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REPORT TO THE CONGRESS

Discounts Granted Generating And Transmission Cooperatives, Eastern Division, Missouri River Basin Project B-125042

Bureau of Reclamation

Department of the Interior

BY THE COMPTROLLER GENERAL
OF THE UNITED STATES

AUG. 9, 1968

COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

B-125042

To the President of the Senate and the
Speaker of the House of Representatives

This is our report on the review of discounts granted generating and transmission cooperatives in the Eastern Division of the Missouri River Basin Project, Bureau of Reclamation, Department of the Interior.

Copies of this report are also being sent to the Director, Bureau of the Budget, and to the Secretary of the Interior.

Elmer B. Staats

Comptroller General
of the United States

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WHY THE REVIEW WAS MADE

The General Accounting Office (GAO) has made a review of the Department of the Interior's policy of granting discounts on power sales to generating and transmission cooperatives (G&Ts) located in the Eastern Division of the Missouri River Basin Project to determine the effect on the repayment of the Government's investment in the project.

The Eastern Division serves all or portions of Montana, Nebraska, Iowa, Minnesota, and the Dakotas.

FINDINGS AND CONCLUSIONS

The Bureau of Reclamation's rates for the sale of electric power in the area have not been set to cover the cost of transmitting power to customers located in close proximity to a Bureau substation.

These customers must construct, at their own expense, feeder lines or pay for the transmission or "wheeling" of power over the lines of a third party.

GAO examined discounts granted in calendar year 1965 to two of nine G&Ts and found that of these discounts, $300,000, were granted on power deliveries to G&T members located in close proximity to the Bureau's substations, which they would not have received if they had purchased power directly from the Bureau.

The G&Ts perform certain services for their members located in close proximity to a Bureau substation, which the Bureau would have to perform if these members had built their own feeder lines or had made their own wheeling arrangements. GAO estimates, however, that the discounts granted to one of the cooperatives in 1965 were about $176,000 more than what the Bureau's cost would have been under wheeling arrangements consistent with that on which the rates were established. (See p. 16.)

RECOMMENDATIONS OR SUGGESTIONS

GAO suggested, in a draft report, that the Secretary of the Interior direct the Bureau to reexamine, in connection with future contracts or contract amendments with G&Ts, discounts granted in lieu of wheeling power short distances. GAO suggested also that such discounts be limited to those deliveries which conform to the wheeling policy on which the power rates were established.

AGENCY ACTIONS

The Department did not agree with GAO's suggestions but, with regard to the amount of discounts allowed the G&Ts, stated that the contracts provide that if average wheeling costs are less than 1 mill the lower cost will apply. The Department stated that it would have no objection to making a cost finding of this type. (See p. 19.)

ISSUES FOR FURTHER CONSIDERATION

GAO continues to believe that its suggestions have merit and therefore is recommending that they be adopted. The Department's cost-finding study on the relationship of wheeling costs to the discounts being granted to G&Ts should be based on the wheeling policy on which the rates were established and should consider all alternatives including estimates of the Bureau's cost of constructing and operating its own transmission lines to provide direct service to members of the G&Ts that are eligible for such service at Bureau expense.

LEGISLATIVE PROPOSALS

None.

COMPTROLLER GENERAL'S
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DIGEST

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LEGISLATIVE PROPOSALS

None.

INTRODUCTION

As a part of a continuing review of the power marketing activities of the Bureau of Reclamation, Department of the Interior, the General Accounting Office has reviewed the discounts allowed on power sales to generating and transmission cooperatives (G&Ts) located in the Eastern Division, Missouri River Basin Project (MRBP) power marketing system. These discounts were granted the G&Ts in lieu of the Bureau's constructing transmission facilities or providing the equivalent transmission services by contract with third party utilities referred to as "wheeling."

This review was made pursuant to the Budget and Accounting Act, 1921 (31 U.S.C. 53), and the Accounting and Auditing Act of 1950 (31 U.S.C. 67).

Our review was made at the Bureau's offices located in Washington, D.C.; Billings, Montana; Watertown, South Dakota; and Denver, Colorado. We reviewed policies and procedures, contractual provisions, and other documents and information pertinent to the allowances by the Bureau of discounts in lieu of wheeling. The Eastern Division of MRBP is the only power marketing area in which discounts in lieu of wheeling have been allowed by the Bureau, and this report is related to these specific discounts. The principal officials responsible for the activities discussed in this report are listed in appendix I.

BACKGROUND

GENERAL

The development of water resources in the Missouri River Basin is conducted jointly by the Bureau of Reclamation and the Corps of Engineers under a comprehensive plan as set forth in Senate Document 191 and House Document 475 approved by the Flood Control Act of 1944 (58 Stat. 891). Although each agency operates the projects it constructs, the Bureau is responsible for constructing and operating the transmission lines and for marketing all power not required in project operations.

The sale of MRBP power is governed by the Reclamation Act of 1939 (43 U.S.C. 485h) and the Flood Control Act of 1944 (58 Stat. 891). These acts require that the Secretary of the Interior sell the power at such rates as, in his judgment, will produce sufficient revenues to recover operating costs and the Government's investment in power facilities, with interest.

POWER RATES

As a basis for determining appropriate rates at which the power must be sold to recover the reimbursable project costs within the established time periods, the Bureau periodically prepares a power system average rate and repayment study. Such a study involves the compilation of historical data and future projections relating to power systems investment, operation and maintenance expenses, provisions for depreciation, interest, and other proper expenses for the power system.

The sales of the estimated power generation are generally divided into classes of service: use in project operations, nonfirm energy, and firm energy. The rates for power used in project operations are established on the basis of assigned costs for producing the power by the Government, and nonfirm energy rates are generally established on the basis of estimated savings in fuel costs that would otherwise be incurred by a customer operating a fuel-fired power plant. The average rate for the firm commercial energy is established by determining the remaining power revenues that must be obtained from firm power sales to repay the remaining reimbursable project costs which are to be repaid from power revenues.

The Bureau's internal correspondence indicates that the rates established for the MRBP firm power sales included a factor to recover transmission costs. We were unable, however, to determine from documentation made available to us what portion of the firm energy rate was specifically associated with the recovery of the cost of transmission and delivery, whether through the use of Government facilities or of the facilities of third parties.

In response to a congressional inquiry, however, an Assistant Secretary of the Department stated on May 2, 1955, The sale of MRBP power is governed by the Reclamation Act of 1939 (43 U.S.C. 485h) and the Flood Control Act of 1944 (58 Stat. 891). These acts require that the Secretary of the Interior sell the power at such rates as, in his judgment, will produce sufficient revenues to recover operating costs and the Government's investment in power facilities, with interest.

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In response to a congressional inquiry, however, an Assistant Secretary of the Department stated on May 2, 1955, that the Bureau had not established a power rate structure in the Missouri River Basin to cover the cost either of constructing feeder lines from its substations to customers in the vicinity of such substations or of wheeling fees to reach such customers.

The Department has encountered difficulties in obtaining sufficient revenues to repay the Government's investment in MRBP commercial power facilities. A study prepared by the Department in December 1963, at the request of the House Committee on Interior and Insular Affairs, on ways and means of placing the MRBP in a sound financial position was discussed extensively during congressional hearings held in 1964 and 1965 in connection with Public Law 89-108 (79 Stat. 433) which authorized construction of the Garrison diversion unit of the MRBP. The MRBP average rate and repayment studies, prepared by the Bureau for fiscal years 1966 and 1967, have not included projections as to when the Government's investment will be repaid but instead have indicated that economic analyses, which would permit reasonably accurate projections, were under way.

Criteria for negotiating power contracts

In August 1949, the Secretary of the Interior announced that the Bureau had been authorized to negotiate contracts for the marketing of power by using criteria which he had approved for the marketing of the first power to become available from power plants to be installed in dams constructed, or about to be constructed, on the Missouri River between Fort Peck, Montana, and Omaha, Nebraska, by the Corps of Engineers. These criteria defined the initial marketing area and provided that the Bureau observe the rights of preference customers (public corporations or agencies, and cooperatives or other nonprofit organizations financed in whole or part by loans made pursuant to the Rural Electrification Act of 1936 and any amendments thereof). The Secretary announced also that a main-trunk transmission system was planned to interconnect and coordinate operation of all MRB power projects for maximum firm power production.

Interim rate schedules expected to produce revenues sufficient to meet repayment requirements, as well as to provide power at the lowest possible rates considered consistent with sound business principles, were approved by the Secretary in March 1950.

Criteria for furnishing wheeling services

In April 1950, the Bureau stated that members of Congress had previously indicated their desire that all power agencies of the Department of the Interior explore the possibilities of wheeling power beyond load centers (points at which the power load of a given area is assumed to be concentrated) over existing transmission facilities of third parties.

In July 1950, the Secretary issued a set of principles to be followed in negotiating contracts for wheeling power over lines owned by third parties. These principles stated, in general, that the arrangements should provide the Government with an equal or more advantageous method of supplying power to its customers than through construction by the Government of separate transmission facilities. These principles stated also that the compensation payable for the use of transmission capacity of others should be reasonable but in no event exceed the cost to the Government of its own transmission capacity.

Subsequent to the issuance of these principles, the Keating Amendment was adopted as a proviso in the Department of the Interior Appropriation Act, 1952 (65 Stat. 255). This amendment provided that transmission facilities not be constructed when appropriate wheeling arrangements could be made. The intent of Secretary's principles and the Keating Amendment appear, in our opinion, to be reasonably congruent. Language similar to the Keating Amendment has been included in all subsequent appropriation acts for the Department of the Interior.

In September 1953, the Assistant Secretary for Water and Power approved criteria for use in negotiating future contracts for the sale of power in the Eastern Division, MRBP power marketing system. The Eastern Division power marketing system covers all or portions of Montana, North and South Dakota, Nebraska, Iowa, and Minnesota. Article 10 of these criteria provided that, for firm power sold under wheeling arrangements, the Bureau would absorb not more than 1 mill per kilowatt-hour (kwh) and associated losses (such as transmission losses) but that care would be taken to hold wheeling commitments to less than 1 mill where, because of short distance or other reasons, a lesser amount is adequate compensation.

The term "short distance" was not defined in the criteria, but a subsequent statement by a Department official, in response to a congressional inquiry, in connection with the Department's wheeling policy, noted that some customers had been required to construct approximately 15 miles of feeder lines or make their own wheeling arrangements. We noted one instance where a distance of 23 miles from a Bureau substation to a customer was considered by the Bureau as being too short a distance to warrant the Bureau's paying for wheeling service. Article 11 of the criteria provided that, in lieu of wheeling power over the transmission lines of G&Ts for service to member cooperatives, firm power could be sold directly to the G&Ts at a discounted rate.

According to the Bureau of Reclamation Instructions and article 11 of the marketing criteria, the discount in lieu of wheeling would be granted because of savings expected to be realized by the Bureau as a result of making direct delivery to the G&Ts. These savings were identified as including the cost of transmission either by wheeling or by transmission over Bureau lines, transmission losses, processing of contracts with individual members, reading of meters of such customers, accounting and billing such customers, and the like.

The discount to be allowed was to be in an amount equal to the savings per kwh made by the Bureau, but not in excess of the lesser of the G&Ts cost per kwh to service its customers or 1 mill per kwh of firm energy sold and delivered to the G&T. Also, whenever the amount of energy contracted for was increased or decreased the discount per kwh was to be redetermined.

In May 1955 the Assistant Secretary of the Interior stated, in response to a congressional inquiry, that, generally speaking, the Bureau would neither construct feeder lines to reach customers in close proximity to Bureau substations nor pay wheeling fees to reach such customers and that the rates in the MRBP had not been set up to cover such costs. He stated also that the Bureau was following a consistent policy on short-distance wheeling which it did not contemplate changing. The response from the Assistant Secretary does not mention the practice of granting discounts in lieu of wheeling to G&Ts.

The statement concerning the basis of the rate structure did not coincide with the criteria approved in September 1953 for the sale of power in the Eastern Division of the MRBP. The September 1953 criteria permitted the Bureau to pay wheeling costs for deliveries to customers located a short distance from a Bureau substation but required consideration of the short distance in determining whether a rate of less than 1 mill per kwh for such service would be adequate. The Department's statement in 1955, concerning its wheeling policy and the basis of the rate structure, generally does not permit payment by the Bureau for wheeling power to customers located a short distance from a Bureau substation.

FINDINGS AND RECOMMENDATIONS

DISCOUNTS GRANTED G&Ts INCONSISTENT WITH BASIS USED IN ESTABLISHING RATES

The Department has stated that the rate structure of the Eastern Division of the MRBP has not been set up to cover the cost of constructing Government-owned transmission facilities, or wheeling over the lines of third parties, for delivery of power to customers located within a short distance of a Bureau substation. Notwithstanding this statement, the Department has followed a policy of allowing G&Ts in the market area a discount in lieu of wheeling on all firm power deliveries although in certain instances some deliveries are for G&T members located a short distance from a Bureau substation.

Bureau customers other than members of a G&T located near a Bureau substation are required to build their own transmission facilities or make their own wheeling arrangements. This inconsistency in policies provides certain G&Ts and their members with price advantages not available to other Bureau customers located a short distance from a Bureau substation.

Our review showed that, during calendar year 1965, the latest year for which this information was available at the time of our review, the Bureau granted the nine G&Ts in the Eastern Division over $2.1 million in discounts in lieu of wheeling. We examined the discounts granted to two G&Ts and noted that about $300,000 of these allowances were granted on power deliveries to member customers whose distribution systems were in close proximity to the Bureau's substations.

The criteria for allowing discounts in lieu of wheeling stated that the discounts would be granted because of savings expected to be realized by the Bureau as the result of making direct delivery to the G&Ts. We compared the discounts in lieu of wheeling made to one of the G&Ts (East River), which received discounts of about $284,000 in calendar year 1965 for deliveries made to its members in close proximity to the Bureau's substations, with the costs that would have been incurred by the Bureau under the wheeling policy used in establishing its rates. We estimated that the discounts granted to East River in 1965 were about $176,000 more than what the Bureau's costs would have been under wheeling arrangements consistent with that used in establishing the rates.

The circumstances relating to granting discounts in lieu of wheeling to each of the two G&Ts are presented in the succeeding sections of this report.

East River Electric Power Cooperative

The Bureau has allowed discounts in lieu of wheeling on power delivered under its contract No. 14-06-600-1948 dated July 9, 1956, with the East River Electric Power Cooperative, Inc., a large G&T servicing an area located primarily in the eastern section of South Dakota. Under the terms of this contract which is to remain in effect until December 31, 1985, the Bureau agreed to deliver to East River for use of its 20 South Dakota member customers and one Minnesota member customer firm power up to a maximum coincidental demand of 62,300 kilowatts (the contract rate of delivery). On March 10, 1961, the contract rate of delivery was increased to 88,780 kilowatts. The power is delivered to East River from 13 Bureau substations located on a 115-KV transmission line loop constructed by the Bureau mainly for the purpose of serving customers in eastern South Dakota.

During calendar year 1965, discounts in lieu of wheeling amounting to about $435,000 were allowed to East River and about $284,000 of these discounts related to deliveries made to 11 of East River's member customers whose distribution systems were located from less than a mile to less than 15 miles from a Bureau substation. We used 15 miles as a cutoff because of the Department's statement (see p. 7) that other customers had been required to construct 15 miles of feeder lines or make their own wheeling arrangements.

The discounts under the contract have been granted because the Department and the Bureau in initially negotiating for the sale and wheeling of Federal power to member cooperatives of East River made decisions which deviated, in our opinion, from its policies governing wheeling and direct delivery. The conditions evolving from these decisions were further compounded when the Bureau subsequently entered into the 1956 contract for selling the power direct to East River and allowing discounts, although the Department had repeatedly reaffirmed its policy of not providing wheeling services to customers in close proximity to the Bureau's system. The circumstances covering these actions and decisions follow.

Prior to the issuance of the 1953 marketing criteria, the Bureau entered into contracts in 1951 and 1952 for the sale of power to the individual members of the East River Cooperative and for supplying the power by wheeling over the transmission facilities of East River. The initial wheeling contract with East River provided for payment of 1 mill per kwh for this service.

During negotiations in 1950 for the initial wheeling contract with East River, the Bureau's then Director of Power Utilization informed the Commissioner that he had advised representatives of East River and the Rural Electrification Administration (REA) that the Bureau would not pay for wheeling on deliveries to six members. The distribution systems of these six members are within 15 miles of a Bureau substation. He stated that this position was taken because the Secretary's wheeling policy would not permit obligating the Bureau to continue to pay wheeling charges when economy indicated lower costs to the Bureau could be obtained by direct service from the Bureau.

At this same time East River was negotiating with the REA for a loan to construct the transmission system necessary to serve its members. Correspondence in the files of the Bureau of Reclamation indicated that the REA was unwilling to make the loan to East River if the Bureau provided direct service to any of the individual member cooperatives.

According to the then Director of Power Utilization for the Bureau, the REA feared that the six member cooperatives would pull out of the G&T if direct service were provided and that this change would burden the remaining members with the repayment of the loan. The Bureau stated that it appeared that direct service by the Bureau to the six members would reduce East River's annual income from the Bureau for wheeling about 20 percent. This reduction was estimated to be about 12 percent of the total amount that would have to be repaid under the proposed REA loan. For these reasons the negotiations for the loan had reached a stalemate, and without the loan East River was in no position to contract with the Bureau to wheel power.

On December 14, 1950, the Commissioner of Reclamation recommended, for approval by the Secretary of the Interior, a contract with East River that provided for the payment by the Bureau of 1 mill per kwh for wheeling service to be provided by East River to its 21-member cooperatives. In the letter recommending approval, no mention was made of the Bureau's previous position that payment by the Bureau for wheeling service to six of the East River member cooperatives would be contrary to Department policy. The Assistant Secretary for Water and Power Development approved the proposed contracts for the Secretary, and, on December 18, 1950, the Bureau entered into a contract with East River for wheeling power to the 21-member cooperatives.

Under this contract East River was paid 1 mill per kwh for power delivered to East River for the account of its member customers and the Bureau absorbed transmission losses. The Bureau billed the individual members of East River on the basis of maximum monthly kilowatt demand at the member's substations.

In 1953 the Secretary issued marketing criteria to guide future contract negotiations for the disposal of federally generated power in the Eastern Division of the MRBP power marketing system. Article 11 of the criteria provided that, in lieu of wheeling firm power and energy over the transmission lines of public bodies and G&Ts for electric service to nonprofit cost-of-service customers or member cooperatives of such agencies, the Bureau may make arrangements with these agencies as contractors for direct delivery and sale of firm power and energy to them for resale to nonprofit cost-of-service customers or member cooperatives at a discounted rate.

The criteria provided that delivery be at the points of interconnection of the integrated transmission systems of the contractor and the Bureau and that the responsibility of the Bureau not extend beyond such points of delivery. The criteria provided also that--in view of the savings made by the Bureau under such arrangements (such savings included the cost of transmission either by wheeling or by transmission over Bureau lines, transmission losses, processing of individual power contracts with cost-of-service customers or member cooperatives, reading of meters of such customers over rather large areas, accounting and billing such customers, and the like)--the contractor be afforded a discount in an amount equal to the savings per kwh made by the Bureau, but not in excess of the lesser of the contractor's service cost per kwh or 1 mill per kwh of firm energy sold and delivered to the contractor. The amount of the discount will be redetermined whenever the contract rate of delivery is increased or decreased.

In March 1954 the Assistant Secretary of the Interior informed East River that the Bureau was ready to negotiate a contract for the sale of power direct to East River which would include the discount in lieu of wheeling. In April 1954 after a conference with the Assistant Secretary, East River, and representatives of the Bureau, the Commissioner of Reclamation advised East River of the terms of a tentative agreement regarding application of a single contract rate of delivery and stated that power and energy sold to East River would be metered at the points of interconnection, with billing demand on a maximum coincidental demand basis (the highest demand in kilowatts delivered coincidently from various delivery points during a specified period of time).

In May 1954, East River, however, advised the Commissioner that it believed it had more to lose than to gain under the proposed arrangement and elected to continue under the wheeling contract. East River's response did not state why it believed the wheeling contract was more advantageous.

In November 1954 the Regional Director of Region 6 requested instructions from the Commissioner on wheeling versus direct delivery when the customer was located in close proximity to the Bureau's substation. The Acting Assistant Commissioner responded that, in line with previously established principles, a customer would normally be required to construct a transmission line to a Bureau substation for service when the short distance to the customer's system would make the regular wheeling fee out of proportion to the service rendered.

In 1955 the Assistant Secretary--in response to a congressional inquiry concerning a customer, located about 4 miles from a Bureau substation, that was required to pay wheeling costs--further defined the short distance wheeling policy as follows:

> "*** Generally speaking, the Bureau has not and does not propose to construct feeder lines from its substations to the customers in the vicinity of such substations nor does it propose to pay wheeling fees to reach such customers. *** The Bureau's rate structure in the Missouri River Basin area has not been set up to cover such costs."

He also stated that there had been other cases where customers had been required to construct approximately 15 miles of feeder lines or to make their own wheeling arrangements and that the Bureau was following a consistent policy on this short-distance wheeling that it did not contemplate changing.

In December 1955 the Assistant Commissioner and Chief Engineer (AC&CE) informed the Commissioner of the growing concern with regard to the inability of the Bureau to realize revenues required to achieve eventual payout of the Missouri River Basin Project. The letter pointed out that it was becoming evident that with the special provisions of different contracts, including wheeling allowances and special discounts, the average return of 5.5 mills per kwh, which it was assumed was needed to repay the Government's investment, would not be obtained.

The AC&CE specifically referred to the proposed East River contract and the new stipulations introduced that would reduce revenues. He stated that combining all deliveries and billing the sum of the maximum coincidental demands of all of East River's member cooperatives reduced the billing because previously the billing had been based on the maximum demands of the individual member cooperatives. He also pointed out that the proposed contract made East River the direct customer of the Bureau and allowed a 1-mill discount for each kwh sold, a special discount equal to the previous wheeling charge, although wheeling would no longer be involved. The AC&CE stated that he doubted that the savings to the Bureau referred to in the contract could offset the reduction in billings resulting from the proposed revisions.

In May 1956 the Acting Assistant Commissioner of Reclamation informed the directors of Regions 6 and 7 that, during discussions within the Department of the Interior, the question was raised as to whether the United States gained net revenue for service rendered under the provisions of article 11 of the marketing criteria compared with direct sales to cost of service (nonprofit) customers or member cooperatives by wheeling and requested an accurate study on this matter.

Three important items to be considered were identified as transmission losses which would be gained by the United States, either actual or stated by a wheeling contract; diversity lost; and metering, in the broad sense, which includes interest and amortization, operation and maintenance, reading meters, and cost of billings. However, the request for a decision was canceled the following month, apparently due to East River's acceptance of a proposed new contract in June 1956.

Contract No. 14-06-600-1948 with East River, dated July 9, 1956, provided for direct delivery of power at substations of the United States and billing of East River on the basis of the noncoincidental demands and energy readings, increased 2 percent for transformer losses on the low-voltage side of substations, at the points where East River delivered to the member cooperatives until such time as additional metering equipment was installed. The contract provided also that, after the additional metering equipment was installed at the Bureau substations, deliveries would be billed at the highest amount of the maximum coincidental demands.

This latter provision imparted to East River the benefits of diversity derived from such factors as shifting of load demands between multiple points of interconnection on the Bureau's transmission loop serving the individual members and being charged on the basis of coincidental maximum demands rather than the amount of the individual maximum demands which would have otherwise been charged by the Bureau.

The monetary value of these benefits will vary according to the load patterns of the customers and the characteristics of the system used in receiving and delivering the power obtained from the Bureau.

The effect of the 1956 contract providing for a discount in lieu of wheeling on the deliveries to East River, compared with having East River serve as the Bureau's wheeling agent for those of its members whose distribution systems are beyond 15 miles from a Bureau substation and requiring the remaining members to make their own arrangements for receiving Bureau's power, is shown in the following schedule.

Discounts in lieu of wheeling granted on deliveries to East River for its 21 members		$434,600
Less wheeling costs applicable to those members beyond 15 miles		150,700
Discounts allowed on power furnished 11 members in close proximity to Bureau substations		283,900
Revenue lost through billing deliveries to East River rather than billing deliveries to individual members (diversity)		15,400
Revenue lost before reduction for Bureau savings		299,300
Less Bureau savings:		
Estimated additional costs to Bureau to serve the 21 members separately	$66,500[a]	
Value of 7 percent transmission losses which would have been absorbed by Bureau under wheeling arrangements for members beyond 15 miles	56,600	123,100
Estimated Bureau loss for calendar year 1965		$176,200

[a]Includes costs for marketing, metering, accounting, collecting, and administration and general expense.

The amount of discount shown above was determined by using the deliveries made to East River for its members during the 1965 calendar year period--the most recent period available at the time of our fieldwork. The amounts computed for the various elements were based on the procedures generally followed by the Bureau under wheeling conditions, and regional office personnel generally concurred in the basis for our assumptions and estimates.

We believe the above comparison shows that the 1956 contract with East River has resulted in substantially less revenue than an agreement that would have been consistent with the criteria used in establishing the rate structure for the Eastern Division of the MRBP. This condition has continued and will persist until the contract expires or is revised. The 1956 contract with East River provides also that the 1 mill per kwh discount in lieu of wheeling is subject to redetermination if the contract rate of delivery is increased. The contract rate of delivery has been increased several times since 1956 but no redetermination of the discount has been made.

In our opinion, the Department's policy on allowing discounts in lieu of wheeling power to members of a G&T is not consistent with the basis on which the power rates were established or its policy for wheeling power to customers other than G&Ts.

As noted on page 12, discounts are granted to a G&T because of the presumed savings in transmission or wheeling costs, as well as administrative and other costs which would be incurred by the Bureau if delivery was made to the member cooperatives by wheeling or over Bureau transmission lines. By allowing a discount to East River on all energy delivered, however, the Bureau is in effect paying a wheeling charge for deliveries made to those members in close proximity to Bureau substations, who would not be eligible for such service at Bureau expense if they were not members of a G&T.

This situation is directly contrary to the Department's 1954 and 1955 statements relative to wheeling short distances and results in price advantages to the G&Ts and their members which are not available to Bureau customers in close proximity to a Bureau substation who are not members of a G&T.

Corn Belt Power Cooperative

Another situation where, in our opinion, the discount in lieu of wheeling has been allowed to a G&T, under conditions which were inconsistent with the wheeling policy as it is applied to Bureau customers other than G&Ts, involves the Glidden Rural Electric Cooperative. This cooperative, located in Iowa, was seeking a power delivery from the Bureau. The Bureau personnel proposed that Glidden build a line into the Bureau's Denison substation. Glidden indicated that it would accept this proposal. However, Corn Belt Power Cooperative, a G&T also located in Iowa, subsequently indicated its desire to construct 23 miles of transmission line into the Denison substation to service both Corn Belt and Glidden.

In February 1960, the Regional Director, Region 6, informed the Commissioner that this arrangement raised the following questions: (1) would the Bureau pay Corn Belt for wheeling power to Glidden and (2) if Glidden became a member of the G&T, would the Bureau allow Corn Belt a discount in lieu of wheeling for Glidden's portion of the load?

The Assistant Commissioner replied in April 1960 that:

> "Since a distance of only 23 miles is involved between the Bureau of Reclamation's facilities and the Glidden system, we probably could substantiate that Glidden should take direct service from the Bureau of Reclamation's facilities. We consider that your condition (1) approaches a situation of subterfuge."

The Assistant Commissioner of the Bureau of Reclamation further stated that, should Glidden become a member of the Corn Belt G&T, Corn Belt could receive a discount in lieu of wheeling. Subsequently, Glidden joined the G&T, and the Bureau had granted discounts to Corn Belt of about $17,000 annually on the firm power it had purchased for Glidden.

The discount of about $17,000 granted to Corn Belt on deliveries to Glidden is intended to cover Bureau savings in transmission or wheeling costs, as well as certain administrative and other costs that would have been incurred by the

Bureau if the power had been wheeled to Glidden or transmitted over Bureau lines. We did not determine the costs which would have been incurred by the Bureau if Glidden had been required to take direct delivery from Bureau facilities.

Agency comments and our conclusions

In a letter dated October 26, 1967 (see app. II), the Director of Survey and Review, commenting for the Department on our draft report, advised us that in 1954 the then Assistant Secretary for Water and Power pronounced the policy that the generating and transmission cooperatives were in the same position as wheeling agents and therefore were entitled to a discount in lieu of wheeling. According to the Director, the Bureau relied on this policy in entering into long-term contracts with G&Ts wherein the discounts in lieu of wheeling were embodied.

The Director stated that the policy did not require a case-by-case determination whether a G&T had existing facilities within any particular distance from Federal facilities. In applying the reference in article 10 of the Bureau's marketing criteria to short distance considerations, the Director stated that the Bureau had proceeded on the basis that a wheeling agent was offering total system facilities for a combination of delivery distances. According to the Director, it was not considered fair or necessary to divide the facilities available for wheeling into segments according to distance and that the G&Ts have been treated precisely as the private utilities in this respect.

With regard to the amount of the discounts allowed G&Ts in lieu of wheeling, the Director stated that the contracts by which the Department was bound provided that, if average wheeling costs were less than 1 mill, the lower cost would apply. He stated that the Department had no objection to making a cost finding of this type.

According to the Director, queries have been made by the Department from time to time regarding the relationship of wheeling costs to the 1-mill factor and the answers indicate a higher cost than 1 mill. However, in a subsequent discussion, the Assistant Director of Survey and Review informed us that the Department did not have any documentation to support the answers to its queries that wheeling costs may be higher than 1 mill. The Director stated that the Department would request the Bureau to develop up-to-date information on this point.

We do not agree that the G&Ts are treated the same as private utilities. The Bureau allows a discount in lieu of wheeling to G&Ts for power deliveries to member cooperatives who are customers of a G&T; it does not allow a discount in lieu of wheeling to private utilities nor pay for the wheeling of power to customers of the private utility.

Our draft report did not question the Department's policy of recognizing G&Ts, as well as private utilities, as wheeling agents, and we agree that the discounts being granted to East River for delivery to some of its members are in accord with the Department's statements as to the wheeling policy used in establishing the rates. However, it is our opinion that payment of wheeling fees, or allowing discounts in lieu thereof, for deliveries to those members whose systems are in close proximity to a Bureau substation is contrary to Department statements as to the basis used in establishing the power rates and is not consistent with the Bureau's wheeling policy as applied to customers who are not members of a G&T.

Also, the Department's comment that it did not consider it fair or necessary to divide the facilities available for wheeling into segments according to distance is, in our opinion, not germane to a situation such as that noted in connection with the discounts granted on power deliveries to the Glidden cooperative. In that instance an individual cooperative that was not a member of a G&T and which under Bureau policy would not have been eligible for wheeling at Bureau expense because of its location near a Bureau substation is, in effect, receiving a discount in lieu of wheeling merely because it subsequently joined a G&T.

We therefore believe that, consistent with the basis used in the establishment of the rate structure for the Eastern Division of the MRBP, the discount allowance should not have been applied to the total energy deliveries to the G&Ts but to only that portion of energy deliveries related to member customers that could qualify for wheeling if they were not members of a G&T. Consistent with these criteria, we believe that the cost-finding study proposed by the Department should compare the cost that would be incurred by the Bureau in transmitting power to member customers who qualify for wheeling services because of their distance from a Bureau substation with the cost to the G&T of providing this service to the same customers.

The discount in lieu of wheeling allowed to the G&Ts should, in our opinion, be the lower of the above costs but not in excess of the maximum allowance of 1 mill per kwh of energy delivered to the customers who qualify for wheeling services. We believe that the cost-finding study should also compare the effect on net revenues of the Bureau of the present contracts with the G&Ts as opposed to estimates of the Bureau's cost of constructing and operating its own transmission lines to provide direct service to individual members of the G&Ts which would be eligible for such service at Bureau expense if they were not members of a G&T. Factors to be considered in the comparison should include transmission losses, diversity, and operating and administrative costs.

In our view, discounts in lieu of wheeling allowed by the Bureau should be consistent with the departmental policies used in establishing the rate structure and applied consistently to all customers in the MRB area. This policy, as outlined in 1955, would prohibit the payment of wheeling fees or discounts for transmitting power short distances. Consistent with this policy, it would be the responsibility of such customers, whether members of a G&T or direct customers of the Bureau, to construct feeder lines to Bureau substations or pay for the wheeling of power by a third party.

Recommendations

We recommend that the Secretary of the Interior direct the Bureau to reexamine, in connection with future contracts or contract amendments with G&Ts, discounts granted in lieu of wheeling power short distances and that such discounts be limited to those deliveries which conform to the wheeling policy on which power rates were established.

We recommend also that the cost-finding study, which the Department proposes to have the Bureau make on the relationship of wheeling costs to the discounts being granted, be based on the wheeling policy on which the power rates were established and that consideration be given to all alternatives including estimates of the Bureau's cost of constructing and operating its own transmission lines to provide direct service to individual members of the generating and transmission cooperatives which are eligible for such service at Bureau expense.

APPENDIXES

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PRINCIPAL OFFICIALS OF THE DEPARTMENT OF THE INTERIOR AND THE BUREAU OF RECLAMATION RESPONSIBLE FOR THE ACTIVITIES DISCUSSED IN THIS REPORT

	Tenure of office	
	From	To
DEPARTMENT OF THE INTERIOR		
SECRETARY OF THE INTERIOR:		
Oscar L. Chapman	Dec. 1949	Jan. 1953
Douglas McKay	Jan. 1953	Apr. 1956
Fred A. Seaton	June 1956	Jan. 1961
Stewart L. Udall	Jan. 1961	Present
ASSISTANT SECRETARY, WATER AND POWER DEVELOPMENT:		
William E. Warne	July 1947	Nov. 1951
Robert M. McKinney	July 1952	Dec. 1952
Fred G. Aandahl	Feb. 1953	Jan. 1961
Kenneth Holum	Jan. 1961	Present
COMMISSIONER, BUREAU OF RECLAMATION:		
Michael W. Straus	Dec. 1945	Feb. 1953
Wilbur A. Dexheimer	July 1953	Apr. 1959
Floyd E. Dominy	May 1959	Present

UNITED STATES
DEPARTMENT OF THE INTERIOR
OFFICE OF THE SECRETARY
WASHINGTON, D.C. 20240

OCT 26 1967

Mr. James T. Hall, Jr.
Associate Director, Civil Division
General Accounting Office
Washington, D. C. 20548

Dear Mr. Hall:

This letter conveys Departmental views concerning your draft report entitled "Review of Discounts in Lieu of Wheeling Granted Generating and Transmission Cooperatives in the Eastern Division of the Missouri River Basin Project--Bureau of Reclamation."

The essence of the recommendations in this report is that discounts in lieu of wheeling to generating and transmission cooperatives should be reexamined as being at variance with governing policies and that future contracts should conform to the "stated wheeling policy." In 1954 the Department, through the then Assistant Secretary for Water and Power, pronounced the policy that the generating and transmission cooperatives were in the same position as a wheeling agent and therefore entitled to a discount in lieu of wheeling. In reliance upon this policy the Bureau of Reclamation entered long term contracts with G&T's wherein the discount in lieu of wheeling was embodied. The cited policy remains viable.

We do not feel that the policy requires a case by case determination whether a G&T has existing facilities within any particular distance from Federal facilities. In applying the reference in Article 10 of the Marketing Criteria to "short distance" considerations, the Bureau has proceeded on the basis that a wheeling agent was offering total system facilities for a combination of delivery distances. It was not considered fair or necessary to divide the facilities available for wheeling into segments according to distance. If, on the other hand, the agent offered <u>only</u> short distance accommodation, the wheeling compensation must be adjusted. The G&T's have been treated precisely as the private utilities in this respect.

Your report makes a further point regarding the relationship of wheeling costs to the one mill factor. The contracts by which we are bound provide that if average wheeling costs are less than one mill the lower cost will apply. The Department has no objection to making a cost finding of this type. From time to time queries have been made regarding this cost relationship and the answers indicate a higher cost than one mill. The Department will request the Bureau to develop up-to-date information on this point.

Sincerely yours,

D. Darlington Denit

Director of Survey and Review