Docket No. 04-035-42
Mary H. Cleveland
Exhibit No. DPU 3.0
December 3, 2004

BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

In the Matter of the Application of PacifiCorp for Approval of its Proposed Electric Rate Schedules & Electric Service Regulations	)))	DOCKET NO. 04-035-42

PREFILED DIRECT TESTIMONY OF

MARY H. CLEVELAND

FOR THE

DIVISION OF PUBLIC UTILITIES

DEPARTMENT OF COMMERCE

STATE OF UTAH

DECEMBER 3, 2004

I. QUALIFICATIONS

Q. PLEASE STATE YOUR NAME FOR THE RECORD.

A. Mary H. Cleveland

Q. BY WHOM ARE YOU EMPLOYED AND WHAT IS YOUR BUSINESS ADDRESS?

A. I am employed by the Utah Department of Commerce, Division of Public Utilities (Division). My business address is 160 East 300 South, Suite 400, Salt Lake City, Utah, 84114.

Q. WHAT IS YOUR POSITION?

A. Utility Regulatory Analyst.

Q. BRIEFLY DESCRIBE YOUR EDUCATIONAL AND PROFESSIONAL BACKGROUND.

A. I hold a Bachelor of Business Administration, as well as a Master of Business Administration, from the University of Missouri-Kansas City. I am a licensed Certified Public Accountant (CPA) in the state of Kansas and I am a member of the Institute of Certified Public Accountants. In addition I have attended the National Association of Regulatory Utility Commissioners (NARUC) Staff Subcommittee on Accounts meetings and have served on the NARUC Securities and Exchange Commission (SEC) Subcommittee.

I have over twenty years of utility regulatory experience, both as a consultant and as an employee of state regulatory agencies. I have participated in regulatory proceedings in the states of Alaska, Arizona, Connecticut, Kansas, Missouri, New Mexico, Ohio, Utah and Wisconsin. I have also testified before the Kansas Supreme Court. Further details regarding my background are provided in Appendix A.

II. PURPOSE OF TESTIMONY

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. My testimony addresses PacifiCorp's management fee, ScottishPower cross-charges, incentive compensation, insurance and union labor overtime. Division witness Bart Croxford will address all other payroll, including compensation levels, projected number of employees and projected wage increases.

III. ADJUSTMENTS

1. PacifiCorp Management Fee

Q. PLEASE EXPLAIN YOUR ADJUSTMENT TO PACIFICORP'S MANAGEMENT FEE.

A. This adjustment consists of two parts. First, it updates the allocation factors used to allocate PacifiCorp's corporate costs among its affiliates to the most recent known and measurable level. Secondly, it recognizes the estimated dollar amount of PacifiCorp's corporate costs that will be charged to ScottishPower.

PacifiCorp's corporate costs are recorded on the electric utility's books. A portion of these corporate costs is then allocated to PacifiCorp's other subsidiaries by a three factor formula, which is based on each subsidiary's share of operating expenses, number of employees and assets at the end of the previous fiscal year. Thus, FY '03 operating expenses, year-end employee numbers and year-end assets form the basis for the allocation of corporate costs incurred in FY'04. PacifiCorp's projected FY'06 test year utilized the FY'04 allocation factors. The Company provided no justification for the continued use of the FY'04 allocation factors. The Division adjusted the projected FY'06 test year to reflect the current FY'05 allocation factors. The FY'05 allocation factors are based on more current operating characteristics of the subsidiaries and therefore are more representative of the future.

Additionally, PacifiCorp's corporate costs have been reduced for the estimated amount thereof to be cross-charged to ScottishPower. In FY'05 a cross-charge was implemented between ScottishPower and PacifiCorp wherein ScottishPower began charging PacifiCorp for a portion of its corporate costs and PacifiCorp likewise began direct charging ScottishPower for select corporate services. Per Docket No. 03-035-26, PacifiCorp charges to ScottishPower were estimated to be under $2 million annually.

Updating the allocation factors to the most recent known and measurable, and removing the estimated corporate costs to be charged to ScottishPower, results in a reduction to projected FY'06 Utah jurisdictional expenses of $1,021,535 as shown on DPU Exhibit No. 3.1 (MHC).

2. ScottishPower Cross-Charge

Q. PLEASE DESCRIBE THE SCOTTISHPOWER CROSS-CHARGE.

A. PacifiCorp and ScottishPower UK plc (”SPUK”), executed a cross-charge policy agreement, effective October 1, 2003, governing the allocation of costs incurred by each entity on behalf of the other. Prior to the execution of this agreement PacifiCorp was only charged for the direct costs of ScottishPower international assignees. Subsequent to the execution of this agreement, ScottishPower began, in April 2004, to allocate a portion of its corporate costs to PacifiCorp.

Q. PLEASE DESCRIBE THE METHODOLOGY USED TO CHARGE SCOTTISHPOWER CORPORATE COSTS TO PACIFICORP.

A. ScottishPower costs may be directly charged, directly allocated, or apportioned to the various business segments using a four-factor formula. Costs that are directly attributable to entities within the ScottishPower group are directly billed to that entity. For example, costs incurred to work on a specific project for a particular entity are charged to that entity. Some costs are directly allocated based on a cost causation factor. For example, the cost of preparing and distributing the internal news magazine to employees is directly allocated to each entity based on the number of employees in the entity.

Currently there are five direct allocation factors: (1) Employee numbers; (2) Senior Management Group (SMG) membership; (3) Group FTEs at site; (4) Total Group FTEs; and, (5) LTIP membership. As mentioned previously, employee numbers are used to allocate the cost of the employee magazine. SMG membership within each entity is used to allocate the costs of supporting the SMG function. Group FTEs at each of the corporate locations, Atlantic Quay and Avondale are used to allocate the location's property costs. Total Group FTEs are used to allocate IT support costs. LTIP membership in each entity is used to allocate LTIP costs across the group.

ScottishPower corporate costs, which are not directly assigned or directly allocated, are apportioned on a four-factor formula. The four-factor formula develops weighted average percentages of the following characteristics for each business segment within the ScottishPower group: (1) turnover, or gross retail sales; (2) operating profit; (3) net assets; and, (4) number of employees. Each characteristic is equally weighted.

Q. HAS THIS ALLOCATION METHODOLOGY RECEIVED APPROVAL FROM ANY REGULATORY BODIES?

A. Yes, both the Securities and Exchange Commission (SEC) and the Oregon Public Service Commission have approved the allocation methodology. PacifiCorp was required to seek approval in Oregon pursuant to ORS 757.490, ORS 757495 and OAR 800-027-0040, which require authorization from the Commission to engage in business transactions with affiliates.

The Division has reviewed and discussed the process under which the methodology was established with both PacifiCorp and ScottishPower. We met with members of the Oregon staff. We do not object to the methodology and have adopted it within the context of this rate filing.

Q. WHAT IS THE BASIS FOR THE AMOUNT OF SCOTTISHPOWER CROSS-CHARGES INCLUDED IN THIS DOCKET?

A. The amount of the ScottishPower cross-charge included in this docket are the FY'05 budgeted amounts. There were no cross-charges in FY '04.

Q. WHAT ADJUSTMENTS DID YOU MAKE TO THESE BUDGETED AMOUNTS?

A. I made three adjustments to the budgeted amounts. First, I removed non-regulated items. Second, I updated the allocation factors to the most recent known and measurable level. Third, I assigned a portion of the cross-charge received by PacifiCorp to its subsidiaries based on the three-factor formula used to allocate the management fee.

The FY'05 cross-charge budget contained two non-regulated items, Long Term Incentive Plan (LTIP) and Strategic Projects. LTIP applies to a limited number of executives. PacifiCorp's LTIP has not been allowed in rates and the Company has not requested recovery of LTIP in the current docket. LTIP allocated from ScottishPower should likewise be excluded. Strategic Projects involves scouting for business opportunities and managing their development. This is a non-regulated activity.

The allocation factors applied to the FY’05 cross-charge budget to derive PacifiCorp’s share were based on March 2003 year-end accounts. These factors have since been updated per the Group Recharge policy to reflect March 2004 year-end accounts. I have adjusted PacifiCorp’s share to reflect the updated factors. These factors are based on more current operating characteristics of the ScottishPower Group and therefore are more representative of the future.

PacifiCorp allocates a portion of the cross-charge it receives from ScottishPower to its other subsidiaries, with the exception of Pacific Power Marketing (PPM), based on the three-factor formula it uses to allocate corporate overhead costs. PPM does not receive an allocation of the ScottishPower cross-charge as it, like PacifiCorp, is a recipient of the ScottishPower cross-charge. I have reduced the ScottishPower cross-charge to reflect the amount charged to PacifiCorp other subsidiaries.

These adjustments to the ScottishPower cross-charge result in a reduction to projected FY’06 Utah jurisdictional expenses of $866,913 as shown on DPU Exhibit No. 3.2 (MC).

Q. DPU EXHIBIT NO. 3.2 (MC) ALSO SHOWS AN ADJUSTMENT TO SCHEDULE M. WOULD YOU PLEASE EXPLAIN THE SCHEDULE M ADJUSTMENT.

A. The Company's income tax calculation includes the ScottishPower cross-charge as a permanent addition on Schedule M, thus not allowing the cross-charge to be a deductible expenditure. On a stand-alone basis, had PacifiCorp received these same services from an outside source, they would be deductible. Since for ratemaking purposes income tax is computed on a stand-alone basis, the cross-charge should not be included on Schedule M. This adjustment reduces Schedule M additions $14,116,629. It results in a $2,229,161 reduction to Utah jurisdictional federal income taxes as shown on Exhibit DPU 3.2 (MC), page 2.

3. Insurance Expense

Q. PLEASE EXPLAIN YOUR ADJUSTMENT TO INSURANCE EXPENSE.

A. This adjustment corrects various errors in the Company's projection of insurance expense for FY'06. First, the base year, FY'04, premiums and uninsured losses for the twelve months ended March 31, 2004, shown on Tab 4.13.1 in the Company's filing are incorrect. The actual costs recorded on the Company's books and records for property insurance premiums (SAP Acct. 548000) and property uninsured losses (SAP Acct. 548050), were $11,378,024 and $14,000,000 respectively, for a total recorded cost of $25,378,024. This compares to property insurance premiums and uninsured losses shown on Tab 4.13.1, of $12,345,921 and $12,300,000 respectively, for a total of $24,645,921.

The actual costs recorded on the Company's books and records for liability insurance premiums (SAP Acct. 545000) and liability uninsured losses (SAP Acct. 545050) were $7,179,322 and $8,253,159 respectively, for a total of $15,432,481. This compares to liability insurance premiums and uninsured losses shown on Tab 4.13.1, of $6,552,897 and $8,528,445 respectively, for a total of $15,081,342. The erroneous figures for the twelve months ended March 31, 2004, on Tab 4.13.1 were compared to the FY'06 budget for property insurance, $25,050,000, and liability insurance $16,680,000, the difference being the adjustment needed to bring the actual FY'04 property and liability insurance to the budget FY'06 level.

But, the error did not cease at this point. Within the filing, the Company applied the FY'05 inflation factors to the actual recorded FY'04 property and liability insurance to calculate projected FY'05 property and liability insurance, and then proceeded to add the erroneously calculated difference between the FY'04 property and liability insurance and the budgeted FY'06 property and liability insurance to the projected FY'05 property and liability insurance, to arrive at the FY'06 property and liability insurance actually included in the calculation of the revenue deficiency. This resulted in the FY'06 property and liability insurance actually included in the filing significantly exceeding the Company's FY'06 budget shown on Tab 4.13.1.

This adjustment reduces the property and liability insurance expense actually included in the filing to the Company's FY'06 budgeted levels. It results in a reduction to projected FY'06 Utah jurisdictional expenses of $1,465,640, as shown on DPU Exhibit No. 3.3 (MC).

4. Incentive Compensation

Q. PLEASE EXPLAIN YOUR ADJUSTMENT TO INCENTIVE COMPENSATION.

A. This adjustment is twofold. First it reduces the incentive compensation included in the projected FY'06 test year to target levels. Secondly, it removes that portion of incentive compensation that is based on financial goals, lobbying and image building that are not appropriate for rate recovery.

PacifiCorp's compensation package consists of a base salary plus a target incentive designed to provide total compensation at market levels when performance is at desired levels. In exceptional performance years, the incentive may be up to two times the target, but **on average** over several years, the incentive is designed to produce results generally very near the target level (Response to DPU Data Request 1.14). However, the incentive level included in the Company's projected FY'06 test year is 70% of the maximum achievable level, two times the target. This is in excess of the 50% required to achieve market pay-rates.

The target consists of three components; total PacifiCorp, business unit, and individual performance, each of which, comprise a percentage of the target. Total PacifiCorp comprises 10% of the target. If 100% of total PacifiCorp goals and objectives as established within the incentive plan are met, a participant receives 10% of the target. The goal and objective for total PacifiCorp is to optimize profitability through the achievement of a certain level of earnings before income tax. The business unit comprises 30% of the target. Each business unit has its own set of goals and objectives some of which are financial and others, which consist of influencing elected officials and enhancing and protecting the reputation of the ScottishPower group. For example, Regulation & External Affairs goal and objectives include the following; regulatory ROE allowed (20%), ensure that federal and state laws and attitudes amongst state and federal elected officials do not impede cost recovery opportunities (10%) and meet rate case process performance goals (10%). Corporate Communications goal and objectives include enhance and protect reputation of ScottishPower group (25%).

Reducing the projected FY'06 incentive compensation to the target level; and removing that portion of incentive compensation that is based on financial goals, lobbing and image building results in a reduction to projected FY'06 Utah jurisdictional expenses of $4,126,767 as shown on Exhibit DPU No. 3.4 (MC).

5. Over-time Pay

Q. PLEASE EXPLAIN YOUR ADJUSTMENT TO OVER-TIME PAY.

A. In late December 2003, heavy wet snow caused significant outages and damage in Utah as well as the Company's southern Oregon and northern California service areas. This resulted in a significant increase in overtime paid to the Company's union employees as evidenced by the sharp increased in overtime and premium pay expensed on the Company's books in January 2004, for maintenance of overhead lines. Overtime and premium pay expensed in January 2004 for maintenance of overhead lines was nearly twice the normal level. The Company's projected payroll expense for FY'06 used actual FY'04 overtime.

This adjustment reduces overtime and premium pay for maintenance of overhead line to a normal level. The reduction in expense is prorated between the Utah jurisdiction and others based on the actual loss incurred in each jurisdiction. It results in a reduction to FY'06 Utah jurisdictional expenses of $1,374,879, as shown on DPU Exhibit No. 3.5 (MC).

6. Revenue

Q. PLEASE DESCRIBE YOUR ADJUSTMENT TO REVENUE.

A. This adjustment increases Utah jurisdictional revenues, $2,809,419, to reflect the recent change in US Magnesium LLC's contract. There are other Utah jurisdictional contracts that are scheduled to expire in December 2004. The Division reserves the right to further adjust revenues for any known and measurable changes to these other contracts that occur prior to this docket's rate effective date.

IV. CONCLUSION

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes.

RESUME
MARY H. CLEVELAND

EDUCATION:

BBA-Accounting: University of Missouri-Kansas City, 1971
MBA-Accounting: University of Missouri-Kansas City, 1974

HONORS:

Beta Gamma Sigma

CPA STATUS:

Licensed in Kansas

EMPLOYMENT:

Mar. 1998 to present: Utah Division of Public Utilities
160 East 300 South, Suite 400
Salt Lake City, UT 84114

Position: Utility Regulatory Analyst IV

Description: Primarily responsibilities include reviewing utilities' affiliated transactions and accounting for regulated and non-regulated activities. Participated in the evaluation of the ScottishPower / PacifiCorp merger. Also review gas procurement activities, participate in rate case investigations, prepare written testimony and testify before the Utah Public Service Commission.

Aug. 1991 to Mar. 1998: Utah Committee of Consumer Services
160 East 300 South, Suite 408
Salt Lake City, UT 84114

Position: Utility Regulatory Analyst IV

Description: Represented residential, small commercial and agricultural customers in utility matters. Monitored, assessed and reported on current issues facing the utility industry. Planned and conducted audits of gas and electric utilities in conjunction with rate applications, prepared written testimony and testified before the Utah Public Service Commission. Assignments included participation in the IndeGO (proposed independent system operator for the Northwest region) Pricing Work Group and Steering Committee, evaluating PacifiCorp's integrated resource planning process, participating in PacifiCorp's Demand-Side Management Advisory Group, and assisting in the evaluation of PacifiCorp's stranded cost exposure. Also evaluated gas procurement activities of Questar Gas.

Oct. 1998 - Aug. 1991: Utah Division of Public Utilities
160 East 300 South
Salt Lake City, UT 84114

Position: Utility Rate Engineer

Description: Participated in audits of utilities in conjunction with rate applications, prepared written testimony and testified before the Utah Public Service Commission. Evaluated and prepared written recommendations on utility tariff and special contract filings. Assisted in the evaluation of the PacifiCorp / Utah Power & Light merger.

Apr. 1985 - Oct. 1998: LMSL, Inc.
10955 Lowell
Overland Park, KS 66210

Position: Senior Regulatory Consultant

Description: Participated in rate case investigations and other special studies on behalf of state utility commissions, prepared written testimony and testified in various proceedings.

Aug. 1983 - Apr. 1985: Troupe Kehoe Whiteaker and Kent
800 Penn Tower Building
3100 Broadway
Kansas City, MO 64111

Position: Senior Regulatory Consultant

Description: Local CPA firm specializing in regulated industries. Work included rate case investigations, preparation of written testimony and testifying before various state regulatory commissions. Also participated in year-end financial audits of small independent telephone companies and rural electric companies and assisted in tax return preparation.

Mar. 1981 - Aug. 1983: Kansas Corporation Commission
Utilities Division
1500 S.W. Arrowhead Road
Topeka, KS 66604-4027

Position: Senior Utility Regulatory Auditor

Description: Planned and conducted audits of utilities in conjunction with rate case applications, prepared written testimony and served as an expert witness in rate hearings before the Commission.

Aug. 1977 - Mar. 1981: University of Kansas Medical Center
Institutional Research & Planning / Budget Office
3900 Rainbow Boulevard
Kansas City, KS

Position: Analyst / Accountant

Description: Conducted special operational and long-range planning studies. Work involved programming with SPSS, SAS and Mark IV; program documentation and report writing.

Jun. 1973 - Aug. 1977: Midwest Research Institute
425 Volker
Kansas City, MO 64110

Position: Operations Analyst

Description: Performed operational audits and developed management information systems for a variety of clients. Also conducted workshops on long-range planning. Work involved programming with FORTRAN and SPSS, program documentation and report writing.

Apr. 1969 - Jun 1973: University of Missouri - Kansas City
Library Accounting / Acquisitions
5100 Rockhill Road
Kansas City, MO 64110

Position: Accountant

Description: General accounting, budget preparation and fiscal reporting.

MEMBERSHIPS:

American Institute of Certified Public Accountants.
