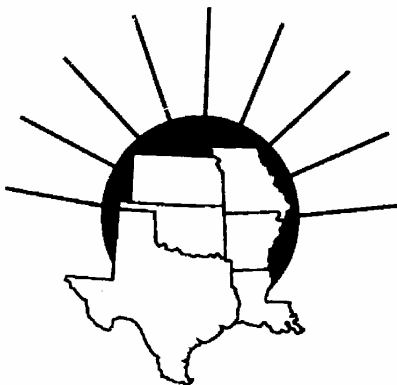


Why Cost-Based Rates?

- Cost-based rates are tariffs for electric energy and capacity that are designed to recover the cost of generating or delivering the energy and capacity. In the case of investor-owned utilities, cost-based rates also include a “reasonable” return on shareholders’ investments in the production facilities. Cost-based rates for rural electric cooperatives, municipally owned electric utilities and power marketing administrations such as Southwestern Power Administration do not include a profit or rate of return.
- Until recently, cost-based rates were the norm for electric utility transactions. However, beginning in the 1990s, the Federal Energy Regulatory Commission began to allow investor-owned utilities and power marketers to charge “market-based rates” for wholesale power — in other words, they could charge what the market would bear for these transactions. This authority was based on the premise that sufficient competition exists in wholesale markets and thus market-based rates would reflect “just and reasonable” charges. Recent events have cast doubts on this premise.
- Section 5 of the Flood control Act of 1944 requires SWPA and other PMAs to market federal power “in such a manner as to encourage the most widespread use thereof at the lowest possible rates to consumers consistent with sound business principles...” Since enactment, this provision has been interpreted to require PMAs to sell federal power at cost-based wholesale rates.
- Some people in Congress (particularly the Midwest-Northeast Congressional Coalition) would like to require the PMAs to sell federal power at market-based rates. Such action would be contrary to the expressed intent of Congress over the past 60 years; would subject rural electric cooperatives and municipally owned electric utilities to daily, widespread fluctuations in wholesale power costs; would mean higher retail electric rates to more than 6 million consumers in 6 states receiving SWPA power; and would lead to the generation of federal power strictly on-peak (when market rates are highest), thus restricting or eliminating off-peak releases made to benefit fish and wildlife conservation, recreation, navigation and water supply.



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