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STATEMENT OF
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BEFORE THE
SUBCOMMITTEE ON WATER AND POWER RESOURCES
COMMITTEE ON INTERIOR AND INSULAR AFFAIRS
U.S. HOUSE OF REPRESENTATIVES
ON THE
BUREAU OF RECLAMATION'S
BONNEVILLE UNIT OF THE CENTRAL UTAH PROJECT
FUTURE REPAYMENT ARRANGEMENTS

Mr. Chairman:

We are pleased to be here today to discuss our concerns regarding future repayment arrangements for the Bureau of Reclamation's Bonneville Unit, Central Utah Project. Our concerns were documented in a September 9, 1985, report to Senator Howard Metzenbaum, entitled Bureau of Reclamation's Central Utah and Central Valley Projects Repayment Arrangements (GAO/RCED-85-158). In brief, we concluded that

(1) The Bureau of Reclamation's use of the Water Supply Act of 1958 to defer repayment of costs associated with the majority (60,000 acre-feet out of the 99,000 acre-feet estimated yield) of municipal and industrial (M&I) water supplies of the Bonneville Unit was illegal. We

estimate that such a deferment could result in the federal government losing up to $97 million in interest revenues.

(2) The Bureau did not seek the Congress's approval of a 1984 modified cost allocation of the Bonneville Unit, although the Department of Energy Organization Act of 1977 requires this approval.

During our review for Senator Metzenbaum, we asked the Department of the Interior's Assistant Secretary for Water and Science, on April 22, 1985, to respond to several issues regarding the Bonneville Unit. In September, when we reported to the Senator, we had not yet received a response to our letter.

By letter dated November 22, 1985, the Assistant Secretary disagreed with our conclusions. After evaluating his response, we remained convinced of our conclusions and documented our views in a follow-up report to Senator Metzenbaum, entitled Bureau of Reclamation's Bonneville Unit: Future Repayment Arrangements (GAO/RCED-86-103, March 7, 1986).

BACKGROUND

A little background on the events leading up to the current repayment arrangements for the Bureau's Bonneville Unit may be helpful. The Bonneville Unit is the largest of six components of the Central Utah Project. The principal purposes of the unit are to supply water for irrigation and M&I users and to generate electric power. Construction of the unit began in 1966 and is currently almost one-third completed; completion is expected in 1996. The unit's estimated total costs as of January 1985 was $2.1 billion, $1.9 billion of which is to be repaid to the federal government.

Bureau of Reclamation policy requires a firm repayment contract with the users of M&I water before M&I project facilities can be built. Once a repayment contract is in place construction spending may not exceed the contract obligation.

In 1965 the Central Utah Water Conservancy District signed a contract with the federal government to repay $102 million which was to cover all of the costs then allocated to M&I water supply at the Bonneville Unit (79,000 acre-feet and later increased to 99,000 acre-feet).

In the late 1970's, the Bureau recognized that the 1965 repayment contract would not recover all allocated M&I costs, which had increased because of a lengthened construction period and inflation. The Bureau--recognizing that construction would have to be stopped unless the repayment obligation could be increased--negotiated a supplemental contract with the district in 1980 that would have increased the district's repayment ceiling. However, the Department of the Interior rejected this contract because it was legally questionable, contained several provisions which were not fiscally prudent, and did not adequately disclose the cost of the project to those responsible for repayment. Therefore, the Bureau sought other means of continuing construction.

First, in 1981, the Bureau invoked the Water Supply Act of 1958 to defer to the future the district's repayment of costs associated with 60,000 acre-feet of the M&I water which was covered in the 1965 repayment contract. As a sign of good faith that it eventually intended to purchase all the M&I water, the district contributed $10 million in cash, increasing its repayment obligation and the construction ceiling to $112 million. Second, in 1982 at the district's request, the Bureau reassigned to M&I costs $38 million in ad valorem tax revenues from property owners within the district's boundaries. These prospective revenues--originally intended for irrigation

repayment--increased the M&I construction ceiling to $150 million. These actions enabled the Bureau to continue construction because the district's repayment obligation was sufficient to cover the costs of the remaining M&I water under contract.

Costs continued to rise on M&I construction, so the Bureau began negotiations with the district again in July 1984. Contract agreements were reached in November 1985 to increase the M&I repayment obligation by $404 million, making the total repayment obligation $554 million. Based on the Bureau's fiscal year 1986 budget data, this amount would be sufficient to recover the district's share of the M&I costs, including those deferred under the Water Supply Act.

ILLEGAL USE OF 1958 WATER SUPPLY ACT

In our September 1985 report, we concluded that the Bureau's use of the Water Supply Act of 1958 for the Bonneville Unit was illegal. The Assistant Secretary, in his November 1985 response, said that all of the requirements of the Water Supply Act had been met and that the 1965 repayment contract with the water district allowed for the use of the Water Supply Act. In accordance with the act, under the supplemental repayment contract, the Department intends to allow the district a 10-year, interest free deferment of repayment for facilities already completed and allocated to future use.

The Water Supply Act, as indicated by its legislative history, allows the Bureau to enlarge a planned project to store additional water that may be needed to meet future demand and to construct the enlargement without a repayment contract. However, it does not allow the Bureau to defer repayment obligations for facilities supplying water already under contract, as in this case.

The act provides for delayed repayment on the premise that the water supply will not be needed for some time after it becomes available. Because the number of good dam and reservoir sites is limited, and because building a larger facility ordinarily costs less than enlarging a completed facility, the law encourages construction for somewhat uncertain future needs. The Bureau has used the act for a different purpose. In the case of the Bonneville Unit, the M&I water supply was contracted for, under construction, and intended for current use not to meet future demand.

By applying the Water Supply Act to the supplemental contract, the Department intends to allow a 10-year, interest free deferment of repayment. Based on fiscal year 1986 cost estimates, we project that this deferment could cost the federal government up to $97 million in lost interest revenues.

Pursuant to the requirements of the 1986 Energy and Water Development Appropriation Act, on December 12, 1985, the Bureau submitted a copy of the supplemental repayment contract between the Bureau and the district to the Congress to initiate the start of the 100-calendar day waiting period prior to the Bureau obligating or expending funds made available by this act for the Bonneville Unit. This act states that the contract shall recover all costs allocated to M&I water supply plus interest.

Because the Department intends to allow the district a 10-year interest free deferment of repayment pursuant to the provisions of 1958 Water Supply Act, and because the use of such act in this case was illegal, the supplement repayment contract does not satisfy the recovery requirements of the 1986 Energy and Water Development Appropriation Act. Accordingly, in our opinion, none of the funds made available by this act should be used for the Bonneville Unit until such time as the supplemental repayment contract has been revised to eliminate the inappropriate deferment of construction costs and interest repayment. On this matter, it should be recognized that because

of the time needed to revise the contract, Interior and the district may face a situation where new construction contracts cannot be awarded and completion schedules are affected.

In our March 1986 report to Senator Metzenbaum, we recommended that the Secretary of the Interior direct the Commissioner, Bureau of Reclamation, to (1) work with the Central Utah Water Conservancy District to revise the supplemental repayment contract between the Bureau and the district to eliminate any inappropriate deferment of the repayment of construction costs and of interest and (2) not use the funds made available for the Bonneville Unit by the Energy and Water Development Appropriation Act, 1986, until the supplemental repayment contract has been appropriately revised.

Because Interior has taken the position that its use of the Water Supply Act's provisions in the supplemental repayment contract with the district was appropriate, we are concerned that Interior will not act on our recommendation and thus cause the federal government to lose up to $97 million in interest revenues. While our report is limited to the Bonneville Unit of the Central Utah Project, we are also concerned that a precedent may be set--by allowing Interior and the district to proceed under the proposed supplemental repayment contract with what we believe is illegal application of the Water Supply Act of 1958--that has potential implications for similar contracts on other projects.

MODIFIED COST ALLOCATION NEEDS CONGRESSIONAL APPROVAL

In 1984 the Bureau modified its procedure for allocating Bonneville Unit costs. According to the Bureau, this was done in an attempt to make a more equitable allocation of costs to project purposes. The allocation resulting from this change was used as the basis for negotiating the supplemental repayment contract. The Department of Energy Organization Act of 1977 requires congressional approval for the reallocation of the costs

of multipurpose facilities, such as the Bonneville Unit. Although the law does not specify what is required in the way of congressional approval, it is our view that at the least full disclosure of the reasons for and impact of changes in cost allocation should be made to the cognizant committees.

The Assistant Secretary responsed to us that because the change in cost allocation was not a final one formal congressional approval was not required. He said, however, that the Congress is informed annually of such changes through the budget process. He added that the modified procedure distributed costs equitably and reasonably.

We disagree with the Assistant Secretary's position that non-final changes are not subject to the congressional approval provisions of the Department of Energy Organization Act. Section 302(a)(3) of the act makes no reference to a final cost allocation but only to "changes in cost allocation or project evaluation standards" which would "authorize the reallocation of joint costs of multipurpose facilities. . . ." Furthermore, statements by the act's sponsors do not refer to "final" cost allocations. The sponsors wanted to make certain that changes in allocation of joint costs of multipurpose projects were approved by the Congress.

We believe that the allocation procedure the Bureau is currently applying has far-reaching effects on repayment. Attachments to the Assistant Secretary's response show that the modification made major changes in the allocations of joint costs. The reallocation will reduce the interest the Bureau collects on repayment and appears to be just the type of change that requires approval under section 302(a)(3).

While we did not analyze the mechanics or equity of the reallocation, we did look at the effect the modified procedure had on allocated costs and on the interest to be collected. We found that the modified procedure decreased the electric power allocation by $378 million and increased the irrigation

allocation by $381 million to a total of $915 million. Since the Bureau has set the irrigators' repayment ability at $16 million, the remaining $899 million will be repaid primarily by electric power revenues. However, before electric power revenues can be used to repay irrigation costs, they must first be used to repay the costs allocated to Colorado River electric power development. Consequently, since irrigation cost repayment is not subject to interest while repayment of electric power development is, the value of the eventual repayment will be substantially less than the value of the government's expenditures.

To determine whether the Congress has been informed of the reallocation through the annual budget process, as the Assistant Secretary suggested, we examined the Bureau's project data sheets and the records of appropriation hearings concerning the Bonneville Unit. Other than updated cost data reflecting the results of the reallocation, we found no evidence that the Congress or cognizant committees were informed of a new allocation procedure. On the contrary, the record shows that the Bureau attributed changes in cost allocations primarily to a change in the Bonneville Unit's physical facilities.

In our report to Senator Metzenbaum we recommended that the Secretary of the Interior direct the Commissioner of Reclamation to more fully inform the Congress, by explaining why the modified procedure was developed, how it was developed, and what effect it will have on allocated costs and repayment. Further, to comply with the requirements of the Department of Energy Organization Act of 1977, we recommended that the Secretary of the Interior seek congressional approval for this modification.

This concludes my prepared statement. We are providing for the record, copies of the correspondence and reports referred to in this statement. We will be pleased to answer any questions you may have.

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