Affairs on H.R. 14221. We request that the rebuttal statement be made part of the record in the hearing on H.R. 14221 as contemplated by your statement at page 179 of the hearing transcript.

The Northern California Power Agency appreciates the opportunity it was accorded to testify at the hearing on H.R. 14221 and the opportunity to submit the enclosed rebuttal statement.

Sincerely,

GEORGE SPIEGEL,
*Special Counsel to the
Northern California Power Agency.*

REBUTTAL OF NORTHERN CALIFORNIA POWER AGENCY TO STATEMENT BY WILLIAM B. KUDER, ASSISTANT GENERAL COUNSEL, PACIFIC GAS AND ELECTRIC CO., BEFORE THE SUBCOMMITTEE ON WATER AND POWER RESOURCES OF THE HOUSE COMMITTEE ON INTERIOR AND INSULAR AFFAIRS ON H.R. 14221

INTRODUCTION

Northern California Power Agency ("NCPA")¹ has shown in the testimony of its special counsel, George Spiegel, and its consultant, Herbert C. Westfall, (i) that the Bureau adopted improper procedures in considering its proposed \$6,000,000 increase of Central Valley Project rates to its preference customers, and (ii) that the known facts demonstrate that no increase could be justified. Among the factors involved is the fact that no increase would be necessary if Pacific Gas and Electric Company ("PG&E") were required to pay the full cost of the capacity and energy which CVP purchases from the Centralia, Washington, steam plant and resells to PG&E at a loss of some \$6,000,000 per year. The preference customers should not be required to subsidize a loss sale to PG&E.

Mr. Kuder's statement, insofar as relevant, deals with that point, and does in fact concede that there is a loss on this resale to PG&E, but in a lesser amount. He also indicates that PG&E is willing to pick up approximately \$500,000 of this loss by accepting a complicated billing reallocation of power sources, which presumably should result in reducing the preference customers' increase by at least that amount.

Beyond this, Mr. Kuder's statement seeks to justify PG&E's side on many other issues under the USBR-PG&E interconnection agreement,² in cases where NCPA believes PG&E has overreached the Government. Part of the discussion seems to be an effort to create legislative history to support its interpretation of controversial provisions. Finally, the statement raises the broad issue of *private power v. public power* and offers an extensive private industry report on the subject.

They deal with the basic fairness and propriety of the USBR-PG&E Interconnection Agreement which will eventually be resolved in some other forum. Therefore, we do not answer these in depth.

NCPA in this statement answers point-by-point Mr. Kuder's major points—there is question whether this Subcommittee should get involved in many of these substantive matters in connection with H.R. 14221 which is directed to what procedures should be accorded.

It is enough that the failure of the Secretary of the Interior to provide a fair and open hearing, and a reasoned, supported decision, demonstrates the need for the passage of the proposed legislation (H.R. 14221) in order that these can be obtained before the Federal Power Commission.

FIRMING SUPPORT

PG&E is *not* supporting preference firm loads at 985,000 kw but is refusing to support this level. It is only supporting 925,000 kw. As a result preference customers are having allocations improperly withdrawn. (See Statement of George Spiegel to "Reuss" Subcommittee,³ pages 15-16). On the basis of a proper interconnection arrangement, CVP could serve a substantially larger firm preference load. The Bureau studies referred to by Mr. Kuder relate to loads that could be served by CVP as an isolated system, and therefore are irrelevant. The project, with its \$243.6 million investment in electric plant facilities capable of generating 1,471,200 kw was planned to operate on an interconnected basis with other

¹The Northern California Power Agency is a public agency in California created under California law by a joint powers agreement among eleven cities in Northern and Central California and acts in their behalf with regard to electric power supply matters. The members of NCPA are the cities of Alameda, Biggs, Gridley, Healdsburg, Lodi, Lompoc, Palo Alto, Redding, Roseville, Santa Clara and Ukiah. The Plumas-Sierra Rural Electric Cooperative, Inc. is an associate member.

²United States Department of the Interior, Bureau of Reclamation, Central Valley Project, California, *Contract with Pacific Gas and Electric Company for the Sale, Interchange and Transmission of Electric Capacity and Energy*, Contract No. 14-06-200-2948A.

³Subcommittee on Conservation and Natural Resources of the House Committee on Government Operations, Hearings January 22, 23, 1974.

utilities—not on an isolated basis. The fact is that the preference customers, even at 985,000 kw, are not getting the benefit of the full firm capacity available from this hydro plant, even ignoring the additional 400,000 kw of capacity delivered to CVP from the Centralia steam plant (See NCPA's Detailed Response to Reuss Subcommittee, pages 65-71).

ILLUSORY BANKING

Mr. Kuder misstates facts as to the so-called "banking of capacity and energy." CVP studies show that no capacity will ever be repurchased by it from PG&E. Indeed, up to the present time, the Bureau has been refusing to repurchase such capacity in order to sell it to preference customers. It now amounts to 1,361,000 kw-years, i.e., sufficient capacity to serve a 100,000 kw load for over 113 years, or a 400,000 kw load for 28 years. Since it will never be repurchased, the Government can never get any benefit from selling capacity to PG&E at rates below cost. It loses money forever on capacity.

Moreover, PG&E misstates the basis for establishment of the repurchase price, as well as the total economic benefits to PG&E from the third banking provision.

PAYMENT FOR CENTRALIA CAPACITY

Preference customers have never objected to including in their rates the cost of any portion of Centralia capacity and energy supplied to them. Under their contracts with the Bureau they purchase all power under a single rate schedule; and it is recognized that, to the extent project capacity is considered insufficient to meet preference loads the balance is made up out of Centralia capacity. This has been zero through fiscal 1973, and estimated to grow to 117,000 kw. However, under its contract with the Bureau, PG&E purchases project power and off-project power (i.e., Centralia) under two separate rate schedules, and the Bureau has always billed PG&E on this basis (until a change in this method was considered in a *secret* conference after the November 1, 1973 Bureau announcement of the current rate increase). On this established basis, for the period FY 1972 through FY 1976, the Bureau will lose \$34,440,000 on the sale to PG&E. The preference customers absorb the balance of the Centralia costs in their rates—what they are here objecting to is absorbing additionally the \$34,440,000 subsidy to PG&E.

BALANCE OF BENEFITS

Contrary to Mr. Kuder, on balance more benefits from its transactions with CVP accrue to PG&E than to the preference customers.

IMPROPER FAILURE IN 1971 OF BUREAU TO SEEK INCREASED RATE ON PG&E PURCHASES OF CENTRALIA POWER

The Government's contracting officer, with knowledge of rapidly escalating costs for Centralia power, improperly failed to invoke the Government's contract right to seek an increase in the price for capacity and energy sold to PG&E "from sources other than Project generation" (Art. 22(b)(2)) on the specific contract review date of April 1, 1971 (Art. 32—joint review subject to FPC determination in event of dispute). The Bureau has been unable or unwilling to furnish any information or documentation stating who made this determination for the Government (if any was ever made), when, and the circumstances and basis thereof. Thus, the Government contracting officer has never revealed the facts for silently passing the review date, and thus imposing a five-year loss of \$34,000,000. Mr. Kuder's speculation and attempted rationalizations are not a substitute for a full disclosure by the Department of the Interior and the Bureau of Reclamation.

For a detailed discussion of this matter, see NCPA Detailed Response to Reuss Subcommittee (pages 44-51) and see George Spiegel Statement to Reuss Subcommittee (pages 16-19).

SELLING ELECTRICITY TO PG&E AT A LOSS LOSES GOVERNMENT MONEY

Mr. Kuder argues that the Government saves money by selling capacity and energy today at a low price (actually at a loss) because they are banked, and can be repurchased years later by the Government at a price, one element of this being the price into the bank. This is demonstrably incorrect.

(a) Capacity sold into the Capacity Account is never to be repurchased according to Bureau estimates. Therefore, a loss on the sale is a loss forever.

(b) Energy sold into Energy Account No. 2 will be repurchased an average 20 years later. The higher the price into the bank, the greater the repayment of project electric plant investment, and therefore a net reduction in the outstanding principal upon which interest is charged as part of the price for power sold to preference customers. To the extent that the price into the bank is lower, there results an increased burden on preference customers, of paying more interest on plant investment. The average interest rate of the project is somewhat greater than 3%. Three per cent compounded over 20 years makes a total of 80.6% interest on every dollar not charged to PG&E when energy is sold into the bank.

Moreover, the USBR-PG&E interconnection agreement is so badly worded that no one knows for sure, and no parties agree, as to what the actual price will be for energy repurchased out of the Energy Account No. 2. The contract (Art. 22(c) (2) (ii)) places this repurchase price at the "current average rate [i.e. the price sold to PG&E] plus a service charge, both modified to reflect any adjustment made pursuant to Article 32", i.e., adjusted monthly to reflect the changes in costs of energy from the "thermal generating units" added to PG&E's system "during the preceding 5-year period" (Art. 22(c) (1) (ii)). The Bureau estimates that the service charge will be a mere 14% as the total repurchase surcharge. Mr. Kuder, however, in his example on pages 7 to 8, calculates a surcharge of 2 mills, "plus the service charge" (undefined). In Mr. Kuder's example, he started with a price to PG&E of 3 mills, so that his 2 mill adder represents a 66% surcharge, and he still has a claim for an undefined service charge. This difference is substantial, and illustrates the financial jeopardy to the Government in pricing energy at less than cost into PG&E's so-called "bank".

It should be noted that PG&E is quietly seeking to establish here some legislative history as to how this ambiguous contract provision should be interpreted. As preference customers, we cannot accept Mr. Kuder's interpretation.

These matters are discussed in greater depth in NCPA's Detailed Response to the Reuss Subcommittee (pages 40 through 42).

THE MYSTERY OF THE LOST LOAD CURVES

The CVP project has a generating capacity of 1,471,200 kw, but under the contract the Government has accepted a so-called Project Dependable Capacity of 925,000 kw (and this in effect limits the amount of capacity which can be sold to preference customers). The balance of the capacity (after project use) is being made available free of charge to PG&E under the Bureau's interpretation (approximately 500,000 kw, see NCPA Detailed Response to Reuss Subcommittee, pages 65-69). In short, this is a critical determination which now controls:

- (a) how much power will be sold to preference customers;
- (b) how much power can be sold at a price; and
- (c) how much capacity PG&E gets for free.

There is a mystery as to the details of the calculation or determination of Project Dependable Capacity, and Mr. Kuder's explanation only deepens that mystery. He says that the 1967 capacity figure (925,000 kw) was not based on 1967 load curve data. There was a determination for the original 1951 contract, and modifications were made in the 1955 and 1963 amendments. Then he continues (page 9):

"Load curve data used in calculating these capacity factors were not retained in our files."

The PG&E information void is matched by the Reclamation-Interior void; NCPA's repeated requests to the Bureau for the data underlying the 925,000 kw Project Dependable Capacity were completely unsuccessful: neither the Bureau or Interior has any such data, nor could any official be identified as familiar with the data. All NCPA could discover is a cryptic statement in a letter of November 17, 1967 from the Bureau to PG&E purporting to state the date upon which the 925,000 kw would be effective. This letter references a meeting in the office of PG&E's President S. L. Sibley at which "a final review and agreement was reached on the test data and related information for determination of Project Dependable Capacity."

Where is that "test data and related information?" The Bureau has been unwilling or unable to furnish it upon request either by NCPA or by the Reuss Subcommittee. And Mr. Kuder, PG&E's Assistant General Counsel, states that these materials "were not retained in our files." This Subcommittee can take official notice of the fact that PG&E has vast and extensive files, and some explanation should be forthcoming as to why these important documents were discarded.

As to the Government contracting officer, the lack of such data raises a serious question. It is as though a Government contracting officer negotiating a contract for the purchase of aircraft had no cost documentation to support the determination of a price in the order of many millions of dollars.

To make matters worse, Mr. Kuder states that "the capacity factors used in the 1963 amendment to the 1951 contract would be . . . applied . . . in all future determinations of Project Dependable Capacity" (page 10). In short, unknown data will be blindly applied in future redeterminations. This may be a proper way for private businesses to negotiate, but it is an improper method of disposing of federal government assets.

CUSTOMERS SHOULD BE PERMITTED TO PARTICIPATE IN CURRENT USBR-PG&E NEGOTIATIONS TO REDETERMINE PROJECT DEPENDABLE CAPACITY

Mr. Kuder states that "We are currently conducting a redetermination of Project Dependable Capacity." This is another closed-door negotiation between the Bureau and PG&E from which NCPA's representatives are excluded—although in the final analysis the preference customers will bear the burden of whatever the Bureau representatives accept. His statement indicates very clearly that PG&E is unreasonably narrowing the scope of the redetermination, and we believe that the Bureau may improperly acquiesce in such procedure. We believe that the public interest will best be served if representatives of the preference customers can participate.

PG&E AND BUREAU ARE IMPROPERLY DEPRIVING PREFERENCE CUSTOMERS OF 60,000 KW OF PREFERENCE POWER LAWFULLY DUE TO THEM

Under the USBR-PG&E Interconnection Agreement, PG&E has agreed to support 985,000 kw of preference customer firm loads (Art. 14(a)(2)) and on page 1 of Mr. Kuder's statement it is said that "PG&E provides firming support which enables the Bureau to serve firm loads up to 985,000 kilowatts until 1975." Nonetheless, preference customers are having their allocations withdrawn by the Bureau on the contention that PG&E will only support a total of 925,000 kw of preference customer load. Mr. Kuder's statement appears to place the responsibility on the Bureau, while the Bureau, as we understand it, bases its position upon PG&E's position. Meantime, the Bureau is selling only 925,000 kw while its preference customers are having their allocations withdrawn.

Mr. Kuder implies that, if the Bureau had given PG&E "information . . . as provided by Article 14(a)(2)" including a larger portion of the preference customer loads so as to make up a total of 985,000 kw, the larger amount of preference power would not be said to preference customers. As we understand it, however, the Bureau considered that PG&E would not support 985,000 kw.

PG&E IS PURCHASING ALL RESIDUAL CENTRALIA CAPACITY IN ACCORDANCE WITH THE CONTRACT AND SHOULD PAY ITS FULL COST TO THE GOVERNMENT

The contract is clear that project capacity and energy (generated in CVP hydro plants) are first supplied to preference customers; and if this is insufficient the balance required by preference customers is then supplied from the non-project capacity and energy (Centralia import). The residue of either project and/or non-project capacity and energy is available for sale, and is being sold to PG&E, under two clearly delineated separate rate provisions⁴ in the USBR-PG&E interconnection agreement. The agreement has always been administered on this basis, PG&E has always been billed on this basis, but strangely to PG&E, and subsequent to the November 1, 1973 rate increase announcement, PG&E and Bureau are attempting to create a fiction that PG&E and the preference customers share pro-rata in both project and non-project power. This fiction is utilized in Mr. Kuder's statement in an effort to shift a major part of the Centralia loss to the preference customers.

⁴ Article 22(a)(3). "In determining the amounts of capacity and energy for which Contractor shall pay the United States in any month under subparagraphs (b)(1) and (b)(2) below, it shall be deemed that capacity required for maximum Demand of Firm Load and energy required for Firm Load were first furnished from Project generation."

Article 22(b)(1) sets forth a rate schedule for capacity and energy "sold" to PG&E "from Project generation . . ."

Article 22(b)(2) sets forth separately a rate schedule for capacity and energy "sold" to PG&E "from sources other than Project generation."

The rates are the same, to start with, but there are different procedures specified for changing the two rates.

This demonstrates the evil inherent in the refusal of the Bureau to provide full and open hearings, so that this aspect could be fixed and determined on the record. It would prevent what is happening here: the basic data and assumptions upon which all parties relied, including the Bureau, for considering the rate increase, had PG&E purchasing the bulk of the Centralia capacity. After the so-called proceeding was terminated with the announcement of a rate increase, the Bureau and PG&E secretly met and may have agreed upon a change in methods of billing (contrary to the Agreement) in a desperate effort to stem the proper criticism of its action.

In this regard, the record is silent as to whether or when this change was actually made. The rate increase was announced November 1, 1973. By memo of November 20, 1973, the Bureau's Assistant Regional Solicitor, Ms. Rita Singer, forwarded a "November 12, 1973, Power System AR&R Study substantiating new rate increase." (It is odd that a November 1st rate increase announcement is based upon a November 12th study.) This data shows that CVP would continue to sell most of the Centralia capacity to PG&E.⁵ This is the same allocation of Centralia capacity as the Bureau had used in the past, which the Bureau had furnished to GAO, and upon which GAO, accepting Interior's credibility, had relied in preparing its report finding a capacity loss of \$31,434,000 and an energy loss of \$8,597,000 on the sale to PG&E for the period through April 1, 1976.

In December 1973, the Bureau submitted a statement to the Reuss Subcommittee claiming the loss was only \$17,000,000 without explaining why its figures differ from the GAO's. Accordingly, NCPA requested the Bureau's back-up papers; and by January 15, 1974, the Bureau disclosed the reallocation of Centralia capacity—as a revision "proposed" by PG&E, "discussed" with PG&E, which "appears to have advantages over present procedures". This was explaining to the Reuss Subcommittee in the second Statement of Georgia Spiegel to Reuss Subcommittee (pages 1-6), submitted at the hearing on January 22, 1974.

The Reuss Subcommittee thereupon questioned Mr. E. F. Sullivan, Assistant Commissioner of the Bureau of Reclamation, concerning this matter. He agreed that the Bureau had been billing PG&E for all of the Centralia capacity because it was assumed that all of it goes to PG&E (Tr. 221).⁶ Mr. Sullivan stated that other methods of allocating this capacity "are under consideration" (Tr. 221). He stated "... PG&E has made a suggestion along this line. We have that that other methods of allocating this capacity 'are under consideration' (Tr. 222). He stated that "we have not made a decision" on whether to change the billing system (Tr. 222). He committed the Bureau to "advise this Committee before changing the billing system with PG&E." (Tr. 222)

Mr. Spiegel's testimony on behalf of NCPA, the next day (January 23, 1974) explained that the data submitted to the Reuss Subcommittee by Interior had been presented as representing actual billed dollars to PG&E, as if the billing of Centralia capacity to PG&E had already been changed as of June 30, 1973 (Tr. 344). The question was put to Mr. William F. Graham, Chief of the Bureau's Division of Power, who stated that this had been done "unknowingly" and that "we only found out these numbers were wrong last week." (Tr. 346). (He never explained why the Bureau had not corrected these numbers at the time of the hearing, but waited until NCPA had ferreted out this important misstatement of data.) He stated that no bills had yet been issued under this method (Tr. 346).

It was then pointed out that, as a matter of fact, the General Counsel of Sacramento Municipal Utility District had called this misstatement of billing data to the attention of the Secretary and officials of the Bureau in a letter dated January 7, 1974 (Tr. 347-348), which would place Bureau knowledge considerably prior to "last week" (Tr. 347).

⁵ See the following table:

	CVP customers (MW-year)	P.G. & E. (MW-year)
1973.....	13	369
1974.....	26	356
1975.....	51	331
1976.....	117	265

⁶ Preliminary Transcript of Reuss Subcommittee hearings are used in this statement because printed transcript is not yet available.

Mr. Spiegel of NCPA then explained that the same misstatement of billing data occurred in Mr. Kuder's testimony (Tr. 349) which would indicate that the misstatement was either a coincidence or resulted from collaboration.

Mr. Kuder's testimony of May 20, 1974, to this Subcommittee on Water and Power Resources, continues to assume or imply that there is a change in billing for Centralia capacity, under which the Bureau has reduced the amount billed to PG&E. His testimony is vague as to whether an agreement on this has been reached, and whether the method of billing has in fact been changed. (Evidently, PG&E-Bureau arrangements are to continue to be cloaked in secrecy). He states "In fact, less than half of the Centralia capacity will be sold to PG&E" (page 13). What does "in fact" mean? Has there been an agreement without the Bureau advising the Reuss Subcommittee, as promised? His testimony on page 26 merely states that the "concept . . . was first discussed with the Bureau . . . on November 21, 1973." At page 16, he testifies that, as a result of this reallocation of capacity, under which PG&E is considered to buy less Centralia capacity and more Project capacity, "PG&E will pay the increased rate for this capacity and associated energy beginning on April 1, 1974. . . ." This sounds like an accomplished fact.

Mr. Kuder states (page 16) that as a result PG&E will pay \$500,000 more than estimated by GAO (based on Bureau estimates). This means that PG&E's rates have been increased \$500,000 rather than the \$6,679,000 which would be required to fully offset the loss as explained by NCPA's witness Herbert C. Westfall in his Statement to this Subcommittee (pages 8-11). Mr. Westfall points out that the proper correction for Centralia costs would alone eliminate the need for an increase.

In any event, the November 1, 1973 announcement of the approximately \$6,000,000 increase to preference customers was not predicated on a \$500,000 increase to PG&E, as shown on data furnished by the Bureau on November 12, 1973. However, it is obvious that the increase of \$500,000 to PG&E should be offset by reducing by \$500,000 the amount of any increase to the preference customers. CVP has two classes: the preference customers and PG&E. It assessed a total increase of \$6,679,000 to the preference customers based upon the assumption of no increase to PG&E; thus it proposed in effect a total of \$6,679,000 for both customer classes. Now that it discovers that PG&E will be increased by \$500,000, the Bureau must reduce the preference customers announced increase to \$6,179,000, to avoid collecting more than it considered necessary on November 1, 1973.

This, once again, illustrates the evil of rate-making behind closed doors, instead of in open, fair hearings.

INCREASED WATER INCREASES PROJECT CAPACITY

We are satisfied that future redetermination of Project Dependable Capacity under the broad criteria of Article 11 can consider the effect of the fact that hydrology data now available shows a higher water flow (and consequently higher energy generation) than that which was used in the original CVP studies. PG&E, having failed to retain in its files the back-up data upon which Project Dependable Capacity has been previously determined, is hardly in a position to assert that increased average water would not increase capacity available for sale.

PG&E HAS A SUBSTANTIAL NET BENEFIT FROM 500 MW OF CAPACITY PROVIDED FREE

See the discussion at pages 9-11, above.

Under a proper interconnection agreement the Bureau could obtain integrated operation and reserve back-up without giving up 500 MW of capacity to PG&E without charge. Bonneville Power Authority does not have to give away this type of capacity without charge.

PG&E UNDERSTATES BENEFITS AND OVERSTATES DETRIMENTS OF ENERGY ACCOUNT NO. 1

Contrary to Mr. Kuder's assertions, PG&E had substantially greater benefits than it discloses from Energy Account No. 1. For one thing, the low cost hydro power sold to it at an average of 2.44 mills per kwh displaced energy at incremental costs considerably higher than its average of 2.77 mills. Moreover, combined with PG&E control over the dispatch of CVP's total generation it did provide capacity which enabled it to postpone capacity and minimize capacity costs through capacity transactions with interconnected systems.

The fact that PG&E's rates are regulated does not obviate the soundness of the usual economic analysis under which benefits in earlier years are recognized by compounding interest savings throughout the payback period.

As shown in the appendix attached to this rebuttal statement, PG&E also recognizes, in an internal memorandum, the benefits to it of the interconnection arrangements of Contract No. 2948A. This 1973 PG&E memorandum lists the benefits accruing to PG&E as a result of this contract. The more important advantages cited by PG&E may be summarized as follows:

1. In 1972 PG&E purchased 400 MW of capacity and 1.2 billion kwh of energy with a resultant savings of \$7,000,000 in capacity and \$930,000 in energy. If invested at 7% interest, this would result in an annual benefit of \$490,000 for capacity and \$65,000 for energy.

2. PG&E receives, at no cost to it, use of Contract Dependable Capacity during those months when preference customers loads are less than the maximum annual customer load. In 1972 this amounted to 713,000 kw-months and resulted in a benefit to PG&E of approximately \$1,000,000.

3. PG&E similarly benefits in those years when hydro conditions are above the historical minimum adverse dry period. Thus, PG&E has available to it the excess hydro capacity at no cost to displace thermal generation. Also, because the CVP and PG&E generation are integrated and because PG&E can have Project water releases deferred, it can use its more efficient thermal plants off peak and use hydro power to displace less efficient thermal units during peak periods, thus requiring less fuel to produce the same total energy.

4. In 1971, the preference customer load reached a maximum dependable capacity of 925 MW so that PG&E no longer is being billed for project-generated capacity. This permitted PG&E to purchase all project-generated energy in the lowest (2 mill) energy block prior to the rate increases in question (which eliminate a block rate structure). PG&E estimated that savings from this were \$762,000 for the period 1971 to mid-1973, or about \$305,000 per year.

5. To the extent PG&E has excess transmission capacity, the Bureau pays PG&E for the use of this capacity to transmit power to Bureau customers and thus PG&E receives additional revenues it would not normally receive. Furthermore, the presence of Federal transmission lines can provide added reliability during emergencies.

6. CVP generation, personnel, materials and supplies are available for use in emergencies to provide additional back-up and support to PG&E in maintaining or restoring service.

The advantages outlined above, plus others enumerated in the appended memorandum, demonstrate the invalidity of the implication in Mr. Kuder's statement that the USBR-PG&E contract (No. 2948A) is unduly burdensome to PG&E.

THE CENTRALIA REALLOCATION MYSTERY

See discussion at pages 12-19 above.

THE UNITED STATES IS UNLAWFULLY RESTRICTED BY THE AGREEMENT WITH PG&E

PG&E states that the USBR-PG&E interconnection agreement restricts the Government from utilizing in its CVP project, power from sources other than its own plants and northwest surplus—except by agreement with PG&E. These restrictions were obviously imposed on the Government by PG&E in the initial negotiation and they appear to be inconsistent with the antitrust laws. The monetary benefits which the Government can obtain from its substantial CVP investment by expanding its sources, as Bonneville Power Administration does, should not be under the control of private interests.

PG&E RECEIVES SUBSTANTIAL FREE AND UNDERPRICED CAPACITY FROM CVP

The CVP project has 1,471,200 kw of installed hydro generating capacity but only supports 925,000 kw for firm sales to preference customers. The difference of approximately 500,000 kw⁷ is made available free to PG&E, and this is valuable capacity, as discussed at page 9. above. In addition, there is 400 MW of Centralia capacity, purchased by CVP, most of which is resold to PG&E at a loss of over \$6,000,000 per year, as discussed above at pages 12-19.

⁷ There is only a minor amount of project pumping load which cannot be interrupted at time of PG&E's maximum load requirements.

PG&E SEEKS IRRELEVANTLY TO INJECT ITS VERSION OF THE PRIVATE VERSUS PUBLIC POWER ISSUE

The question involved here is whether the Secretary of the Interior has lawfully exercised his authority in increasing CVP rates to preference customers. These customers have rights under the laws of the United States, and, in this case, do not believe that they can lawfully be required to pay an approximately \$6,000,000 per year increase in order to make up an approximately \$6,000,000 per year loss on CVP's sales of Centralia capacity and energy to PG&E. The relative benefits and burdens created by statute on private companies and public agencies have no relevance to that issue.

If the relative benefits or subsidies are so heavily weighted in the favor of public agencies—as the private industry report claims—why is it that PG&E has been able successfully to compete with public agencies in California and develop an almost complete monopoly over most of the aspects of the electric and gas industry in Northern California, a region as large as all of New England and with a comparable population? The fact is that, on balance, the laws strongly favor and benefit the private electric industry—but these vast benefits are not discussed in the Report to the private-company Edison Electric Institute. PG&E has grown into one of the largest utilities in the country; it should not knock the system of laws that has enabled it so to prosper.

This effort to divert from the subject matter at hand, suggests that it considers its position weak on the merits of the particular controversy here involved.

1. PG&E BENEFITS FROM POWER THAT BUREAU IMPORTS FROM NORTHWEST

The Bureau presently imports 400 Mw of power at approximately 80% capacity factor. To the extent that this 400 Mw is not being used to serve Bureau customers, PG&E buys the power at a lower cost than from alternative sources. This power is credited to so-called "bank accounts" for later repurchase by the Bureau. The saving is passed on to PG&E customers but must be returned to the Bureau at the time of unbanking.

(The following to be deleted)

In 1972, the first year that the full 400 Mw was available, PG&E purchased all of the 400 Mw of capacity and 1.2 billion kwh of import energy. The savings passed on to PG&E customers for that year was about \$7 million on capacity and \$930,000 on energy. Assuming that PG&E customers could invest this savings at approximately 7 percent, the benefit to them would be about \$490,000 for capacity and \$65,000 for energy each year that the power remains in the account. An added benefit to PG&E from the import power is that it reduces PG&E's fuel oil requirements at a time of critical supply.

2. PG&E RECEIVES SUCH CAPACITY AS MAY BE AVAILABLE IN EXCESS OF PROJECT LOAD AND PROJECT DEPENDABLE CAPACITY

The power plants of the Bureau's Central Valley Project are hydroelectric plants and as such are rated according to the amount of water that can reliably be projected to be available for power production under dry year conditions. In the Bureau-PG&E contract, Project Dependable Capacity (PDC) is defined as that capacity available with energy support under the most adverse stream flow conditions of record, which remains after deducting on-peak project loads. The rating of hydroelectric plants which results is necessary to account for the decreased capacity which occurs in very dry periods. Whatever benefit may accrue to PG&E from plant capability in excess of PDC, results from: (1) the ability to utilize such capability during system emergencies or other contingencies and (2) short term displacement of thermal generation as discussed in Item 7.

3. PG&E CAN BENEFIT FROM STORAGE OF WATER BY THE BUREAU FOR PG&E'S ACCOUNT

The Contract provides the PG&E may request and the Bureau will defer water releases made for power production when total water releases exceed the minimum requirements for purposes other than power. In such event, PG&E would substitute PG&E power from other sources for that power which the Bureau would have produced. The Bureau then holds water in storage to be released at PG&E's request. This provision allows PG&E operating flexibility.

4. BENEFITS OF RATCHET PROVISIONS

(a) Interim Use of Contract Dependable Capacity Without Charge i.e. In Months When Customers' Loads Are Less Than Their Annual Peak

The Bureau generation available during months when Bureau preference customers' loads are less than the maximum customer load is useful to PG&E to the extent that it is used for scheduled overhaul and maintenance of PG&E plants which avoids the need for PG&E to install or purchase additional generation for such purposes.

In 1972 the generation available under this provision amounted to approximately 713,000 kw-months. This capacity would not be fully usable because of uncertainties in scheduling and in forecasting. Assuming, however, that it was fully usable by PG&E and, further, that the alternative would be gas turbine capacity, then the dollar benefit in 1972 would have been about \$1 million.

This benefit decreases as Project Dependable Capacity becomes insufficient to meet the customer load and the needed capacity is drawn from the Capacity Account.

(b) PG&E Is Paid For Kilowatts Withdrawn From Capacity Account Based On The Maximum Withdrawal In The Year Ending With The Current Month

Resources installed by PG&E to meet peak month loads of Bureau customers are available to the Company in off-peak months to the extent not needed for such loads. This provision will benefit PG&E when purchases from the Capacity Account begin. Thereafter, the benefit of this provision to PG&E will roughly offset the decrease in benefit stated in 4a above.

5. WHEN ALL PROJECT DEPENDABLE CAPACITY IS BEING SOLD TO PREFERENCE CUSTOMERS, PROJECT GENERATION (ENERGY FROM PROJECT'S HYDROELECTRIC PLANTS) PURCHASED BY PG&E GOES INTO THE ENERGY ACCOUNT NO. 2 AT THE LOWEST BLOCK ENERGY RATE

Under this condition, which first occurred in 1971, energy from the Central Valley Project's hydroelectric plants is purchased at the lowest of the 4, 3, and 2 mills/kwh block rates. This energy at 2 mills/kwh is less expensive than PG&E's alternate cost. The saving is passed on to PG&E customers but must be returned to the Bureau when the energy is withdrawn from Energy Account No. 2.

(The following to be deleted)

During the period 1971- mid 1973 PG&E purchased 600 million kwh from Bureau plants at an effective rate, with voltage discounts, of 1.99 mills/kwh. PG&E's weighted incremental cost was 3.26 mills/kwh. The saving to PG&E customers was:

$$600 \times 10^6 \text{ kwh} \times (3.26 - 1.99) \times 10^{-2} = \$762,000 \text{ or about } \$305,000 \text{ per year}$$

Assuming that PG&E customers were able to invest this saving at approximately 7%, the benefit from one year's energy purchase would be about \$21,000 each year until the energy is withdrawn from the Energy Account.

6. COMPANY RECEIVES REVENUE FOR EXCESS TRANSMISSION CAPACITY

To the extent that PG&E has excess transmission capacity, it is paid for the use of this capacity to transmit power to Bureau customers, and, thus, receives revenue that it would not receive had the Bureau constructed duplicate transmission facilities.

7. INTEGRATION OF FEDERAL GENERATION PERMITS MORE EFFICIENT USE OF PG&E THERMAL PLANTS

By integrating federal generation with PG&E generation, it is possible to obtain a more economic dispatch of the combined resources. This is because off-peak area loads can be met in part with PG&E's more efficient thermal units and the federal hydro energy can be used to meet on-peak loads. Thus, hydro energy can be used on-peak to displace energy that would otherwise be generated by PG&E's less efficient thermal units. This procedure benefits PG&E customers by requiring less fuel to produce the same total energy.

8. PG&E BENEFITS FROM USE OF FEDERAL FINANCING FOR A PORTION OF THE PACIFIC NORTHWEST INTERTIE

(These benefits result from the Bureau-California Companies Contract 2947A for EHV transmission and exchange service which is separate from but related to Contract 2948A). One of the two 500 kv circuits of the Pacific Intertie between Malin (Oregon) and Round Mountain (California) was constructed by the Bureau rather than by the investor owned utilities. The investor owned utilities obtain use of the Bureau circuit by paying the federal cost of ownership with relatively low interest rates and no taxes. The annual revenue requirements of the investor owned utilities using the circuit are therefore less than the alternative of private ownership. For cost purposes PG&E has use of 50% of the Bureau circuit. The approximate annual benefit to PG&E is reflected by the difference in revenue requirements as follows:

PG&E Revenue Requirements:

Private Ownership ¹ (16,806,781 x 13.0% x 50% (PG&E 13.0% includes taxes) -----	\$1, 092, 441
Federal Ownership ¹ (16,806,781 x 3.89% x 50%) -----	326, 892
Difference (benefit) -----	765, 549

¹ Federal and Private Costs are based on 1967 financing.

9. PG&E HAS USE OF ROUND MOUNTAIN-COTTONWOOD 230 KV TIE TO STRENGTHEN ITS SYSTEM

The Round Mountain-Cottonwood 230 kv transmission line was built by the USBR in order to provide a direct tie between the USBR facilities in California and the BPA facilities in Oregon (by way of the USBR 500 kv transmission line between Round Mountain and Main). Although this 230 kv line was not built with the intention of reinforcing the PG&E 230 kv transmission lines between Round Mountain and Cottonwood, and is not required for that purpose, nevertheless, there is a benefit to having the additional line between these two substations. For example, it has been established that the underlying 230 kv system, which is in parallel with the 500 kv Intertie, provides support during disturbances on the 500 kv system, and, therefore, contributes to system reliability. Therefore, the additional 230 kv line from Round Mountain to Cottonwood can contribute to overall system reliability. This would also apply, of course, in the event of a fault on one or more of the 230 kv lines from Round Mountain to Cottonwood.

10. CONTRACT PROVIDES MEANS TO USE FEDERAL GENERATION TO MEET AREA EMERGENCY CONDITIONS

PG&E can call upon federal generating capacity during an emergency and to the extent that it is not being used to meet load.

11. CONTRACT 2948A PROVIDES A BASIS FOR INTEGRATING FUTURE CVP HYDROELECTRIC FACILITIES

The contract provides the basis for integrating future CVP generating plant additions such as New Melones and Auburn. This provision could benefit PG&E customers by permitting the Company to defer the construction of alternative generation.

12. USE OF FEDERAL PERSONNEL AND MATERIAL TO ASSIST IN EMERGENCY RESTORATION OF SERVICE

PG&E can call on the Bureau for assistance in supplying materials or personnel to repair damaged equipment under emergency or extraordinary conditions.

13. FEDERAL TRANSMISSION SYSTEM ADDS TO THE AREA TRANSMISSION SYSTEM

The Bureau 230 kv transmission facilities with ties to the PG&E system at Cottonwood, Tracy, and Folsom (115 kv) add to the transmission available to the PG&E area. At times this is a benefit to PG&E and at other times it is not. Under conditions where the USBR 230 kv lines parallel those of PG&E and the

PG&E lines are opened due to disturbances, the presence of the additional lines improve reliability. On the other hand, there are conditions where the Bureau's lines are not beneficial. For example, during the 1972 winter peak load, the USBR system transmitted some 490 MW to the PG&E system across the tie at Cottonwood. This power flow had the detrimental effect of (1) increasing the load on the PG&E Cottonwood-Vaca 230 kv lines and (2) diminishing system stability for a 500 kv fault at Table Mountain. Similarly, part of the USBR power will flow, by displacement, on the 500 kv system, and this increased load reduces the stability margins of the system.

PACIFIC GAS AND ELECTRIC COMPANY,
San Francisco, Calif., June 26, 1974.

Hon. HAROLD T. JOHNSON,
Chairman, Subcommittee on Water and Power Resources, Committee on Interior
and Insular Affairs, Washington, D.C.

DEAR MR. JOHNSON: Enclosed is Pacific Gas and Electric Company's answer to the rebuttal of the Northern California Power Agency which was submitted by Mr. George Spiegel in his letter of June 6, 1974. We request that this be made part of the record in the hearing on H.R. 14221.

We appreciate this opportunity to submit the enclosed answer.

Sincerely yours,

WILLIAM B. KUDER.

ANSWER OF PACIFIC GAS AND ELECTRIC COMPANY TO REBUTTAL OF
NORTHERN CALIFORNIA POWER AGENCY

The NCPA rebuttal to Mr. Kuder's May 20 statement before your committee substitutes speculation and argument for fact. We have therefore not prepared a detailed answer, and shall correct only a few of the more egregious errors in that rebuttal.

NCPA (p. 4) alleges that capacity in the capacity account will never be repurchased. Possible termination of the 400 mw of Northwest capacity in 1982 and the authorization of project additions such as the East Side Division could require the Bureau to repurchase large amounts of this banked capacity. (Kuder p. 17)

The rebuttal (NCPA P. 9-11) implies the existence of secrets and mysteries surrounding load curves and Project Dependable Capacity.

With respect to the "lost load curves", the 1951 contract contained capacity factor requirements for Bureau plants which placed Bureau Project Dependable Capacity in a more favorable position on the area load curves than many of PGandE's own plants to give maximum value to CVP capacity. In 1955, the capacity factor requirements for then existing plants were improved for the Bureau. In 1963, the Bureau and PGandE negotiated capacity factors for the Trinity Division plants which gave the Bureau credit for dependable capacity in excess of that which could be absorbed into the area load at that time. The 1963 capacity factors for then existing plants and for the project as a whole were carried forward in the 1967 contract, thus continuing the favorable position which the Bureau plants occupy on the load curve. Once the capacity factors for existing plants were agreed to, there was no need to maintain the data used over the years to establish these capacity factors.

With respect to Project Dependable Capacity, it is defined in the contract as "The lowest electric capacity . . . which could be available with energy support from Project Plants in any month during the most adverse period of stream flow conditions of record . . . after deducting the estimated capacity required from Project Plants for Project Load during Contractor's Peak Load Period." (Article 9(i))

That part of the Bureau's total generating capacity which meets the definition of Project Dependable Capacity is a reliable substitute for thermal capacity that would otherwise be built. Thus, Project Dependable Capacity from CVP plants meets the basic criteria established throughout the electric utility industry as firm power; Bureau capacity beyond Project Dependable Capacity does not. The main value of the Bureau's non-dependable capacity is the energy it produces. It has a limited additional value as a substitute at times for thermal capacity taken out of service for routine or emergency overhaul. (Kuder P. 30-31)

Pages 13 and 14 of the NCPA Rebuttal contain the following statement:

"... Strangely and secretly, since NCPA has demonstrated the Government's loss on the sale to PG&E, and subsequent to the November 1, 1973 rate increase announcement, PG&E and Bureau are attempting to create a fiction that PG&E and the preference customers share prorata in both project and non-project power. This fiction is utilized in Mr. Kuder's statement in an effort to shift a major part of the Centralia loss to the preference customers."

It is neither strange nor secretive for the parties to a contract to meet and discuss application of the contract when they realize that part of the contract is being misinterpreted in its application. It is not fiction that, when preference customers are consuming more than half of the energy that the Bureau is importing from Centralia, these same preference customers are also making use of a large part of the Centralia capacity which produces that energy. (Kuder P. 13-15)

At pages 20 and 21 of the rebuttal, NCPA states:

"Contrary to Mr. Kuder's assertions, PG&E had substantially greater benefits than it discloses from Energy Account No. 1. For one thing, the low cost hydro power sold to it at an average of 2.44 mills per kwh displaced energy at incremental costs considerably higher than its average of 2.77 mills."

NCPA apparently is not aware that during the Energy Account No. 1 banking period, 1951-67, most of the fuel used in PGandE thermal plants was natural gas. Incremental use of natural gas in power plants during this period permitted fuller utilization of pipeline facilities and thus a declining incremental cost for PGandE gas fuel. For this reason, the 2.77 mill average cost is a good engineering estimate for the cost of PGand E's alternative to buying CVP energy from the Bureau.

At pages 19 and 20, NCPA incorrectly speculates that hydrology data showing higher water flow should increase Project Dependable Capacity in future redetermination studies. The additional hydrology data that the Bureau has agreed to use in its repayment studies only increase the long-term average water supply and consequent energy generation. The additional data do not change the critical 1930-34 historical water supply data on the most adverse period of steam flow conditions which are used in determining dependable capacity. (Kuder P. 18)

The rebuttal statement repeatedly refers to the benefits that PGandE allegedly receives from its purchases of power from the Bureau. This power is sold to PGandE customers at cost. (Kuder P. 23-25) There is no profit to the Company from this transaction.

At pages 21 and 23, NCPA summarizes excerpts from a draft copy of a PGandE internal memorandum regarding benefits to PGandE and its customers. Items 1 and 4 of this list clearly are not benefits to PGandE but to its customers. (Kuder P. 23-25) With respect to the benefits described in items 2, 3, 5 and 6, it is not surprising that PGandE should receive such benefits in return for enabling the CVP to serve twice the customer load it could serve without PGandE support. (Kuder P. 19) Moreover, under the rate making process, all such benefits to a utility which reflect themselves in reduced operating costs are passed on to the utility's customers and not to its owners.

[Whereupon, at 12:15 p.m., the subcommittee was adjourned subject to the call of the Chair.]