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BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

In the Matter of the Application of PacifiCorp for an Investigation of Inter- Jurisdictional Issues	Docket No. 02-035-04
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**PREFILED DIRECT TESTIMONY OF NEAL TOWNSEND IN SUPPORT OF MSP
SETTLEMENT AGREEMENT**

The Utah Association of Energy Users (UAE) hereby submits the Prefiled Direct
Testimony of Neal Townsend in support of the MSP Settlement Agreement in this docket.

DATED this 18th day of August, 2011.

HATCH, JAMES & DODGE

/s/ _____
Gary A. Dodge
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CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing was mailed, postage prepaid, this 18th day of August, 2011, to the following:

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BEFORE
THE PUBLIC SERVICE COMMISSION OF UTAH

Direct Testimony of Neal Townsend
In Support of MSP Settlement Agreement
On behalf of UAE

Docket No. 02-035-04

August 18, 2011

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DIRECT TESTIMONY OF NEAL TOWNSEND

INTRODUCTION

Q. Please state your name and business address.

A. My name is Neal Townsend. My business address is 215 South State Street, Suite 200, Salt Lake City, Utah, 84111.

Q. By whom are you employed and in what capacity?

A. I am a Senior Consultant in the firm of Energy Strategies, LLC. Energy Strategies is a private consulting firm specializing in economic and policy analysis applicable to energy production, transportation, and consumption.

Q. On whose behalf are you testifying in this proceeding?

A. My testimony is being sponsored by the Utah Association of Energy Users (“UAE”).

Q. Please describe your educational background.

A. I received an MBA from the University of New Mexico in 1996. I also earned a B.S. degree in Mechanical Engineering from the University of Texas at Austin in 1984.

Q. Please describe your professional experience and background.

A. I have provided regulatory and technical support on a variety of energy projects at Energy Strategies since I joined the firm in 2001. Prior to my employment at Energy Strategies, I was employed by the Utah Division of Public Utilities as a Rate Analyst from 1998 to 2001. I have also worked in the aerospace, oil and natural gas industries.

Q. Have you previously filed testimony before this commission?

23 A. Yes, I have testified in several utility regulatory proceedings before the Utah
24 Public Service Commission (PSC or Commission).

25 **Q. Have you testified before utility regulatory commissions in other states?**

26 A. Yes. I have testified in utility regulatory proceedings before the Arkansas Public
27 Service Commission, the Illinois Commerce Commission, the Kentucky Public Service
28 Commission, the Michigan Public Service Commission, the Public Utility Commission of
29 Oregon, and the Public Service Commission of West Virginia.

30

31 **Overview and conclusions**

32 **Q. What is the purpose of your testimony in this proceeding?**

33 A. The purpose of my testimony is to:

34 (1) Recommend Commission approval of the Agreement Pertaining to PacifiCorp's
35 September 15, 2010 Application for Approval of Amendments to Revised
36 Protocol Allocation Methodology ("MSP Agreement") entered into among
37 PacifiCorp, the Utah Division of Public Utilities, the Office of Consumer Services
38 and UAE; and

39 (2) Explain UAE's reasons for signing the MSP Agreement, and articulate UAE's
40 understandings and assumptions in so signing.

41

42 **Background**

43 **Q. Can you provide some background about the interjurisdictional allocation issues**
44 **that are the subjects of this current MSP proceeding?**

45 A. Yes. PacifiCorp's interjurisdictional allocation issues have existed since the
46 merger of Pacific Power and Light and Utah Power and Light which the Commission
47 approved in Docket No. 87-035-27.

48 In Docket 90-035-06, the first rate case following the merger, the Commission did
49 not adopt an interjurisdictional allocation method. However, it did include a "Merger
50 Fairness Adjustment" as an addition to the Utah revenue requirement which recognized
51 cost differences that existed in the two previously separate utilities at that time of the
52 merger. The merger fairness adjustment was to be phased out over time. This merger
53 fairness adjustment was included in subsequent Semi-Annual Utah Results of Operations
54 Reports filed with the Commission.

55 **Q. What happened after the Docket 90-035-06 rate case?**

56 A. In February 1997, a recommendation was made to the Commission that a Utah
57 Power and Light rate case be initiated. The rate case, Docket No. 97-035-01, was
58 suspended by the legislature while it studied restructuring of the electric industry, but the
59 suspension included a refund provision. While the rate case was suspended, the
60 Commission adopted the "Rolled-In" interjurisdictional allocation method for use in Utah
61 ratemaking in Docket No. 97-035-04.

62 **Q. What happened after the suspension of the rate case in Docket 97-035-01 was lifted?**

63 A. The Utah revenue requirement in that case was determined using the Rolled-In
64 allocation method. As part of Utah's move to the Rolled-In methodology in that case, the
65 Utah Commission reduced a \$111 million refund due to Utah customers by \$71 million,

66 the amount of the present value of the remaining portion of the Merger Fairness
67 Adjustment.¹

68 **Q. What is the Rolled-In allocation methodology?**

69 A. “Rolled-In” is a name often used for a particular methodology of apportioning the
70 costs and revenues associated with PacifiCorp's generation, transmission and distribution
71 systems among the six states in which PacifiCorp operates. The Rolled-In allocation
72 methodology, as currently defined for PacifiCorp's system, allocates PacifiCorp's
73 generation and transmission costs based on a demand factor derived using twelve
74 monthly coincident peaks (12 CP), an annual energy factor, and a 75% demand
75 factor/25% energy factor weighting.

76 **Q. What is the Revised Protocol allocation methodology and how did it come to be used
77 in Utah ratemaking?**

78 A. The Revised Protocol is the name used for a different methodology for
79 apportioning the costs and revenues associated with PacifiCorp's generation, transmission
80 and distribution systems among the six states in which PacifiCorp operates. The Revised
81 Protocol was developed during the first half of the last decade following a series of
82 discussions among representatives from various states served by PacifiCorp in what has
83 come to be known as the Multi-State Process (MSP). The MSP was initiated several
84 years after the 1999 final decision in Docket No. 97-035-01.

85 **Q. How long has the Revised Protocol been used in Utah rate proceedings?**

1 See Docket No. 97-035-01 Report and Order, pp. 54-63, dated March 4, 1999.

86 A. The Revised Protocol's role in Utah ratemaking proceedings was the subject of a
87 Commission order approving an MSP stipulation in December 2004 in this docket. The
88 Revised Protocol (along with certain rate mitigation measures) methodology has been
89 used by RMP in its Utah rate filings since that order, along with Rolled-In.

90 **Q. Is PacifiCorp proposing to make a change to the Revised Protocol?**

91 A. Yes. On September 15, 2010, PacifiCorp, dba Rocky Mountain Power (RMP) in
92 Utah, filed a request with the Commission to amend its "Revised Protocol" inter-
93 jurisdictional allocation methodology.

94 **Q. Why is PacifiCorp proposing to modify the Revised Protocol?**

95 A. The Utah Commission has been using the "Rolled-In" allocation method as a
96 "benchmark" to gauge the reasonableness of Revised Protocol results since 2004. The
97 Commission's benchmarking analysis indicated that the actual Utah results under the
98 Revised Protocol were not trending in the same manner as the Utah results projected
99 during development of the Revised Protocol methodology. This discrepancy in results
100 led the Utah Commission to notify the MSP Standing Committee that it was not satisfied
101 with the Revised Protocol methodology. That notification led to development of the
102 2010 Protocol.

103 **Q. Can you describe the changes PacifiCorp proposed to the Revised Protocol in its
104 September 15, 2010 filing?**

105 A. Yes. As described in the testimony of RMP witness Steven R. McDougal, the
106 Company proposes several changes to the Revised Protocol to arrive at a new allocation
107 method termed the "2010 Protocol". The 2010 Protocol would govern inter-jurisdictional
108 allocations through 2016. The changes to the Revised Protocol include 1) elimination of

109 the unique allocation of Seasonal Resources, 2) replacement of the variable embedded
110 cost differential calculation with a more limited, fixed dollar levelized calculation, and 3)
111 situs treatment of Klamath Hydro removal costs. Underlying the more limited, fixed
112 dollar levelized calculation is an embedded cost differential calculation for a Hydro
113 Endowment that compares the cost of hydro (both Company-owned and Mid-C contracts)
114 with the cost of All-Other resources that existed prior to 2005. Additionally, the fixed
115 dollar calculation includes situs treatment for the Klamath Surcharge which is not treated
116 as situs in the underlying cost allocation.

117 **Q. Please explain the Utah MSP Agreement that is the subject of your testimony.**

118 A. After PacifiCorp filed its Revised Protocol amendments, the Company and
119 various Utah parties had several meetings to discuss various aspects of the proposed
120 amendments. Those discussions culminated in the MSP Agreement that basically adopts
121 the 2010 Protocol for Utah ratemaking purposes, subject to the terms set forth in that
122 agreement.

123 **Q. Can you generally describe the terms of the MSP Agreement?**

124 A. Yes. The MSP Agreement has several important terms. First, the Agreement
125 continues use of the Rolled In methodology as the Utah benchmark for ratemaking
126 purposes. As a practical matter, the Utah revenue requirement will be determined using
127 the Rolled-In allocation method for the duration of the Agreement. Second, the
128 Agreement sets the proposed offsetting 2010 Protocol Hydro Endowment and the
129 Klamath surcharge situs fixed dollar adjustments to zero. These two adjustments result in
130 Utah forgoing about \$1 million a year credit, but allows the 2010 Protocol to produce
131 results generally consistent with the Rolled-In methodology in Utah (subject to

132 continuing disagreement over treatment of Klamath Related Costs, as discussed below).
133 Third, the Agreement preserves the right of all Utah parties to challenge or contest the
134 proper Utah ratemaking treatment of all costs associated with shutting down and
135 removing the Klamath Dam hydro resource (“Klamath Related Costs”). These costs
136 include the ratemaking treatment for Klamath plant in service, recovery of relicensing
137 and settlement costs, and dam removal costs. UAE addressed some of these Klamath
138 issues in its prefiled testimony in RMP's recently concluded general rate case (Docket
139 No. 10-035-124). In that case, UAE raised two issues related to the Klamath Dam. First,
140 UAE argued that it was premature to change the depreciation rate for the Klamath plant
141 at this time. Second, UAE recommended including a revenue credit in Utah for revenues
142 collected in California and Oregon to offset the cost of dam removal. These two
143 adjustments reduced Utah's revenue requirement by roughly \$9 million. The rate case
144 was resolved by a settlement which was recently approved by the Commission. In that
145 settlement, issues relating to Klamath Related Costs have been deferred to future cases
146 for resolution. UAE is satisfied that the rate case settlement satisfactorily addresses these
147 issues for the time being, with UAE and other parties reserving their rights to take any
148 position deemed appropriate on Klamath Related Costs in future proceedings.

149 **Q. What method will be used to allocate interjurisdictional costs after 2016?**

150 A. It is not clear under the 2010 Protocol what method will be used after 2016. The
151 2010 Protocol continues the Standing Committee function, which will presumably
152 address this issue. According to RMP witness Andrea Kelly, the Standing Committee
153 and its workgroup will address the post-2016 issue in a process similar to the one that
154 developed the 2010 Protocol. The result could be a continuation of the 2010 Protocol or

155 it may involve some other new allocation regime. UAE will likely continue to argue that
156 some type of Rolled-In allocation methodology should be used in Utah, at least so long as
157 an Energy Balancing Account (EBA) continues to subject Utah ratepayers to hydro-
158 related risks.

159 **Q. Do you have any other general background comments?**

160 A. Yes. I note that, at the time of the Utah Power and Pacific Power merger,
161 PacifiCorp explicitly accepted the risk that inconsistent inter-jurisdictional cost allocation
162 methods might be used by various state commissions. Commission approval of the
163 merger would likely have been far more complicated had the Company not explicitly
164 accepted that risk. The Company's explicit agreement to accept this risk must be
165 factored into any fair and reasonable resolution of inter-jurisdictional allocation disputes.

166

167 **Support for the MSP Agreement**

168 **Q. Do you believe the Commission should approve the MSP Agreement and the**
169 **associated 2010 Protocol and related agreements?**

170 A. Yes. Taken as a package, I believe the MSP Agreement and associated 2010
171 Protocol and agreements are in the public interest and should be approved by the
172 Commission.

173 **Q. Why do you believe the MSP Agreement and associated 2010 Protocol are in the**
174 **public interest?**

175 A. From UAE's perspective, there are at least two reasons why the MSP Agreement
176 should be approved. First, UAE believes that it is important for the various states served
177 by the Company to at least attempt to develop reasonable and generally consistent cost

178 allocation methodologies that will both produce just and reasonable results in this State
179 and also provide the Company with a reasonable opportunity to recover its prudently
180 incurred costs. The MSP Agreement reduces the risk that various jurisdictions will adopt
181 inter-jurisdictional cost allocation methods that are materially inconsistent.

182 Second, in PacifiCorp's energy balancing account (EBA) proceeding, UAE has
183 consistently argued that a Rolled-In allocation methodology should be used in Utah rate
184 proceedings if an EBA is to be used in Utah in order to match risk and reward. The
185 Commission has now authorized an EBA pilot and the MSP Agreement will ensure that a
186 Rolled-In methodology will be used during that pilot period.

187 For these reasons, I conclude that the MSP Agreement and associated 2010
188 Protocol and agreements, taken as a whole, are in the public interest. The 2010 Protocol
189 should largely continue the use of generally-consistent inter-jurisdictional allocation
190 methods if adopted by most of the states that PacifiCorp serves. In addition, the
191 Agreement provides Utah with the benefits of a Rolled-In methodology, at least during
192 the term of the EBA pilot.

193 I caution, however, that the 2010 Protocol and MSP Agreement should be viewed
194 for what they represent – reasonable compromises among the competing interests of the
195 Company, Utah ratepayers and ratepayers from other states. As such, it should not be
196 considered as definitive in determining appropriate cost-allocation procedures among the
197 various Utah rate classes. Other relevant factors should also be taken into consideration
198 in that process.

199 **Q. Does this conclude your direct testimony?**

200 **A.** Yes, it does.