Reply to July 10 Comments

I. Introduction

As part of its customer engagement process for developing an updated cost of service study ("COSS" or "Study"), Grant County Public Utility District #2 ("Grant PUD" or "PUD") requested comments and feedback regarding its draft COSS for transmission ("wheeling") service.

The draft study was published on June 19. Following a review process with stakeholders, written feedback regarding the draft Study was due to the PUD by July 10.

Grant PUD received two sets of comments. One set of comments from the United States, Bureau of Reclamation ("USBR"). The second set of comments was delivered jointly by the Quincy-Columbia Basin Irrigation District and the East Columbia Basin Irrigation District (jointly "the Districts").

Within their comments, the Districts noted that Federal Reserved power delivered from the USBR and wheeled across Grant PUD's transmission and/or distribution facilities are utilized to enable the Districts' irrigation water deliveries. Due to their relevance in this process, the comments and responses will be included with the final Transmission Rate Proposal, targeted to be published in July.

A recurring theme within their comments is the fact that many of Grant PUD's accounting titles include "PRP" in the title, and the misconception that the Priest Rapids Project ("PRP")-related costs are all generation costs. The April 17, 2008 Federal Energy Regulatory Commission's Order Issuing New License for continued operation of the Priest Rapids Project (available at https://www.grantpud.org/templates/galaxy/images/images/Downloads/About/Environment/ShorelineManagement/PriestRapidsProjectLicenseh1.pdf) lists several transmission specific components to the project.

Including the following on page 54 of the license:

> The project's six primary transmission lines (three at the Wanapum development and three at Priest Rapids development), totaling 56.5 miles, deliver project power to the transmission grid via the BPA's Columbia and Midway substations. Grant PUD is proposing no changes that would affect its own or other transmission services in the region. The project and its transmission lines are important elements in providing power and voltage control to local Grant County, Washington, communities and the region.

And including the following located on page 59 license:

> (e) three 230-kilovolt (kV) overhead transmission lines with: (i) the first transmission line connecting and terminating at 2 adjacent switchyards 1.5 miles away; (ii) the second running from one of the two switchyards north for 31 miles to the BPA's Columbia substation; and (iii) the third connecting the Wanapum substation with the Priest Rapids substation running south for 17 miles; and (f) appurtenant facilities.
>
> (f) three 230-kV transmission lines from the transformers at the powerhouse to the Priest Rapids switchyard 1 mile away, then continuing for 6 miles to the BPA's Midway substation;

Within their comments, the Irrigation Districts submitted a list of information requests stating additional information is necessary for them to fully evaluate the Draft COSS model and verify the accuracy of the results. Specifically, regarding the transmission and distribution costs proposed by the PUD in the COSS.

As part of their comments, the Districts have requested various information regarding Grant PUD's financial data. This financial information is gathered and published by Grant PUD's finance and accounting department in accordance with generally accepted accounting principles. Additionally, Grant PUD's financial statements are audited by an independent financial firm. Where specific data has been requested, the response to those inquiries may be provided via Grant PUD's records department. If additional data is

required, please visit www.grantpud.org/contact-us to complete a public records request form.

With regards to further comments concerning the designing of separate rates for certain customers that the parties consider separate and distinct from other system customers. Grant PUD offers the white paper from August 17, 2017 (see Attachment B) prepared by Brent Bischoff (Sr. Manager Power Delivery Engineering). Within the document Mr. Bischoff discusses how Grant PUD's electric distribution system is designed and operated.

This paper states in Part:

> *The Grant County PUD electric distribution system is designed as a networked system. This design practice is common in the electric utilities industry in order to provide the most reliable possible electric service to customers…This ensures that outage frequency and duration to utility customers are kept to a minimum…The distribution system is a networked system designed to provide the highest level of reliability and service to each customer regardless of their location in the service territory.*
>
> *…Since electric distributions systems are networked and provide equal quality of service to all customers, it is common utility practice to spread the cost to build, operate and maintain the system equally among customers…*

II. Irrigation Districts' Comments

Grant should establish a set of transmission/distribution wheeling rates that apply solely to the wheeling of Federal Reserved power to loads located on Grant's system. There is a unique and long-running history of how the 115KW facilities originally constructed by the Federal Government and now owned by the PUD were initially developed to deliver Federal Reserved power to USBR pumping plants that, in turn, are utilized to provide irrigation water to local farms throughout Grant County. These circumstances, however, differ from other potential usages of the PUD's transmission system including the wheeling of power from newly constructed generating resources to serve customers located

outside of Grant County. The Irrigation Districts believe that not all Grant PUD wheeling customers are similarly situated and therefore the Commission should have the flexibility to establish multiple sets of transmission rates that recognize these differences, should they choose to do so.

Grant PUD purchased certain transmission facilities from BPA in 1976 for a price of $4 million, plus the service provision for specified periods. At that time, Grant assumed the obligation to provide USBR up to 44 MW of wheeling free of charge for a 40-year period that ended on June 30, 2017. Grant provided this service as specified for this period. Grant further assumed an obligation to provide 66 MVA of no charge wheeling to Washington Water Power (now Avista) that ended on August 10, 1993.

The 40-year wheeling obligation represented the typical depreciation life for new facilities. But, in this case the facilities were used. Thus, while Grant PUD purchased the facilities, Grant was obligated to provide wheeling without additional charges for the life of the facilities; Grant PUD was not able to recover costs that were unrelated to the facilities capital cost, such as additional capital costs and Operation and Maintenance Expenses. These unrecovered costs from the PUD's wheeling customers have been borne by Grant PUD's retail customers.

The capital cost of substations and transmission lines represent only a portion of the costs to provide wheeling by Grant PUD. Grant PUD's updated COSS intends to capture all the costs of providing transmission (wheeling) service.

The PUD's primary system customer is its retail load and this load is considered equal with USBR load in the rate calculation shown in the COSS model. The PUD's treatment is consistent with FERC policy. Establishing rate treatment that provides preferential treatment to a specific class of customer is contrary to FERC policy and would create potential FERC risk.

At this time, Grant is not considering a separate wheeling rate for wheeling load verses wheeling generation.

For further discussion, see Section I – Introduction and Attachment B concerning how Grant PUD's system is designed and operated.

1. Grant's Transmission COSA that is ultimately utilized to establish new transmission rates for the wheeling of Federal Reserved power should only incorporate the PUD's actual, verifiable costs. In this vein, the 9.8% Return on Equity component of the Draft 2019 Transmission COSA does not appear to be tied to any actual, verifiable costs that the PUD incurred in CY 2017.

The model utilizes a cost of capital to reflect the financing costs associated with Grant PUD's capital costs. Rather than adjusting target revenue to meet financial metrics and obtaining cash necessary for capital investments, this method estimates the cost of capital, which includes the cost of equity in the market, and treats this as an operating cost.

Use of these funds carries with it, at a minimum, an opportunity cost. The cost estimates that Grant PUD would need to pay investors if the equity was not supplied by customers. Conversely, it represents a return that customers could expect to earn if they were able to invest that money in similar projects in the marketplace.

3. Grant's derivation of the annual revenue requirements for Grant's Transmission and Distribution wheeling rates should be performed in a consistent manner with its derivation of the annual revenue requirements for its retail rate classes.

Grant agrees that the methods should be consistent across the Studies.

4. Taxes included in the annual revenue requirements for Grant's Transmission and Distribution wheeling rates should reflect the actual amount of taxes that the PUD will owe on its provision of wholesale transmission/distribution wheeling services.

Grant PUD agrees with this statement.

5. The 13.2 KV distribution wheeling rate assessed to the USBR's Sand Hollow and Babcock pumping loads must reflect the fact that: 1) these two loads have unique physical interconnection characteristics, and 2) under the cost-causation principle there should be a lower proportion of Grant's overall system distribution costs allocated to the cost of service for these two discrete loads.

Similar to billing for an Irrigation District, Grant's transmission costs do not consider distance. Developing distance-based costs would be a significant undertaking and would result in costs that would be both below and above current estimated costs for the transmission customer class.

The Sand Hollow line is a distribution line of short distance, but this is not unique. Many Grant PUD service lines in the urban areas are short, and if the PUD were to calculate a short distance rate, Grant would need to acquire the total load data for a defined short distance. At present, this data is not readily available. The distribution level rates do not take into account the length of the distribution lines, which in general favors rural service.

The Babcock service conductor material is owned by USBR. A used USBR conductor was installed on this Grant distribution service in 2002. If new material is used for a conductor, the cost of the conductor represents approximately 4% of the total distribution service cost. This service is about 2.5 miles which is longer than most urban service. At this time, Grant PUD does not plan to calculate a special rate for this line, but if Grant were to do so, it could be higher than the average rate.

For further discussion, see Section I – Introduction and Attachment B concerning how Grant PUD's system is designed and operated.

Grant PUD is willing to discuss with USBR staff the possible terms for the PUD to purchase this conductor.

6. Grant should incorporate into the transmission rate billing units calculation all wholesale wheeling services it expects to provide during the upcoming rate period (i.e. CY 2020) including wheeling services that it provides to BPA, even if Grant charges BPA a different transmission rate under one or more pre-existing wheeling agreements.

The current COSS has assumptions for which contracts will be included in the new rate. Currently, the BPA wheeling service is included as part of the new transmission (wheeling) rate service.

7. Exhibit VIII to the Draft 2019 Transmission COSA contains an apparent error with regard to how non- USBR Point-to- Point transmission service is incorporated into the per-unit transmission rate. For example, inputting an assumed 100 MW monthly transmission usage figure into the PTP column should increase the total overall transmission billing units and reduce the per-unit (i.e. $/KW- yr. or $/KW – mo.) transmission wheeling charge. The current spreadsheet logic does not do this.

The spreadsheet logic in Exhibit VIII of the Draft 2019 Transmission COSS has been revised to include Firm Point-to-Point load in the Total System Load used to determine rates for the service over the 115kV-230kV system. At this time, Grant PUD does not have Firm PTP customers.

8. The Districts note that several line items in the Transmission O&M Expenses section in Exhibit III have "PRP" in the title. To the extent that these line items are associated with Priest Rapids Project-related costs, these line items should be removed from the set of Transmission O&M expenses incorporated into the annual transmission wheeling rate annual revenue requirement.

To the extent the items are generation related, Grant PUD agrees. If the items are related to the PRP transmission system, then they should be included as transmission costs. Also, see the Priest Rapids Project discussion in Section 1 - Introduction.

9. The Districts note that many of the line items in the Administrative & General Expenses section in Exhibit III have "PRP" in the title. To the extent that these line items are associated with Priest Rapids Project-related costs or revenues, I) these

line items should be removed from the set of Administrative & General expenses incorporated in to the annual transmission and distribution revenue requirements, or 2) the allocation factor(s) used to allocate total A&G expenses to the transmission wheeling rate and the distribution wheeling rate annual revenue requirements should be adjusted, if needed, to ensure that no Priest Rapids Project-related costs are assigned to the PUD' s transmission and/or distribution wheeling cost or service.

To the extent the items are generation related, Grant PUD agrees. If the items are related to the PRP transmission system, then they should be included as transmission costs. Also, see the Priest Rapids Project discussion in Section I - Introduction.

10. The Districts reserve the right to provide additional comments to Grant regarding the various allocation factors that are incorporated into the Draft 2019 Transmission COSA. In particular, the Districts have not been provided with the detailed data inputs to the "W/S-T" and the W/S-D" allocation factors. The Districts are therefore requesting that the PUD provide this information (sec Clarifying Question No. 18).

III. United States Bureau of Reclamation (USBR) Comments

GCPUD has stated the intent to develop one single wholesale transmission rate to apply to not only the USBR reserved power loads, but also to commercial wheelers (i.e., from wind and solar installations in the county to customers outside PUD boundaries). USBR requests that wholesale transmission and distribution rates be developed to represent the unique history of development of the transmission system within Grant PUD and the local nature of the loads served.

Grant PUD purchased certain transmission facilities from BPA in 1976 for a price of $4 million. At that time, Grant assumed the obligation to provide USBR up to 44 MW of wheeling free of charge for a 40-year period that ended on June 30, 2017. Grant provided this service as specified for this period. Grant further assumed an obligation to provide 66 MVA of no charge wheeling to Washington Water Power (now Avista) that ended on August 10, 1993.

The 40-year wheeling obligation represented the typical depreciation life for new facilities. But, in this case the facilities were used. Thus, while Grant PUD purchased the facilities Grant was obligated to provide wheeling without additional charges for the life of the facilities. Grant PUD was not able to recover costs that were unrelated to the facilities capital cost, such as additional capital costs and Operation and Maintenance Expenses. These unrecovered costs from the PUD's wheeling customers have been borne by Grant's retail customers.

The capital cost of substations and transmission lines represent only a portion of the costs to provide wheeling by Grant PUD. Grant's updated COSS intends to capture all the costs of providing transmission (wheeling) service.

For further discussion, see Section I – Introduction and Attachment B concerning how Grant PUD's system is designed and operated.

1. Exhibit II - Plant Data, Line 2 (Franchise and Consents) - USBR understands that the cost study is based on a standard FERC accounting system. Based on the Uniform System of Accounts and account descriptions, Account 302 Franchises and consents states "This account shall include amounts paid to the federal government, to a state or to a political subdivision thereof in consideration for franchises, consents, water power licenses, or certificates, running in perpetuity or for a specified term of more than one year, together with necessary and reasonable expenses incident to procuring such franchises, consents, water power licenses, or certificates of permission and approval, including expenses of organizing and merging separate corporations, where statutes require, solely for the purpose of acquiring franchises". It is USBR's understanding that this description refers to generating stations that are going through the licensing process. The $59 million gross plant in service and associated depreciation expense, should not be allocated to the wholesale transmission or distribution. Please explain why this should be included in wholesale transmission or distribution.

Grant PUD is reviewing its COSS calculation and as a result, the PUD may modify its study.

2. Exhibit II - Plant Data, Line 3 (Miscellaneous Intangible Plant) - USBR requests a breakdown and description of this $135 million gross plant in service item.

Grant PUD is in the process updating the PUD's accounting system to reflect the FERC Uniform System of Accounts. Currently, the PUD's accounting system reflects the use its own internal chart of accounts. For COSS purposes, the PUD's accounting department matched the current PUD accounts to the appropriate FERC accounts.

The FERC Uniform System of Accounts for Account #303 states the following:

A. This account shall include the cost of patent rights, licenses, privileges, and other intangible property necessary or valuable in the conduct of utility operations and not specifically chargeable to any other account.
B. When any item included in this account is retired or expires, the book cost thereof shall be credited hereto and charged to account 426.5, Other Deductions, or account 111, Accumulated Provision for Amortization of Electric Utility Plant (for non-major utilities, account 110, Accumulated Provision for Depreciation and Amortization of Electric Plant), as appropriate.
C. This account shall be maintained in such a manner that the utility can furnish full information with respect to the amounts included herein.

Grant PUD believes that the plant balance for Account 303, reflected in Exhibit II, Line 3 – Miscellaneous Intangible Plant have been recorded properly. This is support by the Independent Audit Report Letter reflected in the PUD's 2018 Annual Report (See Attachment A), which states:

As part of obtaining reasonable assurance about whether the District's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts.

If further information is still needed, see Section I – Introduction for Grant PUD's procedures in acquiring public data.

3. Exhibit II- General Plant, Line 36 (Office Furniture and equipment) - USBR requests a breakdown and description of this $43 million item.

Grant PUD is in the process updating the PUD's accounting system to reflect the FERC Uniform System of Accounts. Currently, the PUD's accounting system reflects the use its own internal chart of accounts. For COSS purposes, the PUD's accounting department matched the current PUD accounts to the appropriate FERC accounts.

The FERC Uniform System of Accounts for Account #391 states the following:

> This account shall include the cost of office furniture and equipment owned by the utility and devoted to utility service, and not permanently attached to buildings, except the cost of such furniture and equipment which the utility elects to assign to other plant accounts on a functional basis.
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> ITEMS
>
> 1. Bookcases and shelves.
> 2. Desks, chairs, and desk equipment.
> 3. Drafting-room equipment.
> 4. Filing, storage, and other cabinets.
> 5. Floor covering.
> 6. Library and library equipment.
> 7. Mechanical office equipment, such as accounting machines, typewriters, etc.
> 8. Safes.
> 9. Tables.

Grant PUD believes that the plant balance for Account 391, reflected in Exhibit II, Line 36 – Office furniture and equipment have been recorded properly. This is support by the Independent Audit Report Letter reflected in the PUD's 2018 Annual Report (See Attachment A), which states:

As part of obtaining reasonable assurance about whether the District's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts.

If further information is still needed, see Section I – Introduction for Grant PUD's procedures in acquiring public data.

4. Exhibit II - Plant Data, Line 42 (Communication equipment) - This line item shows up as $225 million gross plant in service with associated depreciation and 100% wholesale allocation USBR requests a breakdown and description of this item. Please explain why this should be included in wholesale transmission or distribution.

Grant PUD is in the process updating the PUD's accounting system to reflect the FERC Uniform System of Accounts. Currently, the PUD's accounting system reflects the use its own internal chart of accounts. For COSS purposes, the PUD's accounting department matched the current PUD accounts to the appropriate FERC accounts.

The FERC Uniform System of Accounts for Account #397 states the following:

This account shall include the cost installed of telephone, telegraph, and wireless equipment for general use in connection with utility operations.

ITEMS

1. Antennae.
2. Booths.
3. Cables.
4. Distributing boards.
5. Extension cords.
6. Gongs
7. Hand sets, manual and dial.
8. Insulators.
9. Intercommunicating sets.
10. Loading coils.

11. Operators' desks.
12. Poles and fixtures used wholly for telephone or telegraph wire.
13. Radio transmitting and receiving sets.
14. Remote control equipment and lines.
15. Sending keys.
16. Storage batteries
17. Switchboards.
18. Telautograph circuit connections.
19. Telegraph receiving sets.
20. Telephone and telegraph circuits.
21. Testing instruments.
22. Towers.
23. Underground conduit used wholly for telephone or telegraph wires and cable wires.

Grant PUD believes that the plant balance for Account 397, reflected in Exhibit II, Line 42 – Communication equipment have been recorded properly. This is support by the Independent Audit Report Letter reflected in the PUD's 2018 Annual Report (See Attachment A), which states:

> As part of obtaining reasonable assurance about whether the District's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts.

If further information is still needed, see Section I – Introduction for Grant PUD's procedures in acquiring public data.

5. Exhibit II - Plant Data, Line 43 (Miscellaneous Equipment) - This line item shows up as $5.3 million gross plant in service with associated depreciation; and 100% wholesale allocation. Based on the Uniform System of Accounts and accounts description, items such as hospital and infirmary equipment, kitchen equipment, employees' recreation equipment, restaurant equipment, soda fountains etc. are to be included in this account. Please explain why this should be included in wholesale transmission.

Grant PUD is in the process updating the PUD's accounting system to reflect the FERC Uniform System of Accounts. Currently, the PUD's accounting system reflects the use its own internal chart of accounts. For COSS purposes, the PUD's accounting department matched the current PUD accounts to the appropriate FERC accounts.

The FERC Uniform System of Accounts for Account #398 states the following:

> This account shall include the cost of equipment, apparatus, etc., used in the utility operations, which is not includible in any other account of this system of accounts.
>
> ITEMS
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> 1. Hospital and infirmary equipment.
> 2. Kitchen equipment.
> 3. Employees' recreation equipment.
> 4. Radios.
> 5. Restaurant equipment.
> 6. Soda fountains.
> 7. Operators' cottage furnishings.
> 8. Other miscellaneous equipment.
>
> NOTE: Miscellaneous equipment of the nature indicated above wherever practicable shall be included in the utility plant accounts on a functional basis.

Grant PUD believes that the plant balance for Account 398, reflected in Exhibit II, Line 43 – Miscellaneous equipment have been recorded properly. This is support by the Independent Audit Report Letter reflected in the PUD's 2018 Annual Report (See Attachment A), which states:

> As part of obtaining reasonable assurance about whether the District's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts.

If further information is still needed, see Section I – Introduction for Grant PUD's procedures in acquiring public data.

6. Exhibit II - Structures and Improvements, Poles and Towers and Overhead conductors, Lines 15, 17, 18, 19, 23, 25, and 26- Depreciation is being calculated on items that were once federally-owned. Please explain how elements which were once wholly-owned by the federal government are now subject to depreciation as a part of wholesale transmission and distribution. What "Initial Equipment" value was used to calculate the depreciation of the formerly federally owned structures and equipment?

Grant does not track the depreciation of individual poles and lines. They are treated as a type of item that is used and provides service over its useful life. Over a 40-year period, the cost of the facilities would have been fully depreciated.

As far as the specific USBR facilities purchased, many of facilities have been replaced because of wear or upgrading. Previously, Grant PUD retail customers paid the additional costs to maintain the wheeling service for the 40 years. This liability was not recovered from USBR.

7. Exhibit III - Transmission O&M Expenses, Lines 3, 4, 5, 13, 14, 15 - Items with "QC, PEC, PRP and Gen" appear to be associated with generation functions. USBR had made a previous comment that any costs associated with generation function should be excluded from the wholesale transmission. Please explain why these are a part of wholesale transmission.

To the extent the items are generation related, Grant PUD agrees. If the items are related to the PRP transmission system, then they should be included as transmission costs. Also, see the Priest Rapids Project discussion in Section I - Introduction.

8. Exhibit III - Transmission O&M Expense, Line 6 (Transmission of Electricity By Others)- USBR requests a clarification of this line item - $572k.

Grant PUD is reviewing its COSS calculation and as a result, the PUD may modify its study.

The FERC Uniform System of Accounts for Account #565 states the following:

> This account shall include amounts payable to others for the transmission of the utility's electricity over transmission facilities owned by others.

If further information is still needed, see Section I – Introduction for Grant PUD's procedures in acquiring public data.

9. Exhibit III - Administrative & General Expenses, several items with "QC, PEC, and PRP" appear to be associated with generation functions. USBR had made a previous comment that any costs associated with generation function should be excluded from the wholesale transmission. Please explain why these are a part of wholesale transmission.

To the extent the items are generation related, Grant PUD agrees. If the expenses are related to the PUD's transmission system, then they should be included as transmission related.

For QC (Quincy Chute), PEC (Potholes East Canal), and PRP (Priest Rapids Project), the PUD considers these "common" operational expenses that are shared by production, transmission, and distribution services. Grant PUD does not track administrative and general expenses by function. Grant PUD believes this practice is standard industry practice.

For further discussion, see the discussion provided in Section I – Introduction.

10. Exhibit III - Distribution O&M Expenses, Lines 74 and 75, Meter Install ($1.1M) and Customer Install ($164k) expenses, do not appear to be directly associated with wholesale distribution. Please provide background information on why these should be part of wholesale distribution function.

Grant PUD is reviewing its COSS calculation and as a result, the PUD may modify its study.

11. Exhibit III-Distribution O&M Expenses, Line 76, USBR requests a breakdown and description of this $6 million miscellaneous item.

Grant PUD is in the process updating the PUD's accounting system to reflect the FERC Uniform System of Accounts. Currently, the PUD's accounting system reflects the use its own internal chart of accounts. For COSS purposes, the PUD's accounting department matched the current PUD accounts to the appropriate FERC accounts.

The FERC Uniform System of Accounts for Account #588 states the following:

> This account shall include the cost of labor, materials used and expenses incurred in distribution system operation not provided for elsewhere.
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> ITEMS
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> Labor:
> 1. General records of physical characteristics of lines and substations, such as capacities, etc.
> 2. Ground resistance records.
> 3. Joint pole maps and records.
> 4. Distribution system voltage and load records.
> 5. Preparing maps and prints.
> 6. Service interruption and trouble records.
> 7. General clerical and stenographic work except that chargeable to account 586, Meter expenses.
> Expenses:
> 8. Operating records covering poles, transformers, manholes, cables, and other distribution facilities. Exclude meter records chargeable to account 586. Meter Expenses and station records chargeable to account 582, Station Expenses (For Nonmajor utilities, account 581.1, Line and Station Expenses), and stores records (For Nonmajor utilities, station records) chargeable to account 163, Stores Expense Undistributed (For Nonmajor utilities, account 581.1, Line and Station Expenses).
> 9. Janitor work at distribution office buildings including snow removal, cutting grass, etc.

Materials and Expenses:
10. Communication service.
11. Building service expenses.
12. Miscellaneous office supplies and expenses, printing, and stationery, maps and records and first-aid supplies.
13. Research, development, and demonstration expenses (Major only).

Grant PUD believes that the plant balance for Account 588, reflected in Exhibit III, Line 76 – Miscellaneous distribution expenses have been recorded properly. This is support by the Independent Audit Report Letter reflected in the PUD's 2018 Annual Report (See Attachment A), which states:

> As part of obtaining reasonable assurance about whether the District's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts.

If further information is still needed, see Section I – Introduction for Grant PUD's procedures in acquiring public data.

12. Exhibit III - Distribution O&M Expenses, Lines 82 and 83, Maintenance of Street Lighting ($50k) and Maintenance of Meters ($129k) expenses, do not appear to be directly associated with wholesale distribution rate. Please provide background information on why these should be part of wholesale distribution function.

Grant PUD is reviewing its COSS calculation and as a result, the PUD may modify its study.

13. Exhibit IV - M&S and Prepayments, Lines 7 and 8 (Prepayments) - These items "PRP Revenue Insurance - $1.1 million" and "PRP Revenue Prepayments Water Rights - 172k". It is USBR's understanding that this is unrelated to the transmission function. Please provide information on how the 0.7177% was derived and how the product should be part of wholesale function.

Grant PUD is reviewing its COSS calculation and as a result, the PUD may modify its study.

14. Exhibit V - ROR, Line 2 - The Return on Equity (ROE) may not be applicable to a non-investor owned utility. If Grant PUD believes otherwise, please provide background information on how this is calculated.

Cost of equity is based on the FERC approved return on equities (ROE) of PacifiCorp and Puget Sound Energy, which are both interconnected with Grant PUD. Avista's transmission rate is currently based on a stated rate and, therefore, there is no specific ROE that has been identified in the determination of the transmission rate (i.e. based on a settled black box). (For reference, see the 2017 COSS, Exhibit V, footnote C.)

15. Exhibit VI - Other Taxes, Lines 23, and 25 (PRP Revenue) - The PRP taxes seem to be associated with generation and not wholesale transmission. Please provide background on why these should be a part of the wholesale function.

To the extent the items are generation related, Grant PUD agrees. If the items are related to the PRP transmission system, then they should be included as transmission costs. Also, see the Priest Rapids Project discussion in Section 1 - Introduction for further explanation.

16. Exhibit VII - Wheeling Revenues, Lines 7, 8, 9, and 10 - Four sources of wheeling revenue are listed. Will these sources be under contract throughout the life of the USBR contract? How will the addition or reduction of wholesale customers impact the wholesale transmission and distribution?

The first two items (Puget Sound Energy and Vantage Energy) are for a bus interconnection fee and the current assumption is that these two contracts will remain as stated.

The second two items (Seattle City Light and Tacoma Power) represent an accrual of a prepaid fee for an exchange service. These revenue credits continue into the future. Both of these contracts expire on January 1, 2027, At this point in time, Grant PUD does not know the intentions of either party.

If additional customers such as a new generation plant are added to the system, the customers will be included the rate calculation resulting from the COSS data. Additional customers will increase the billing units under a wheeling rate. Conversely, if customers leave the system, the billing units would be reduced.

17. We understand that the cost study will be utilized to determine revenue requirements and wholesale wheeling rates. It is USBR's request that a specific wholesale rate for Federal Reserved Power customers be developed to incorporate the unique nature of the customers served and the installation that was developed to server those customers.

The customers served with Reserved Power utilize the Grant system and there is not a unique nature from a technical perspective. For further information, please see Attachment B regarding Distribution System Networked Design and Infrastructure Cost Recovery.

The PUD's primary system customer is its retail load and this load is considered equal with USBR load in the rate calculation shown in the COSS model. The PUD's treatment is consistent with FERC policy. Establishing rate treatment that provides preferential treatment to a specific class of customer is contrary to FERC policy and would create potential FERC risk.

Attachment A

MOSSADAMS

Report of Independent Auditors on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

The Board of Commissioners
Public Utility District No. 2 of Grant County, Washington

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Public Utility District No. 2 of Grant County, Washington's (the District), which comprise the statement of net position as of December 31, 2018, and the related statements of revenues, expenses and changes in net position, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated April 9, 2019.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the District's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control. Accordingly, we do not express an opinion on the effectiveness of the District's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the District's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Moss Adams LLP

Seattle, Washington
April 9, 2019

Attachment B- Distribution System Networked Design and Infrastructure Cost Recovery

The Grant County PUD electric distribution system is designed as a networked system. This design practice is common in the electric utilities industry in order to provide the most reliable possible electric service to customers. Ideally distribution substations are built in close enough proximity to each other so the entire load from one substation can be redistributed and fed from adjacent substations in the event of a failure at one substation, a fault on a distribution line, or in the event a line or transformer needs to be taken out of service for maintenance. This ensures that outage frequency and duration to utility customers are kept to a minimum. Main distribution feeder lines are built out from the substation on a path that will most effectively deliver power to a given area and to provide a connection point to a main distribution feeder from an adjacent substation. Radial feeders are then connected to the main feeders to serve groupings of customers. Customers can be served from either the main or radial feeders. In some instances where customer density is low, it is not economically feasible for substations to be built close enough together to provide this tie to a second substation source (sometimes referred to as contingent service). The distribution system is a networked system designed to provide the highest level of reliability and service to each customer regardless of their location in the service territory.

Electric utility customers are dependent on the proper operation of all distribution system components on the circuit from their electric meter back to the substation transformer. These components include the substation power transformer, feeder circuit breakers, distribution lines, voltage regulators, distribution capacitor banks, disconnect switches, power poles, fuses, and distribution transformers. In the network, components closest to the customer serve only one or a few customers. Conversely, components closest to the substation are shared by many customers. The amount of distribution system infrastructure required to serve any single customer is primarily a factor of their physical distance from the substation. Components inside a substation are shared by all customers served from that substation. The distribution system is a networked system designed to provide the same level of service to each customer but each customer depends on a different amount of distribution infrastructure based on their distance from the substation from which they are served; the farther a customer is from the substation, the more infrastructure is required to serve them.

Electric distribution utilities establish rates to recover two basic components of the cost to serve customer load, the cost of the energy consumed by the customer and the cost to build, operate and maintain the electric distribution system. The energy consumed by each customer is easily measured by the service meter. Therefore the utility can simply and accurately account for each customer's energy usage and charge the customer appropriately for their share of consumed energy - seen as kWh on the bill. The individual customer share of the cost to build, operate and maintain the distribution system is not easily measured. In order to recover this cost, the utility must chose a method to allocate the distribution system cost to its customers. As explained above the networked electric distribution system is designed to provide equal quality of service to each customer but each customer utilizes a different amount of infrastructure in order to be served. Since electric distributions systems are networked and provide equal quality of service to all customers, it is common utility practice to spread the cost to build,

operate and maintain the system equally among customers. This is considered fair based on quality of service provided but it is not necessarily fair based on customer share of infrastructure required to serve their load. This equality of service model for cost recovery results in customers that are close to the substation paying a larger portion of the distribution system cost relative to the portion of infrastructure they utilize in order to be served. The converse is true for customers who are more remote from the substation – they pay a smaller portion of the total distribution system cost relative to the amount of infrastructure required to serve them. Effectively under this common equality of service model where distribution costs are spread equally across a customer class, the customers close to the substation are subsidizing the customers who are far from the substation.

Another method that electric utilities could use to recover distribution system costs would be to develop a method to determine what portion of the distribution system each customer utilizes for their service and proportionally charge each customer. Using this model, each customer would pay their fair share of cost based on the infrastructure required to serve their load. Customers farther away from the substation would pay higher rates. Although this may be a more fair allocation of cost, it would be very difficult for a utility to track and administer. Additionally every time a customer connected to or disconnected from a distribution circuit, the share of cost paid by all customers on that circuit would have to be recalculated and reallocated. Rates would be volatile. This distribution system cost recovery method is discussed here for illustration only because it is not used in practice.

The equality of service model is the common electric distribution utility practice to recover cost to build, operate and maintain the electric distribution infrastructure. The customer sees this charge in what is called the “basic” or “service” fee on their bill. This cost recovery method is considered fair to all customers based only on the fact that the utility provides equal quality of service to all customers. This method spreads the infrastructure cost equally across each rate class. On the other hand this common cost recovery method is unfair to customers from another perspective. This unfairness stems from the fact that customers require varying amounts of distribution infrastructure to serve their load based generally on their proximity to the substation serving their load. A customer further from the substation requires a larger proportion of the distribution infrastructure to serve their load than a customer adjacent to the same substation. Each infrastructure cost recovery method is fair from one perspective and unfair from another perspective. The method an electric utility uses to recover the cost of distribution infrastructure is based on a justifiable measure of fairness, practicality of administering that method, policy established by the governing body and industry best practice.

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Grant County PUD
September 19, 2017