MWD
METROPOLITAN WATER DISTRICT OF SOUTHERN CALIFORNIA

June 29, 1993

To: Board of Directors (Engineering & Operations Committee--Information) (Finance and Insurance Committee--Information)

From: General Manager

Subject: Hoover Negotiations

Report

In 1987, Metropolitan executed a 30-year Hoover contract (Contract) with the Federal Government providing for Metropolitan's entitlement to 247.5 megawatts of contingent capacity and 1,292 million kilowatt hours (kWh) per year of firm energy. Generation received from the Hoover Power Plant (Hoover), in addition to Metropolitan's Parker Power Plant entitlement, are sufficient to sustain the peak requirements of the Colorado River Aqueduct and import approximately 760,000 acre-feet of water at an equivalent unit cost of approximately $23 per acre-foot. The average annual base costs of the project are approximately $60 million of which Metropolitan pays 20.6 percent or approximately $13 million annually. In addition, there is a 2.5 mills/kWh surcharge on Hoover energy which is used for specific purposes including Colorado River Salinity Control. Collectively, the charges to Metropolitan equate to approximately $16 million annually at an average equivalent rate of 12.7 mills/kWh.

Over the past six years, administrative problems have surfaced and resulted in disagreements among the Western Area Power Administration (Western), the United States Bureau of Reclamation (Reclamation) and each of the Hoover Contractors (collectively referred to as Parties and individually as Party). Western is responsible for marketing the power and administration of the Contract and Reclamation is responsible for the operation and maintenance of Hoover. In order to resolve the administrative problems, in February 1993, a group consisting of representatives from each Party was formed to address eleven outstanding administrative issues. Metropolitan has participated in extensive discussions through which consensus solutions are being developed on all issues. Shown in the attachment is a brief summary of the issues and the current proposed resolution of each issue.

Metropolitan would benefit from the resolution of these issues both from an economic standpoint and from an operating standpoint. If implemented, as currently discussed by the Parties, the savings from the recommendations would be on the order of 1 mill/kWh, which on a present worth basis is the equivalent of approximately $13 million. Operational benefits that would be achieved from increased communication regarding operation and maintenance issues, and the government's awareness of the Contractor's concerns are also extremely important. It is intended that these proposed resolutions to the issues be implemented by October 1, 1993. Metropolitan's staff plans to work actively in the next few months to reach that goal subject to your Board's approval of the final recommendations.

Board Committee Assignments

This letter is referred for information to:

The Engineering and Operations Committee because of its authority to study, advise and make recommendations with regard to energy matters in general pursuant to Administrative Code Section 2431 (i); and

The Finance and Insurance Committee because of its authority to study, advise and make recommendations with regard to disposition of funds pursuant to Administrative Code Section 2441 (c).

Recommendation

For information only.

for R W Balcerzak
General Manager

DAL:bvf

Attachment

Hoover Negotiations

1. REPLACEMENTS: Replacements are investments in capital equipment which are necessary to maintain the project in good operating condition. The Contract intended that Reclamation seek appropriation from Congress for the funds necessary for replacements on an annual basis. Appropriations would thus allow the cost of the replacement to be amortized over 50 years, reducing the economic impact in any one year to the Contractors of these investments on annual rates. However, due to budget constraints and political pressure, Reclamation has instead been "expensing" replacements, resulting in recovery of the full cost of the replacement in the year the investment is made. This results in the Contractors paying as much as approximately $12 million in some years and the government's recovery of more capital from the Contractors during the Contract period than it would have recovered if appropriations had been obtained.

The resolution of this issue, as currently being discussed, is for Reclamation to continue to seek appropriations from Congress. If it is unsuccessful, the Contractors would not object to "expensing" replacements provided Western would agree to reimburse the Contractors upon termination of the Contract in 2017. Western would reimburse the Contractors over a five-year period the amount of principal that would have been outstanding as of September 30, 2017 if such amounts had been appropriated.

2. VISITOR FACILITIES: The Hoover Power Plant Act of 1984 (1984 Act) authorized the construction of new visitor facilities at Hoover in the amount of $32 million (in 1983 dollars), which when adjusted for inflation and interest during construction (IDC) currently equates to approximately $51 million. This amount is to be reimbursed by the Contractors through payment of their power rates. However, to date, Reclamation has obtained Congressional approval for the appropriation of $80.3 million from the United States Treasury (Treasury), which when added to IDC equates to a total of $106 million. This higher amount has been used by Western in its computation of costs for Hoover power rates. This results in exceeding the amount the Contractors previously agreed to repay the Treasury by approximately $55 million.

The recommendation is that this $55 million of additional cost be recovered in user fees, to the extent possible. User fees may include increased tour prices and parking fees.

3. AMENDING REGULATIONS: Some Contractors are concerned that Western's current regulations do not reflect the rate methodology currently being used by Western. This is one of

the issues that is currently under review by the Federal Energy Regulatory Commission (FERC). It has been suggested that this issue be held in abeyance pending the FERC decision.

4. MULTI-PROJECT BENEFITS AND COSTS: The Contract anticipated the integration of Hoover with other federal projects on the Colorado River, and requires that any benefits and costs arising from such integration be shared among the projects. Consistent with that intent, Western included in the current rate order charges for costs incurred by other federal projects which Western believes are reasonably incurred by Hoover. However, this inclusion of costs in Hoover rates represents only a partial solution to the concern in that the direct power benefits shared between Hoover and the other federal projects have not yet been considered.

The resolution of this issue is to develop a procedure for the justification of such costs, and outline a program to calculate and allocate the direct power benefits between Hoover and the other federal projects.

5. ENGINEERING AND OPERATING COMMITTEE (E&OC): The Parties are focusing on formalizing a current working group that was formed to improve communications between the Contractors and the government on administrative, operation and maintenance issues, and to provide an avenue for discussion on cost and revenue issues. Additionally, the Parties have suggested that a Steering Committee be created to oversee the E&OC, to review and agree upon Hoover operating criteria, practices and procedures, and to attempt to facilitate the resolution of differences among the Parties through informal means whenever possible.

6. BILLING AND PAYMENT: Due to fluctuation in generation at Hoover and the Contract's billing procedures which are based on actual generation received, Reclamation is having increasing problems meeting its expenses in a timely fashion.

The resolution to this issue proposes to levelize the billing system to the Contractors, and thus revenue receipts to Reclamation, based on estimated energy generation and to adjust the billing at the end of the fiscal year based on actual energy generated. As part of this resolution, a mechanism would be established to assure that 50 percent of the power revenues are collected from capacity, and 50 percent are collected from energy, consistent with the Contract and applicable regulations. Also, since 1987, because of the low energy production, more revenue has been collected from capacity. It is proposed that the Parties agree to reimburse the capacity component for the accumulated capacity/energy imbalance.

7. WORKING CAPITAL: With the revised billing procedure, Reclamation has agreed to reduce the demand for working capital, which is currently $8 million, to $2 million and use such working capital only to bridge the time delay between the date of billing by Western for power sales and the date of receipt by Reclamation of the resulting revenue.

8. PRINCIPAL PAYMENTS: Currently, Reclamation pays the Treasury debt for outstanding appropriations on an annual basis. However, increments of the debt are collected on a monthly basis from the Contractors for the retirement of such debt. Once collected, these funds are held in an account that does not collect interest.

The Contractors have requested that Reclamation pay the Treasury when funds are available. This procedural change would decrease the amount of interest the Contractors would pay over the term of the Contract.

9. ANNUAL RATE ADJUSTMENT: Some Contractors were concerned regarding the procedures followed by Western in reviewing and adjusting rates, and their lack of opportunity to participate in that process. However, with the change in billing, rates would be calculated and adjusted annually and the Contractors would have an opportunity to more actively participate in the process.

10. AUDITS: The Contract allows each Contractor to review the records and books of Reclamation and Western. To date, audits have been performed, although they have been done at random in an ad hoc fashion.

In order to develop more meaningful audits, the Contractors propose the establishment of an audit protocol providing, among other things, for the Contractors to implement joint financial audits of Hoover. All Contractors would be involved in the joint audit, at their own determination.

11. ADMINISTRATION OF UPRATER CREDITS: The 1984 Act provided for the refurbishment of the Hoover units thereby increasing the total capacity of the plant. In so doing, the financing of the construction project was agreed to be paid by those Contractors benefiting from the increase in capacity (Schedule B Contractors). The Contract defines the terms and conditions for the reimbursement of such financing through the use of uprating credits on the Schedule B Contractors' power bills. Although the Schedule B Contractors have been receiving uprater credits, Western has never developed an implementation plan for the full administration of the uprater credits.

To resolve this issue, procedures would be established to implement the administration of uprater credits in accordance with the Contract.