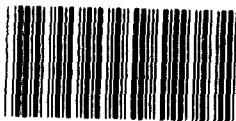


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UNITED STATES GENERAL ACCOUNTING OFFICE



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STATEMENT OF J. DEXTER PEACH, DIRECTOR
RESOURCES, COMMUNITY, AND ECONOMIC DEVELOPMENT
DIVISION

BEFORE THE
COMMITTEE ON ENERGY AND NATURAL RESOURCES
UNITED STATES SENATE

Mr. Chairman:

You have asked us to testify today on a GAO draft report concerning the status of the Bonneville Power Administration's (Bonneville) repayment to the Treasury of the Federal investment in the Columbia River Power System. A draft report on the results of our work was provided to the Department of Energy (DOE) for comment and to congressional committee chairmen who requested a copy. We have received DOE's comments and are currently incorporating them as well as making other appropriate adjustments to the draft report. My statement today will highlight the current status of Bonneville's repayment of the Federal investment.

The Federal investment in the Columbia River Power System exceeds \$7 billion. Federal law requires Bonneville to repay this investment over a period of years. The Bonneville Project Act of 1937 (16 U.S.C. 832f) requires that power rates be drawn to include the "amortization of the capital investment over a reasonable period of years." Subsequent legislation, including the 1974 Federal Columbia River Transmission System Act (16 U.S.C. 838g) and the 1980 Pacific Northwest Electric Power

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Planning and Conservation Act (16 U.S.C. 839e), requires Bonneville to repay the Federal investment and set electric power rates at the lowest possible level consistent with sound business practices.

During the past 10 years, Bonneville has repaid little of the Federal investment in the Columbia River Power System. Bonneville began repaying the Federal investment in 1939 using a cost-based approach to determining revenue needs which incorporated a fixed repayment schedule. Using the fixed repayment schedule, Bonneville repaid about \$364 million through 1965. Because of pressure to raise power rates to meet fixed annual payments, Bonneville adopted in 1965 a repayment study method for determining revenue requirements. Under the repayment study method, repayment of the Federal investment was not scheduled--the only requirement is that each project be repaid within its repayment period (ranging from 35 to 66 years). Using the repayment study method, Bonneville has experienced a net operating loss in 8 of the past 10 years. In fact, Bonneville has not shown a net operating income since 1976 and is projecting a shortfall again for 1983. Bonneville has paid a little over \$43 million on the Federal investment during the past 10 years.

A previous study by GAO and studies by others have recognized the repayment problem at Bonneville. Our June 1981 report¹ recommended a cost-based (mortgage-type) approach to repayment as an alternative. Under that approach, repayments would once again be scheduled on an annual basis and form the basis for determining revenue requirements.

¹"Policies Governing the Bonneville Power Administration's Repayment of Federal Investments Need Revision," (EMD-81-94), June 16, 1981.

Other studies and analyses have suggested the need for changes to assure timely and equitable repayment of the Federal investment. In 1981, DOE's Office of Power Marketing Coordination encouraged Bonneville to explore a cost accounting amortization method as an alternative to the current method. A Price Waterhouse study in 1981 recommended that Bonneville should collect revenues to systematically reduce the Federal investment on an annual basis. Recently, the Federal Energy Regulatory Commission (FERC) which reviews and approves Bonneville's rates, stated that "Bonneville's repayment of the Federal investment is substantially lagging." FERC also pointed out that when Bonneville is unable to collect sufficient revenues in a given year, it does not make those up in the following years, but spreads them over the remaining term left in the repayment period. FERC stated that this practice would result in Bonneville having to overprice power in the future to make up deficiencies and could make such power economically unmarketable.

The repayment issue has also concerned Bonneville's Administrator. In March 1982, he stated actions had been taken to catch up on the repayment by 1985. While Bonneville has raised its power rates since then, it is projecting a net operating loss of about \$121.5 million for fiscal year 1983.

Aside from discussing Bonneville's current repayment status, the report also addresses one repayment policy change Bonneville made in 1972 to repay its highest interest bearing debt first rather than repaying a portion on each increment of debt as it was incurred. This policy change was made to minimize Bonneville's

costs and help offset projected revenue deficits. Under this policy, interest paid by Bonneville on the Federal investment is applied to the highest interest projects first, thus, allowing the low interest investment projects (some at 3 percent) to remain outstanding. Bonneville's practice of repaying highest cost debt first has the effect of reducing its interest expenses, which keeps power rates in the Northwest lower. It also reduces the money Bonneville must return to the Treasury. However, Treasury borrowings are increased, usually at interest rates higher than those paid by Bonneville.

This highest interest first policy has also caught the attention of others. The Chief of the U.S. Army Corps of Engineers stated in 1979 that "* * * this policy is improper. We feel that this procedure results in a subsidization of power users by the general taxpayer * * *." In a 1980 Presidential Audit Report Price Waterhouse stated

"* * * the U.S. Treasury is not relieved of the higher financing costs of newer money as it must redeem the older and lower interest bearing bonds and notes first as they become due. The difference between the higher U.S. Treasury financing costs and the lower financing costs repaid by power users is made up by general tax revenues."

Bonneville's highest interest first policy has been justified under sound business principles since prudent management dictates minimizing expenses. While at this time Bonneville's practice does minimize its project repayment, it results in higher cost to the Federal Treasury.

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Mr. Chairman, my statement to this point has focused on Bonneville's repayment status as well as our past and current work relating to this matter. I should point out that Bonneville objected to our recommendation in 1981 that it adopt a mortgage-type repayment approach and continues to object to such a change. Bonneville's basic arguments against change appear to be that revenue shortfalls could still occur and a fixed type repayment system would reduce its flexibility to deal with changing conditions.

While we are still evaluating DOE's comments, we believe that a mortgage-type repayment approach could allow for annual adjustments as a result of revenue shortfalls in a preceding year or years. Given Bonneville's repayment performance over the last 10 years, we continue to believe that a more systematic approach is needed to assure timely and equitable repayment of the Federal investment.