Witness CCS - 1
Exhibit CCS-1

BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

In the Matter of the Application of PacifiCorp for Approval of its Proposed Electric Rate Schedules and Electric Service Regulations	))))))	Docket No. 01-035-01 PRE-FILED DIRECT TESTIMONY OF HUGH LARKIN, JR. FOR THE COMMITTEE OF CONSUMER SERVICES

June 4, 2001

Non-Confidential

TABLE OF CONTENTS

INTRODUCTION 1

OVERVIEW 2

DAVE JOHNSTON (GLENROCK) MINE CLOSURE 7

SYSTEMS APPLICATIONS AND PRODUCTS SOFTWARE (SAP) 14

RE-ENGINEERING 18

1997 COMPUTER SOFTWARE WRITE-DOWN 21

COMPANY’S PROPOSED 1999 SOFTWARE WRITE-OFF 22

UNCOLLECTIBLE EXPENSE 24

POTENTIAL UPDATES 26

1 INTRODUCTION

2 **Q. WHAT IS YOUR NAME, OCCUPATION AND BUSINESS ADDRESS?**

3 A. My name is Hugh Larkin, Jr., I am a Certified Public Accountant licensed in the
4 States of Michigan and Florida and the senior partner in the firm of Larkin &
5 Associates PLLC, Certified Public Accountants, with offices at 15728 Farmington
6 Road, Livonia, Michigan 48154.

7 **Q. PLEASE DESCRIBE THE FIRM LARKIN & ASSOCIATES.**

8 A. Larkin & Associates PLLC, is a Certified Public Accounting and Regulatory
9 Consulting firm. The firm performs independent regulatory consulting primarily
10 for public service/utility commission staffs and consumer interest groups (public
11 counsels, public advocates, consumer counsels, attorneys general, etc.). Larkin
12 & Associates PLLC, has extensive experience in the utility regulatory field as
13 expert witnesses in more than 400 regulatory proceedings including numerous
14 water and sewer, gas, electric and telephone utility cases.

15 **Q. HAVE YOU PREPARED AN APPENDIX WHICH DESCRIBES YOUR**
16 **QUALIFICATIONS AND EXPERIENCE?**

17 A. Yes. I have attached Appendix I, which is a summary of my experience and
18 qualifications.

19 **Q. BY WHOM WERE YOU RETAINED, AND WHAT IS THE PURPOSE OF YOUR**
20 **TESTIMONY?**

21 A. Larkin & Associates PLLC, was retained by the Committee of Consumer
22 Services (CCS or Committee) to analyze PacifiCorp's (Company) rate case filing
23 for the test year ending September 30, 2000, and to make recommendations to
24 the Utah Public Service Commission (Commission) based on that analysis.

25 I present the Committee's overall revenue requirement recommendations based
26 on the analysis of Larkin & Associates PLLC and other consultants retained by

1 the Committee. These recommendations are based on an analysis of the test
2 year ended September 30, 2000, which we have been able to complete as of
3 this date. I will discuss problems we have encountered in our analysis under the
4 overview section of my testimony.

5 **Q. PLEASE DISCUSS WHICH ISSUES WILL BE SPONSORED BY YOUR FIRM**
6 **AND THOSE TO BE SPONSORED BY OTHER COMMITTEE CONSULTANTS.**
7 A. The summary of the Committee's overall recommendation is shown on CCS
8 Exhibit 1.1, page 1 of 3. The exhibit is a summary of rate base and operating
9 income adjustments which are shown on CCS Exhibit 1.1, page 2 and 3 of 3. On
10 CCS Exhibit 1.1, page 2 of 3, each rate base adjustment is shown with the
11 particular witness responsible for that rate base adjustment identified in the
12 column under the heading of consultant. On CCS Exhibit 1.1, page 3 of 3, the
13 adjustments to operating revenue, operating and maintenance expenses,
14 depreciation and amortization, and taxes are shown. Again, next to each
15 adjustment, the witness responsible for that adjustment is identified. Each
16 witness' testimony will discuss the adjustment they sponsor and identify why the
17 adjustment is appropriate for establishing rates for PacifiCorp's Utah operations.

18 CCS Exhibit 1.1, on page 1 of 3, indicates that rates should be decreased by
19 $38,530,633.

20 OVERVIEW
21 **Q. WOULD YOU PLEASE DESCRIBE PACIFICORP'S FILING AND THE**
22 **LIKELIHOOD THAT THE TEST YEAR IS REPRESENTATIVE OF COSTS**
23 **WHICH MIGHT BE REFLECTIVE OF FUTURE PERIODS?**
24 A. PacifiCorp's Utah filing is actually the amalgamation of two different accounting
25 periods and three different budget procedures. The test year, which
26 encompasses the period October 1, 1999, through September 30, 2000, is
27 comprised of three different budgeting approaches. First, the period October 1,

1 1999, through December 31, 1999, was budgeted in late 1998 under the
2 management of the former chairman, Mr. Fred Buckman. Mr. Buckman was
3 replaced in late 1998 by Mr. Keith McKennon, who incorporated additional cost
4 savings into the 1999 budget and was responsible for the operation of the
5 Company and its budget for the year 2000. Mr. McKennon was subsequently
6 replaced by Mr. Alan Richardson. In June 2000, the Company engaged in a "re-
7 budget" exercise to revise the budget for submission to ScottishPower.
8 Consequently, the test year is comprised of operations under three different chief
9 executives and at least three different budgeting processes. There is no
10 apparent consistency between these three periods since they were neither
11 budgeted, nor managed by the same management team.

12 **Q. WOULD THAT MAKE A DIFFERENCE?**
13 A. Yes. Obviously, the management was changed and budgets revised because
14 the results of operations were not to the liking of the new owners of PacifiCorp.
15 There is not a consistent 12-month period where the current management
16 prepared the budget and was responsible for its implementation.

17 **Q. DID YOU ATTEMPT TO COMPARE BUDGETED DATA FOR THIS PERIOD**
18 **WITH THE ACTUAL RESULTS AND THE EXPLANATION BY MANAGEMENT**
19 **OF THE VARIANCES?**
20 A. Yes. We requested budget to actual comparisons with management's
21 explanations of any variances. We were informed by the Company, that while it
22 prepares budget to actual comparisons, and executives and business unit
23 managers have to explain variances, no documentation is maintained which
24 explains or accounts for specific variances. We were informed that only
25 variances at a "high level" are provided to the officers of the Company. The only
26 budget variances mentioned in management reports to the Board of Directors
27 were bad debt provisions, tree trimming and demand-side resources'
28 amortization expense.

1 **Q. IN YOUR 31 YEARS OF EXPERIENCE EXAMINING TEST-YEAR DATA, HAVE**
2 **YOU EVER ENCOUNTERED A SITUATION WHERE A COMPANY THE SIZE**
3 **OF PACIFICORP DID NOT KEEP OR MAINTAIN BUDGET TO ACTUAL**
4 **COMPARISONS WITH DETAILED EXPLANATIONS?**
5 A. No, I have not. If, in fact, PacifiCorp is not managed in a manner which requires
6 officers, managers and supervisors to maintain explanations of variances from
7 budgets, then effectively there can be no cost control being exercised by the
8 management of this Company. It is necessary to maintain explanations of
9 budget to actual comparisons, both on a monthly basis and on a yearly basis in
10 order to understand fluctuations in cost from those budgeted and to be able to
11 prepare accurate budgets for future periods. If, in fact, PacifiCorp does not
12 prepare monthly actual to budget comparisons with detailed explanations of
13 variances, then this is an indication of a serious management problem. If, in
14 fact, they are prepared, then that documentation should have been provided
15 when requested. The fact that it has not been provided has significantly
16 impeded our analysis of the Company's filing.

17 **Q. ARE THERE OTHER DOCUMENTS WHICH WERE NOT PROVIDED BY THE**
18 **COMPANY WHICH YOU REQUESTED AND WHICH, IN YOUR OPINION,**
19 **EXIST?**
20 A. During our visit to the Company's office in Portland, Oregon, we reviewed the
21 Executive Committee Meeting Minutes of the Board of Directors. We were
22 unable to locate minutes for the months of February, April, May and June, 2000.
23 We requested that the Company provide these minutes. The Company's
24 response was:

25 The Executive Committee of the Board of Directors does not meet if the
26 PacifiCorp Board of Directors meets. For the dates indicated above, there
27 was a PacifiCorp Board of Directors meeting. Therefore, since the
28 Executive Committee did not meet there are no minutes to review.

1 We found specific references in the Executive Committee minutes for the month
2 of March 2000, which refer to the approval of the minutes of the February 16,
3 2000 meeting. In addition, the July 2000 minutes refer to the approval of the
4 June 22, 2000 minutes. In discussing this matter with the Company, it still
5 contends that the Executive Committee of the Board of Directors did not meet on
6 the dates indicated in the minutes we examined.

7 **Q. DOES THE FILING ITSELF PROVIDE EXPLANATIONS, WORKPAPERS AND**
8 **OTHER SUPPORTING DOCUMENTS WHICH FULLY EXPLAIN HOW THE**
9 **COMPANY'S PROPOSED ADJUSTMENTS WERE ARRIVED AT?**
10 A. No, it does not. The filing is essentially a minimal filing. It provides little detail of
11 how certain numbers were arrived at and generally lacks supporting documents
12 for the underlying data. In fact, we have noted a number of errors in the filing
13 which were substantial in nature. For example, the Utah jurisdiction was
14 allocated $7.7 million more than appropriate due to location center errors in the
15 Company's system. The Company removed the Business System Integration
16 Project (BSIP) amortization costs in an adjustment that was not recorded on the
17 books to begin with. It also reversed costs in a "Costs Triggered by Merger"
18 adjustment that had already been reversed on its books in the test year.
19 Additionally, PacifiCorp failed to allocate 100% of a Utah-specific industrial
20 revenue normalization adjustment to Utah in its filing. This resulted in a $1.9
21 million understatement of revenues. These are just a few examples of errors in
22 the Company's filing. These errors, and others, are discussed at length in my
23 testimony and the testimonies of Committee witnesses Helmuth Schultz and
24 Donna DeRonne.

25 **Q. WHEN YOU SUBMITTED OR ASKED FOR DOCUMENTS SUPPORTING THE**
26 **FILING, DID THE COMPANY PROVIDE RESPONSES WITHIN THE 21-DAY**
27 **TIME PERIOD SET IN THIS CASE?**
28 A. I have included as CCS Exhibit 1.2 a schedule identifying the date that the data

1 request was received by the Company and the actual date that the response was
2 provided. The exhibit shows that a large number of responses were late.
3 Certain responses were significantly late and we are still waiting for responses to
4 particular data requests. This greatly impeded our investigation and our ability to
5 file complete and comprehensive testimony on the filing date of June 4, 2001.

6 **Q. WERE THE RESPONSES, ONCE RECEIVED, COMPLETE AND DETAILED**
7 **ENOUGH TO COMPLETE YOUR ANALYSIS?**
8 A. In many instances they were not and required additional data requests in order
9 to completely understand and analyze the issue. This added to the length of
10 time to examine certain issues.

11 **Q. HAS THE COMPANY PROVIDED THE SAME LEVEL OF DETAIL AS IT HAS**
12 **IN THE PAST?**
13 A. No, it has not. CCS Exhibit 1.3, pages 1 and 2, is the Table of Contents for the
14 monthly financial statements for December 1998 and September 2000. The
15 Company's September 2000 monthly report does not include information on coal
16 mining, fuel consumed or construction. This information was available in the
17 December 1998 monthly report.

18 **Q. IS IT POSSIBLE THE COMPANY NO LONGER PREPARES THIS TYPE OF**
19 **INFORMATION?**
20 A. I do not believe so. In my opinion, there appears to be an effort on the part of
21 the Company to limit the amount of original documentation which it includes in its
22 monthly operation and management reports. This impedes the speed with which
23 we can analyze the reasonableness of the Company's proposed adjustments
24 and information relating to the test year.

25 **Q. ARE THE TESTIMONIES BEING FILED ON THIS DATE, AND THE**
26 **ADJUSTMENTS BEING PROPOSED, THE COMMITTEE OF CONSUMER**

1 **SERVICE'S FINAL POSITION?**
2 A. No, it is not. There are a number of issues which we are still reviewing for a
3 possible adjustment. There are additional issues on which we are currently filing
4 testimony that may require further analysis. Therefore, the present filing should
5 be considered our best effort based on the information and responses provided
6 by the Company to date. At the end of my testimony, I delineate issues that we
7 are still investigating.

8 DAVE JOHNSTON (GLENROCK) MINE CLOSURE

9 **Q. DO YOU AGREE WITH THE COMPANY'S ADJUSTMENT REGARDING THE**
10 **DAVE JOHNSTON (GLENROCK) MINE CLOSURE?**
11 A. I agree that mining of coal from the Dave Johnston Mine appears to have ceased
12 on October 9, 1999. That date falls within the test year and I believe it is
13 appropriate to recognize some costs which the Company can actually
14 substantiate are losses that will not be recovered as a result of closing the mine.
15 However, it is not clear to me that the Company has actually taken an
16 abandonment loss on its tax return for the Dave Johnston Mine. Many of the
17 assets are still in use at the mine for reclamation purposes and have not been
18 sold or abandoned.

19 **Q. IS THAT WHAT THE COMPANY REFLECTED IN ITS ADJUSTMENT?**
20 A. No, it is not. What the Company reflected in its adjustment is an estimated loss
21 which it booked in December 1997. These were estimates of what might occur
22 when the mine was actually closed almost two years later. The Company has
23 not provided any updated information in its filing which substantiates any of the
24 estimates or losses. In addition, I do not feel that the use of a five-year
25 amortization of any cost that might be recognized is appropriate; nor does it
26 follow past Commission precedent.

27 **Q. WHY DO YOU FEEL THAT A FIVE-YEAR AMORTIZATION WOULD NOT**

1 **FOLLOW PAST COMMISSION PRECEDENT?**
2 A. My understanding is that one of the criteria the Commission applies in
3 determining an amortization period is whether the amortization of the cost would
4 roughly match the benefit received as a result of the cost being incurred.

5 **Q. WOULD THAT MATCHING OCCUR UNDER PACIFICORP'S PROPOSED**
6 **AMORTIZATION OF THE GLENROCK MINE CLOSURE AND OTHER COSTS**
7 **THE COMPANY WOULD INCUR ASSOCIATED WITH THE SWITCHING OF**
8 **COAL SOURCES FOR THE DAVE JOHNSTON PLANT?**
9 A. No, it would not. On CCS Exhibit 1.4.1, I have shown the savings associated
10 with switching the source of fuel from the Dave Johnston Mine to purchases from
11 suppliers in the Powder River Basin. On that schedule, I have shown the annual
12 savings as testified to in prior cases by the Company associated with switching
13 the coal source. That savings, according to Company documents, is an annual
14 fuel savings of approximately $15 million. This fuel savings will appear in the
15 form of reduced fuel costs included in base rates in this case. As offsets to that
16 fuel savings, I have shown the costs which the Company has requested to
17 include in this rate case, which are a direct result of switching coal sources from
18 the Dave Johnston Mine to the Powder River Basin. On line three of CCS
19 Exhibit 1.4.1, I have shown the amortization costs requested by the Company on
20 a total Company basis. On line four, I have shown the return required on the
21 rate base amount which the Company has included in its rate filing associated
22 with the Dave Johnston Mine abandonment costs. The rate of return is the
23 Company's requested rate of return in this case grossed-up for income tax
24 effects on preferred stocks and common equity. On line five of this same exhibit,
25 I have shown my estimate of costs associated with the new coal offloading
26 facility necessary to offload coal supplied from the Powder River Basin. These
27 costs are comprised of a return on plant associated with the investment,
28 depreciation expense, and estimated operating and maintenance expenses and
29 property taxes.

1 In total, the rate case includes approximately $20 million of costs including the
2 Company's proposed amortization of mine closure costs. As can be seen from
3 this exhibit, ratepayers would not receive any reduction in cost associated with
4 this mine closure, because the cost included in the rate case exceeds the benefit
5 by approximately $5 million. This, of course, is on a total Company basis, and
6 Utah ratepayers would bear approximately 37% of the $5 million loss. The
7 reason for the mine closure and the switch to another fuel source was to
8 implement a cost savings program. However, when the amortization of the
9 closure costs are compressed into a five-year period, ratepayers will not receive
10 any benefits in rates because the costs exceeds the benefits from the mine
11 closure. Unless the Commission extends the amortization period no benefit will
12 be reflected in rates for this mine closure. In fact, a detriment would occur.

13 **Q. WOULD YOU PLEASE EXPLAIN WHAT ADJUSTMENTS YOU FEEL ARE**
14 **APPROPRIATE TO THE COMPANY'S PROPOSED WRITE-OFF?**
15 A. On Exhibit CCS1.4, I have shown the total Company costs which PacifiCorp has
16 included in its exhibits for recovery. On the schedule I have shown the net
17 investment, which was written off by the Company in December 1997.

18 This amount included all the equipment and facilities which were located at the
19 Dave Johnston Mine including equipment currently being used for reclamation.
20 The Company estimated future depreciation to be recovered through coal-cost
21 charges through June 1999. This estimated future depreciation was deducted
22 from the net book value of mine costs at December 31, 1997.

23 **Q. DID THE COMPANY ACTUALLY STOP RECOVERING DEPRECIATION**
24 **EXPENSE WHEN RATES WERE ESTABLISHED USING THE 1997 TEST**
25 **YEAR?**
26 A. No, there was no adjustment to depreciation expense to exclude the Dave

1 Johnston Mine depreciation expense. The Company continued to recover that
2 expense through 1998 and 1999.

3 **Q. DID THE COMPANY RECORD DEPRECIATION EXPENSE PAST JUNE 1999?**
4 A. Yes, it did. PacifiCorp continued to record depreciation expense through
5 October 1999. This is four months more of depreciation expense and
6 depreciation reserve than was actually deducted from the Dave Johnston Mine
7 cost in 1997.

8 **Q. HAVE YOU ADJUSTED THE COST THAT THE COMPANY IS ATTEMPTING**
9 **TO RECOVER FOR THIS ADDITIONAL FOUR MONTHS OF DEPRECIATION?**
10 A. Yes, I have. Since that depreciation expense was recorded as fuel costs and
11 charged against fuel expense, the Company would recover this amount twice if it
12 is not deducted from the total Company amount. On CCS Exhibit 1.4, in the
13 column labeled Adjustments, I have deducted $849,600 from the balance which
14 the Company has reflected in its cost related to the net investment in the Dave
15 Johnston Mine.

16 **Q. REGARDING THAT SAME SCHEDULE, PLEASE EXPLAIN WHY YOU HAVE**
17 **NOT INCLUDED ANY MATERIALS AND SUPPLIES FOR COST RECOVERY.**
18 A. There has been no showing, on the part of the Company, that there were
19 actually any materials and supplies that were not recovered in charges to fuel
20 expense during the period 1998 through October 1999, or that the materials and
21 supplies are not currently being used by the equipment which is involved in the
22 reclamation at the Dave Johnston Mine. The Company has expensed and
23 charged $9,044,318 of materials and supplies to the Dave Johnston Mine from
24 January 1998 through December 1999.

25 **Q. DID THE COMPANY MAKE A LISTING OF OBSOLETE, OR UNUSABLE**
26 **MATERIAL, WHEN IT WROTE OFF MATERIALS AND SUPPLIES IN**

1 **DECEMBER 1997?**
2 A. No, it did not. What the Company did in its adjustment to write off materials and
3 supplies was to assume that only $1.5 million of the inventory at December 31,
4 1997, would be consumed or salvageable at January 1, 1999.

5 **Q. WHY DID THE COMPANY USE THE DATE OF JANUARY 1, 1999?**
6 A. I do not know since it depreciated the plant assets through June 1999. We know
7 that the mine continued to operate through October 1999, so even if one could
8 rely on the Company's estimate of the salvage value, the date was inaccurate.
9 The Company then took the $1.5 million and deducted it from $3,265,657 to
10 arrive at its adjustment to Account 154.15-Glenrock Coal Material and Supply of
11 $1,765,657 ($3,265,657 less 1,500,000=$1,765,657).

12 **Q. WAS THE AMOUNT OF $3,265,657, FROM WHICH THE COMPANY**
13 **DEDUCTED $1.5 MILLION, REPRESENTATIVE OF THE MATERIALS AND**
14 **SUPPLIES INVENTORY AT DECEMBER 31, 1997?**
15 A. No, it was not. This was the net balance after an additional year of amortization
16 of the box cut at the Glenrock Mine at December 31, 1997. In other words, the
17 Company made a mistake in calculating the adjustment. This indicates that
18 there is no basis on which the Company knew what to write off or knew what was
19 actually going to be abandoned or written off in 1999. Clearly, this is not an
20 appropriate basis for charging ratepayers for materials and supplies which may
21 have been used and already charged to them through the cost of coal. I,
22 therefore, recommend an adjustment be made to remove this amount. It is not
23 known and measurable and does not represent a verifiable loss to the Company.

24 **Q. DID YOU MAKE ANY ADJUSTMENTS TO THE INITIAL BOX-CUT COST?**
25 A. No, I did not. Although there have been some additional adjustments to the
26 amortization, they appear to be minor, and the cost may be representative of
27 what might be abandoned.

1 **Q. HAS PACIFICORP ACTUALLY INCURRED ANY COSTS RELATED TO**
2 **RECLAMATION ACCRUAL OR EMPLOYEE SEVERANCE?**
3 A. No, both the reclamation accrual and the employee severance are costs which
4 have not been incurred.

5 **Q. WOULD YOU DISCUSS THE AMORTIZATION WHICH THE COMPANY IS**
6 **ATTEMPTING TO RECOVER FROM RATEPAYERS FOR EMPLOYEE**
7 **SEVERANCE?**
8 A. The Company, at December 31, 1997, estimated severance costs for the
9 employees who would take early retirement or be terminated to be $2.8 million.
10 During the last rate case, the employee complement at the Dave Johnston Mine
11 was decreased by 52 employees, 44 of which took early retirement. This early
12 retirement cost was recorded with other early retirement costs. The current
13 employee complement at the Dave Johnston Mine is employed in reclamation
14 and will remain employed at the mine at approximately the same level through
15 the year 2001. At that point, the complement at the mine will decrease to 13
16 employees through 2006. In its proposed accrual the Company attempts to
17 recover future costs in rates. These costs have yet to be incurred and are not
18 representative of any employee who has accepted an early retirement or
19 severance. The accrual also includes any severance that would have been
20 recorded in 1998. Therefore, the Company is double recovering and attempting
21 to recover a cost it has not yet incurred. It is not appropriate for rates to include
22 estimates of future costs or costs that have already been charged to ratepayers.
23 I have, therefore, removed all of the amortization associated with employee
24 severance.

25 **Q. EARLIER IN YOUR TESTIMONY YOU INDICATED THAT THERE WOULD BE**
26 **NO BENEFIT TO RATEPAYERS UNDER THE COMPANY'S AMORTIZATION**
27 **PROPOSAL. DO YOU HAVE A RECOMMENDATION WHICH THE**

1 **COMMISSION SHOULD ADOPT?**
2 A. Yes. I am recommending that the Commission follow the same policy that it
3 established for the amortization of the gain on the sale of the Centralia Plant.
4 The Commission concluded that it was appropriate to amortize the gain
5 recognized in rates which flowed to the benefit of ratepayers over the remaining
6 depreciable life of the Centralia Plant. This, of course, reduced significantly the
7 benefit that ratepayers will receive in any particular year as a result of that gain.
8 It would be appropriate for the Commission to amortize any cost to be recovered
9 associated with an abandoned plant over the remaining life of that plant in the
10 same manner it has recognized the gain on the Centralia sale. The Company, in
11 the last two rate cases, has claimed that the Dave Johnston Mine was projected
12 to continue operations through the year 2012. In fact, Company Witness
13 Getzelman presented an exhibit in the last case that showed that the Company
14 had planned on producing 4.2 million tons of coal in the year 2012 from this
15 mine. The mine closed in October 1999. The remaining life between October
16 1999 and October 2012 is 13 years. To be consistent with what the Commission
17 has accepted in the Centralia case, and the Commission's policy of roughly
18 matching costs to benefits over an amortization period, then it is appropriate to
19 use a 13-year amortization period.

20 On CCS Exhibit 1.4, I have shown the amortization for the remaining costs of the
21 Dave Johnston net investment in the column labeled CSS Amortization. This
22 amount is $1,735,157. As previously discussed, I am not recommending that
23 any amortization be included for materials and supplies because there has not
24 been any showing that an actual loss occurred. The next line is the Amortization
25 of the box cut, which I have calculated over the same 13-year period.

26 **Q. HAVE YOU ADJUSTED THE AMORTIZATION AUTHORIZED BY THE**
27 **COMMISSION IN THE LAST RATE CASE RELATED TO THE RECLAMATION**
28 **ACCRUAL?**

1 A. Yes, I have. I have deducted from the total reclamation accrual the amount
2 which the Commission authorized and that the Company has collected since the
3 current rates were authorized in May 2000. I reflected the amortization through
4 the end of the test year and deducted it from the total reclamation accrual
5 authorized by the Commission of $33,214,769. The Company would have
6 collected $2,214,318 of amortization through the end of the test year, September
7 30, 2000. This reduces the total amount to be recovered after the end of the test
8 year to $31,000,541. From the end of September 2000 to October 1, 2012 is 12
9 years. The remaining balance of the reclamation costs should be recovered over
10 this period of time. The amortization of the remaining balance is $2,583,371.

11 SYSTEMS APPLICATIONS AND PRODUCTS SOFTWARE (SAP)

12 **Q. IN THE COMMISSION'S DECISION IN DOCKET NO. 99-035-10, DID THE**
13 **COMMISSION SET FORTH A STANDARD TO MEASURE THE**
14 **EFFECTIVENESS OF THE IMPLEMENTATION OF SAP?**

15 A. In my opinion, it did. On pages 66 - 67 of the Commission's decision in that
16 docket the Commission stated:

> 17 We will allow neither the accelerated recovery of this investment proposed
> 18 by the Company and supported by the Division, nor a deferral until a later
> 19 test year as proposed by the Committee and LCG. Accelerated recovery
> 20 is based on a Company argument that benefits in the test year, in the
> 21 form of employee reductions and avoided costs associated with the
> 22 legacy software systems, exceed the costs of SAP, re-engineering and
> 23 the software write off, for a total, company-wide, net benefit of
> 24 approximately $5 million. We do not rely on this argument. The claimed
> 25 benefits are estimates of what the Company might have experienced
> 26 absent the decision to implement SAP. What is important, however, is
> 27 sustainable improvement in efficiency, measured over time as productivity
> 28 gains, resulting in lower costs per customer and increases in the quality of
> 29 service. These normally follow from the implementation of the new
> 30 system, not its anticipated deployment.

31

32 The Commission rejected the Company's argument that employee reductions

1 and other purported avoided costs are the result of SAP-related implementation
2 and associated costs. What the Commission stated was that an evaluation of
3 SAP should be judged based on "...sustainable improvement and efficiency,
4 measured over time as productivity gains, resulting in lower cost per customer
5 and increase in the quality of service." In other words, a cost-benefit analysis
6 showing the direct costs associated with the implementation of SAP compared to
7 the benefits (i.e., cost reductions) directly attributable to the use and
8 implementation of SAP.

9 **Q. WAS THE COMPANY ASKED WHETHER IT HAD UPDATED OR**
10 **PERFORMED A COST-BENEFIT ANALYSIS?**
11 A. Yes. The Committee asked, both in data requests and directly of a Company
12 representative, whether a cost-benefit analysis had been performed. The
13 answer was that no cost-benefit analysis had been performed specifically
14 relating the cost of SAP with directly attributable benefits.

15 **Q. WHAT BENEFIT DOES THE COMPANY CLAIM SAP HAS PROVIDED?**
16 A. Even though the Company has not performed a cost-benefit analysis, it has
17 claimed that all of the employee reductions (which were implemented in 1997
18 and 1998) together with the elimination of other support costs for the old legacy
19 system, are direct benefits of SAP. This claim is made even though SAP was
20 not implemented in 1998 and was phased-into the Company's operations in
21 1999, excluding coal operations. It flies in the face of common sense that one
22 could obtain productivity benefits from the future implementation of a software
23 system prior to that system being implemented. It would be akin to one claiming
24 an increase in gas mileage in the current year because you anticipated buying a
25 new automobile with higher gas mileage two years from now. The Company has
26 clearly stated in response to CCS Data Request 18-3 that "The Company has
27 not updated its SAP cost/benefit analysis." In my opinion, this must be
28 performed before one can accurately assess whether, and to what extent, SAP

1 costs provided a benefit to ratepayers and should be recoverable in rates.

2 ****BEGIN CONFIDENTIAL****

3 **Q.**

1 ****END CONFIDENTIAL****

2 **Q. WHAT ADJUSTMENT ARE YOU RECOMMENDING?**
3 A. I am recommending that the SAP cost and the amortization be maintained at the
4 level that the Commission authorized in Docket No. 99-035-10. The Company
5 has not provided sufficient support to justify any cost above that level. As
6 shown on CCS Exhibit 1.5, rate base should be reduced by $31,028,290 and
7 expenses should be reduced $3,060,404, both on a Utah basis.

8 RE-ENGINEERING
9 **Q. IN DOCKET NO. 99-035-10, THE COMMISSION'S ORDER INCLUDED AN**
10 **EXPENSE ASSOCIATED WITH THE RE-ENGINEERING RELATED TO SAP.**
11 **WOULD YOU PLEASE DISCUSS THOSE COSTS?**
12 A. In Docket No. 97-035-01, which was based on a 1997 test year, the Company
13 expensed $10,000,000 of costs which it had previously capitalized as part of the
14 BSIP/SAP cost. PacifiCorp claimed it was required to write off this cost for
15 accounting purposes as a result a pronouncement issued by the Emerging
16 Issues Task Force (EITF). In that docket, I opposed the expensing of these

1 costs and the recovery of these costs in rates because the re-engineering of the
2 Company's systems had not and could not produce any benefits to customers.
3 The Commission in that docket agreed with my analysis and did not allow the
4 Company to recover this $10 million expense.

5 In Docket No. 99-035-10, the Company had expensed an additional $6,274,127
6 on a total Company basis and sought to amortize this amount, plus the deferred
7 $10 million from the prior rate case, over a five-year amortization period. I again
8 opposed this amortization because the BSIP, which was implemented through
9 SAP, had not really been implemented in the Company's operations except for at
10 one generating station. The Commission accepted the Company's and Division
11 of Public Utilities' (Division) recommendation that the total amount
12 (approximately $16 million) be amortized over a five-year period. The
13 Commission stated: "We believe the record in this docket is sufficient to begin an
14 amortization in this test year because SAP was installed in one generating
15 station and we give some weight to the Company's claim that benefits were
16 realized."

17 **Q. DOES THE ADJUSTMENT PROPOSED BY THE COMPANY IN THIS CASE**
18 **INCLUDE THE AMORTIZATION AUTHORIZED BY THE COMMISSION IN THE**
19 **PRIOR DOCKET?**
20 A. Yes, it does. However, the Company has also included expenses which the
21 Commission did not allow to be deferred and amortized.

22 **Q. WOULD YOU PLEASE EXPLAIN?**
23 A. The Commission authorized the Company to amortize the amounts deferred
24 through 1998. The Commission concluded that SAP was providing some
25 benefits in 1998 and, therefore, the amortization of the approximately $16 million
26 would be appropriate. The Company stated that SAP was fully operational in
27 1999, and therefore, its full cost should be recognized in rates in this rate case.

1 However, the adjustment the Company is proposing on page 4.12 of its filing
2 includes $14,261,417 of expense it incurred from January 1999 to September
3 1999. All of these expenses are prior to October 1, 1999, the beginning of the
4 test year. If included in this adjustment, the Commission would be allowing the
5 Company to recover expenses from prior accounting periods. This would be
6 retroactive ratemaking.

7 **Q. HOW HAS THE COMPANY LABELED THIS ADJUSTMENT?**
8 A. It is interesting to note that the Company has not used the prior label from the
9 last rate case of "re-engineering," but has lumped the level of expenses
10 authorized by the Commission with the retroactive expenses outside of the test
11 year and renamed them as "BSIP/SAP Expense Adjustment." If the Commission
12 is to believe that SAP was fully operational in 1999, there would be no basis for
13 deferring and recovering from ratepayers expenses associated with the
14 operation of SAP in 1999. The Company's adjustment is a back-door attempt to
15 recover 1999 operating expenses that occurred prior to this test year.

16 **Q. ARE YOU SAYING THE COMPANY ACTUALLY EXPENSED THESE COSTS**
17 **IN 1999 FOR ACCOUNTING PURPOSES?**
18 A. Yes, I am. If, in fact, PacifiCorp believed the Commission had authorized the
19 deferral of these expenses, it would have capitalized them for accounting
20 purposes and requested recovery in this rate case. However, the costs were
21 expensed as normal operating expenses in 1999 and are being adjusted into the
22 September 2000 test year by the Company's adjustment on page 4.12 of the
23 filing.

24 **Q. WOULD YOU PLEASE EXPLAIN YOUR ADJUSTMENT TO REMOVE THESE**
25 **EXPENSES FROM THE TEST YEAR?**
26 A. On CCS Exhibit 1.6, I have shown the Committee's adjustment in the column
27 labeled "CCS Total Adjustment." This adjustment removes the expense from the

1 test year and places the amortization authorized by the Commission in the last
2 docket as expense in the current rate case. The next column is the original
3 adjustment proposed by the Company, which the Company acknowledges is in
4 error because it removed test-year expenses which were not actually in the test
5 year. The next column is a total Company correcting adjustment which removes
6 the error made in the Company's adjustment and removes the retroactive
7 expenses that the Company is attempting to recover. The last column of the
8 exhibit shows the Utah jurisdictional adjustment. On line four of my proposed
9 adjustment, I adjust the rate base to reflect only that amount of amortization
10 which was authorized by the Commission in the last docket. The column labeled
11 "Total Company Adjustment" reflects the retroactive portion of expense from the
12 period prior to the test year, which I am removing both from the expense and the
13 rate base. As shown on CCS Exhibit 1.6, test-year expense should be increased
14 by $364,358 and rate base should be decreased by $3,981,893, both on a Utah
15 basis.

16 1997 COMPUTER SOFTWARE WRITE-DOWN

17 **Q. WOULD YOU PLEASE EXPLAIN THE ADJUSTMENT YOU ARE**
18 **RECOMMENDING TO THE COMPUTER SOFTWARE WRITE DOWN?**

19 A. In 1997, the Company wrote off several computer programs in anticipation of the
20 implementation of SAP. The Commission, correctly, did not allow this
21 amortization in the prior two rate cases utilizing 1997 and 1998 test years.
22
23 The Company has stated that SAP was fully operational in 1999. In the current
24 rate case, with the test year ending September 30, 2000, the Company has
25 requested that the software be written off over a three-year period. The benefits
26 of SAP, if they do exist, will be experienced over a longer period of time. There
27 is no justification for using a write-off period as short as three years. In the last
28 rate case, the Division recommended that these programs be written off over a
29 five-year period. My adjustment shown on CCS Exhibit 1.7 revises the

1 Company's amortization to reflect the five-year write-off rather than the
2 requested three years. This has the effect of reducing the expense and the
3 revenue requirement associated with the amortization, while at the same time
4 increasing the rate base for the longer amortization period on a Utah basis. The
5 adjustment reduces test-year expenses by $343,363 and increases rate base
6 $503,970. The Company will still receive a return on and of all of the computer
7 programs written off. The five-year amortization would be more consistent with
8 the benefits which purportedly flow from the adoption of SAP.

9 **Q. DO YOU HAVE ANY CONCERNS ABOUT WHETHER THESE PROGRAMS**
10 **HAVE ACTUALLY BEEN ABANDONED?**
11 A. Yes, I do. The Company's tax adjustments are all to deferred tax balances and
12 deferred tax expense. This would indicate that no actual deduction has been
13 taken on the Company's tax return for these computer programs. The Company
14 should be required to show that it has actually written these off for tax purposes
15 and is still not utilizing these programs in the Company's operations. If, in fact, it
16 has not written them off and is still utilizing the programs, this amortization
17 should be eliminated in its entirety.

18 <u>COMPANY'S PROPOSED 1999 SOFTWARE WRITE-OFF</u>
19 **Q. IS THE COMPANY PROPOSING ADDITIONAL SOFTWARE WRITE-OFFS IN**
20 **THE TEST YEAR?**
21 A. Yes, it is. In November 1999, the Company wrote off approximately $5.6 million
22 of additional software over and above what it had written off in 1997. On page
23 8.14 of the filing the Company is seeking a three-year amortization of the
24 balance written off in 1999.

25 **Q. DO YOU AGREE WITH THE USE OF A THREE-YEAR AMORTIZATION**
26 **PERIOD FOR THE WRITE-OFF OF THESE ADDITIONAL SOFTWARE**

1 **PROGRAMS?**
2 A. No, I do not.

3 **Q. BEFORE YOU DISCUSS THE PROPER AMORTIZATION PERIOD TO UTILIZE**
4 **FOR THESE PROGRAMS, DO YOU THINK THAT THE COMPANY HAS**
5 **REMOVED ALL OF THE AMORTIZATION EXPENSE ASSOCIATED WITH**
6 **THESE PROGRAMS PRIOR TO THE ADJUSTMENT THE COMPANY IS**
7 **PROPOSING ON PAGE 8.14?**
8 A. No, I do not.

9 **Q. WOULD YOU EXPLAIN WHAT THE COMPANY HAS DONE AND WHAT**
10 **ADDITIONAL ADJUSTMENT IS NECESSARY?**
11 A. On CCS Exhibit 1.8 I have shown the amortization expense for each of the
12 software items that were written off, as reflected in the Company's filing under
13 Tab B4. This exhibit shows the description of the software program, the page on
14 Schedule B4 which the amortization appears on and the amortization expense.
15 The total amortization expense in the test year for these programs before the
16 Company's adjustment is $13,698,000. The amortization amount recorded in
17 the test year includes a reversal of part of the amortization expense, which is
18 shown on page 2 of 23, of Company Schedule B4, in the amount of $5,612,000.
19 I have shown this as an adjustment on CCS Exhibit 1.8. On page 8.14 of its
20 filing, the Company has adjusted out additional amortization expense in the
21 amount of $5,639,537. After reducing the amortization expense for these two
22 adjustments, amortization expense still includes an amount associated with
23 these programs that were written off. If this remaining amortization expense is
24 not removed, the Company will continue to recover amortization expense
25 associated with these programs in rates, in addition to the amortization of the
26 write-off the Company is proposing.

27 **Q. WHAT ADJUSTMENT IS NECESSARY TO REMOVE THE REMAINING**

1 **AMORTIZATION EXPENSE ASSOCIATED WITH THE WRITTEN OFF**
2 **SOFTWARE PROGRAMS?**
3 A. An additional adjustment of $2,446,463 is necessary to remove the amortization
4 associated with these abandoned programs. I have adjusted this amount for
5 software programs associated with non-electric operations. The total Company
6 electric operations adjustment, as shown on CCS Exhibit 1.8, is $2,339,511. On
7 a Utah basis, the adjustment is $867,420.

8 **Q. WHAT OTHER ADJUSTMENT ARE YOU PROPOSING TO THE COMPANY'S**
9 **AMORTIZATION OF THE SOFTWARE WRITE-OFF?**
10 A. The Company has requested a three-year amortization of the software write-off.
11 I have adjusted that amortization to reflect a five-year recovery period. There is
12 no reason to adopt a shorter amortization period. The SAP programs, if they are
13 of any value at all, will produce productivity benefits over a longer period of time.
14 The Commission has normally followed a policy of attempting to match costs
15 with benefits. By adopting a five-year amortization period, the software write-off
16 will better match the longer period for which SAP will be used.

17 UNCOLLECTIBLE EXPENSE
18 **Q. DO YOU BELIEVE THAT THE COMPANY'S ADJUSTMENT TO**
19 **UNCOLLECTIBLE EXPENSE REFLECTS THE APPROPRIATE LEVEL FOR**
20 **RATEMAKING PURPOSES?**
21 A. No, I do not. In Docket No. 99-035-10, the Commission adopted the
22 Committee's position that with the implementation of the new customer service
23 system and problems with its implementation, the Company's write-offs had
24 increased because of improper billings and poor collection procedures. The
25 Commission adopted the Committee's position that the percentage of
26 receivables written-off, which had increased in 1997 and 1998, were a direct
27 result of the implementation of CSS. The Commission adopted the percentage
28 of receivables written-off recommended by the Committee, which included the

1 three-year average 1994 through 1996.

2 After reviewing the Company's data since the last rate case, the amount of write-
3 offs has increased as a percentage of receivables. The following schedule
4 shows the percentage of write-offs to average receivables from 1994 through
5 2000, including the test year.

6

7 WRITE-OFFS AS A PERCENTAGE OF AVERAGE RECEIVABLES

	Year	Percentage of Receivables Written-Off
11	1994	0.0417
12	1995	0.0397
13	1996	0.0412
14	1997	0.0851
15	1998	0.1016
16	1999	0.1379
17	TY 09/30/00	0.1194
18	2000	0.0890

19 As can be seen, the Company's write-offs as a percentage of receivables has
20 increased in every year, 1997 through 1999. They declined in the test year to
21 almost 12% of receivables written-off, and declined in the year 2000 to almost
22 9% of receivables written-off. However, the write-offs are substantially higher
23 than they were in the years 1994 through 1996.

24 **Q. DID THE COMPANY'S ADJUSTMENT CORRECT FOR THE HIGH**
25 **PERCENTAGE OF RECEIVABLES WRITTEN-OFF IN THE TEST YEAR?**

26 A. No, it did not. The adjustment sponsored by the Company removes part of the
27 large percentage of the write-off, but does not return it to the average that the
28 Company experienced in the period 1994 through 1996.

1 **Q. WHAT ADJUSTMENT ARE YOU RECOMMENDING?**

2 A. I am recommending that the Commission continue to use the same average
3 receivable write-off percentage which it adopted in the last rate case. That is,
4 the average for the years 1994 through 1996, since there has not been a
5 significant improvement in years subsequent to the adoption of the CSS. I am
6 also recommending that the ratio of write-offs to recoveries be updated to reflect
7 the Company's more recent experience in collections. My recommended
8 calculation is shown on CCS Exhibit 1.10 and reduces the uncollectible expense
9 by an additional $1,286,758.

10 <u>POTENTIAL UPDATES</u>

11 **Q. WHAT ISSUES ARE YOU AWAITING ADDITIONAL RESPONSES ON THAT**
12 **MAY REQUIRE SUPPLEMENTAL TESTIMONY?**

13 A. Along with Committee witnesses Helmuth Schultz and Donna DeRonne, I am still
14 investigating the following areas and we reserve the right to supplement our
15 testimonies and exhibits in these areas:

16 • Supplemental Executive Retirement Plan;
17 • Incentive Compensation;
18 • Employee Benefits;
19 • Income Taxes;
20 • Retention Bonuses;
21 • Company Branding Costs;
22 • Bound for Belize Costs;
23 • Additional Write-Offs;
24 • Outside Services Expense;
25 • Miscellaneous Expenses and Accounting Entries;
26 • Cost Allocations/Corporate Costs;
27 • Auditor Workpapers;
28 • Street Lighting Revenue;
29 • Vehicle Expense; and
30 • Relocation Expense
31
32

33 As previously mentioned, the Company was consistently late in responding to
34 data requests. That development has greatly impeded our investigation.

1 Considering the significant level of overdue data requests, we plan to
2 supplement our testimonies for any issues that may arise as a result of the
3 information provided in the responses.

4 Additionally, Data Request CCS 20.13 requests information regarding the
5 Company's Major Issues Program, including a listing of projects assigned to the
6 program and resulting recommendations. The question was filed on April 9,
7 2001, resulting in an April 30, 2001 due date. We still have not received a
8 response to this question and reserve the right to further address issues that
9 may be presented in the response.

10 **Q. DOES THIS COMPLETE YOUR TESTIMONY?**

11 A. Yes, it does.