Q. Please state your name and business address.

A. My name is Lowell E. Alt, Jr. My address is 4084 Emma Circle, Salt Lake City, Utah, 84124

Q. On whose behalf are you testifying?

A. I am testifying on behalf of PacifiCorp.

QUALIFICATIONS

Q. Briefly describe your educational and professional background.

A. I received a Bachelor of Science degree in Electrical Engineering and a Master of Business Administration degree from West Virginia University. I am a Registered Professional Engineer licensed in Pennsylvania and Utah. I have attended numerous conferences and seminars on various aspects of utility regulation. I retired in December 2005 as Executive Staff Director of the Utah Public Service Commission after a twenty-five year career in Utah utility regulation. I served as Director of the Utah Division of Public Utilities from March 2001 to August 2003, Manager of the Energy Section from October 1995 to March 2001, Chief Engineer from 1983 to 1995 and Rate Engineer from 1980 to 1983. I have testified before the Utah Public Service Commission in numerous electric, natural gas and telecommunication cases on various topics including customer charges, interim rates, rate case stipulations, rate design, cost-of-service, mergers, service extensions and return on equity. I was the Division's witness on class cost of service and rate design for every Utah Power rate case from 1983 to 1998. I have completed numerous cost-of-service studies of various utilities including Utah Power, U.S. West Communications, several rural electric

cooperatives and two water companies. Earlier this year, I published a book, *Energy Utility Rate Setting*. I previously worked for Pennsylvania Power and Light Company from 1968 to 1980. My last positions there were Distribution Senior Engineer-Substations and Senior Tariff Analyst.

PURPOSE AND SUMMARY OF TESTIMONY

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to address issues raised in the direct testimony of the following witnesses regarding the residential customer charge and minimum bill:

1. Abdinasir M. Abdulle – Utah Division of Public Utilities
2. Ronald J. Binz – AARP
3. Anthony J. Yankel - Committee of Consumer Services
4. Elizabeth A. Wolf – The Ratepayers Alliance

Q. Please provide a brief summary of your testimony.

A. I describe the purpose and nature of customer charges and minimum bills. I provide a brief history of PacifiCorp's residential customer charge in Utah and discuss common rate design objectives and principles, including the importance of cost-based rates. I discuss the areas of agreement and disagreement with the positions taken by the witnesses I listed above. Finally, I explain why PacifiCorp's residential customer charge proposal in this case is reasonable.

DESCRIPTION OF CUSTOMER CHARGES AND MINIMUM BILL

Q. As your testimony addresses the residential customer charge and minimum bill, can we start with your understanding of the purpose of each?

A. Yes.

Q. What is a customer charge?

A. A common rate element for both electric and natural gas utilities is a monthly customer charge, although this charge is sometimes called a basic charge, basic service fee or other name. The idea here is that some costs vary directly by the number of customers and should be recovered in a per customer charge in order to track costs. These are costs that each and every customer causes to be incurred by the utility. Some customers may not use any energy in a given month, so a customer charge is a way to assure recovery of direct customer costs. Customer investment costs include meters and service lines. Customer expense items include depreciation of meters and service lines, meter reading, billing and payment processing. The use of a customer charge helps maintain intra-class equity. If customer costs are recovered through an energy rate, very low use customers end up being subsidized by other customers. If a customer uses very little energy each month, the energy charge likely will not recover all of the energy costs plus the direct customer costs. This means high-energy use customers would be making up the difference. Adding a separate customer charge that covers all direct customer costs avoids this problem.

Q. What is a minimum bill?

A. A minimum bill or minimum charge is normally intended to represent the amount of the direct customer charges discussed above. If a customer's bill calculated from the other rate elements (such as energy charges) is less than the minimum bill amount, then the customer's bill is the minimum bill amount. The purpose of this charge is to help assure that all customers pay for their direct customer costs. Yet when a customer is billed such a minimum charge, any energy consumed is basically free since only the direct customer costs are recovered. The only time such a minimum bill recovers the right amount of costs is when the kWh consumption is zero. Having a customer charge based on the full direct customer costs is therefore superior to having a minimum charge since in all cases the direct customer costs as well as other costs are recovered. Also, minimum bills only impacts less than 3 percent of PacifiCorp's Utah customers, while customer charges are paid by all customers. The reason for a minimum charge is when the customer charge is less than the full amount of the direct customer costs. If the customer charge covers all direct customer costs, then a separate minimum charge would not be necessary.

COMMENTS ON ABDINASIR M. ABDULLE'S TESTIMONY

Q. Dr. Abdulle lists the Division's rate design objectives as stable, simple, understandable and acceptable to the public, economically efficient, to promote fair cost apportionment of costs among individual customers within each customer class with no undue discrimination. Do you support these objectives?

A. Yes. I believe rate design, like other facets of the rate-setting process, should be guided by a number of objectives. I support the following objectives: recovery of the class revenue requirement; simple, understandable and acceptable to customers; rate stability; revenue stability; correct price signal; fair cost apportionment among customers within the class; ease of administration; economic efficiency; nondiscriminatory; and conservation of resources. James C. Bonbright indicates in his 1961 book, *Principles of Public Utility Rates*, that he derived such a list of rate-making objectives from a variety of sources including technical literature, reported opinions by courts and commissions and summary lists by a number of writers.

Class and total revenue requirement recovery is essential in rate design since the main purpose of rates is to price utility service such that the utility recovers its prudently incurred costs of providing that service.

Rates that are simple, understandable and acceptable to customers generate less confusion, questions and complaints and are more likely to achieve the desired customer response. I consider a correct price signal one that is cost-based. Bonbright states on page 294 of his aforementioned book, "Without doubt

the most widely accepted measure of reasonable public utility rates and rate structures is cost of service." Theoretically customers react to price signals. If the price signal (rate design) is complicated and difficult to understand, it is unlikely customers will react in the desired way. Therefore a complicated and confusing rate design is unlikely to provide a correct price signal even if the calculation is done right. If a rate design sends the correct price signal to customers, the customers can make their own economic decisions about how they consume utility services.

Rate stability means prices do not change frequently or by large amounts. Customers desire rate stability. Stable rates make budgeting easier for families and businesses. Customers have a difficult time understanding large rate increases that are not comparable percentage-wise to the changes in their own income or even with consumer price index changes. Rate design changes alone can result in significant rate increases for individual customers even if the class revenue requirement is unchanged. The principle of gradualism is often used to implement rate design changes in order to limit rate impacts. Utilities like revenue stability in the sense they want the revenue from customers to track the cost of providing service. A utility's fixed costs do not vary with unit energy sales, although revenues will vary if only a unit energy price rate design is used.

Fair cost apportionment among customers within a rate schedule is not always easy to achieve. A cost of service study is usually employed to determine the fair cost apportionment between rate schedules. Within a rate schedule, it is the rate design that determines how costs are apportioned among individual

customers. Theoretically, fair cost apportionment within a rate schedule requires a number of cost-based rate elements sufficient enough to accurately match each customer's cost of service with their bill. Since some utility costs vary during the day and over a year, time-of-day and seasonal pricing might be needed. Non-discriminatory rates are those that charge all customers with the same service characteristics the same price. These include service characteristics such as delivery voltage, maximum demand and total energy usage.

Economic efficiency refers to the efficient allocation of society's resources. Efficient resource allocation is achieved by basing rates on costs. Patrick Mann, while professor of economics at West Virginia University, stated in a 1977 article in *Public Utilities Fortnightly,* "Rate structures based on actual cost differentials tend to generate more allocative efficiency than rate structures based on noncost criteria." Economic theory states that marginal cost pricing is needed for economic efficiency. There are problems with using marginal costs for rate design. If marginal costs exceed average embedded costs, the utility could recover more than the revenue requirement. If marginal costs are less than embedded costs, the utility would be at risk of under-recovery of its revenue requirement. Therefore use of marginal costs in rate design must be balanced against the need to recover an embedded revenue requirement.

Energy conservation is achieved by correctly pricing incremental usage so as not to encourage wasteful use. Setting prices based on the underlying cost allows consumers to make their own decisions regarding energy consumption and conservation. Rates that accurately track costs often are complicated. Rates that

are easy to administer and are simple, understandable and acceptable to customers often do not accurately track costs. Rate design then must try to find the optimal balance of competing objectives

Q. Dr. Abdulle cites six guiding principles for rate design you developed while working for the Division and included in your testimony in Utah Power rate case 97-035-01. What is your current opinion of these guiding principles?

A. I originally developed these guiding principles as a way to help achieve the proper balance of the competing rate design objectives discussed above. My guiding principles he cited are: simple, correct price signal, multi-part rates, gradualism, marginal and embedded costs, and customer charges. I still believe these guiding principles are important and I fully support them.

Two very important guiding principles relevant for the customer charge are the correct price signal and customer charges. The correct price signal means if rates are correctly based on costs, customers can make the right decision about energy use including energy conservation decisions. In my testimony in case 97-035-01 cited by Dr. Abdulle, I also describe on page 8 the very important cost of service principle of cost causation. Cost causation is the principle that costs should be borne by those who cause them to be incurred. This is done not just because it is perceived to be fair, but to send a correct price signal to the consumer.

Customer charges should include costs that vary directly with the number of customers and are caused by each and every customer. Costs that generally increase with the number of customers, but are not caused by each customer

should be excluded from the customer charge and instead be included within the commodity portion of rates. This customer charge position was stated by the PSC in its Order in Mountain Fuel Case No. 82-057-15.

COMMENTS ON RONALD J. BINZ'S TESTIMONY

Q. Do you believe Mr. Binz's testimony indicates support for cost-based rates?

A. Yes. On page 9 of his direct testimony, he states, "…there are many considerations that go into rate making, only one of which is precise cost recovery on an element-by-element basis. Rate making must serve many purposes, some of which can be in conflict. In general, though, I agree that rates should be set to recover the underlying costs."

Q. Do you believe Mr. Binz's testimony supports the inclusion of the cost components PacifiCorp used in its calculation of the residential customer charge?

A. Yes. On page 10 of his direct testimony, he states, "I think the Company has appropriately limited its derivation of the customer charge to those costs that vary directly with the number of customers."

Q. Do you agree with Mr. Binz that the appropriate cost components were used by PacifiCorp in its calculation of the residential customer charge?

A. Yes.

Q. What is the basis for your agreement?

A. Since I began employment with the Division of Public Utilities in June 1980 and was directly involved with all Utah Power rate cases from 1983 through 2003, I would like to provide a history of the residential customer charge. I was the

Division witness that first recommended the $1.00 residential customer charge that the Commission adopted, and over time I, together with Margo Hovingh of the Committee, helped refine the approved list of included direct customer cost components in the calculation of the customer charge.

HISTORY OF THE RESIDENTIAL CUSTOMER CHARGE

Q. What was the rate design for Residential Rate 1 when you moved to Utah in 1980?

A. Utah Power Tariff 26, effective April 29, 1980, had Residential Rate 1 charges of 10.2029 cents per kWh for the first 60 kWh, 8.1654 cents per kWh for the next 140 kWh and 6.0201 cents per kWh for all additional kWh. There was also a minimum bill of $2.44 for single-phase service.

Q. With no customer charge, how were direct customer costs recovered?

A. Direct customer costs likely were recovered in the first kWh block and possibly in the second kWh block. The first kWh block was priced more than two cents per kWh higher than the second kWh block and more than four cents per kWh higher than the tail block.

Q. What conclusions do you draw from this rate design about customer costs?

A. With customer costs being recovered in the first and possibly the second kWh blocks, small-use customers using 100 to 300 kWh would probably have paid all direct customer costs.

Q. What was the impact on recovery of customer costs when the declining block rate design for Residential Rate 1 was replaced with a flat kWh rate in 1982?

A. Small-use customers no longer paid all direct customer costs since direct

customer costs were spread over all kWh. The use of a minimum bill would allow some cost recovery of direct customer costs, but not all.

Q. When was a customer charge added to the Residential Rate 1?

A. A $1.00 customer charge was added to Residential Rate 1 on July 1, 1985 by the Commission's order in Utah Power rate case 84-035-01. The Commission's order stated:

> Both Division witness Alt and Utah Power & Light witness Faigle testified that a customer charge furthers the objectives of revenue stability, equity and cost-based rates. Ms. Faigle and Mr. Alt also testified that the proposed customer charges included only those costs caused by the customer and that the Commission approved a customer charge for Mountain Fuel Supply Company, which included the same type of costs.

The Commission further stated, "No party to this case opposed the implementation of cost-based customer charges for the remaining schedules."

Q. Did the $1.00 residential customer charge represent the full direct customer costs?

A. No.

Q. Why then was only $1.00 implemented?

A. I testified in support of the reduced amount to alleviate rate impact. Following are statements from my direct testimony in that case:

> We recommend that customer charges be implemented for all rate schedules but at reduced rate where required to alleviate the adverse impact on small use customers. We believe, where necessary to soften the impact, the customer charge should be phased-in over a few years. This phase-in allows us to achieve a balance between the sometimes conflicting objectives of rate stability, revenue stability, equity and cost-based rates.

> I recommend that Residential Rates 1, 5 and 5A include a monthly customer charge of $1.00. This customer charge will result in more equity within the schedules while not imposing a significant adverse impact on small use customers.

The Commission in its July 1, 1985 order also stated:

> The Commission has previously made the finding (Mountain Fuel Supply Company Case No. 82-057-15) that a customer charge results in the payment by each customer of those costs that he imposes upon the system, which are independent of actual energy consumption during a given month. A customer of UP&L, who uses no electricity in a given month, must nonetheless have his meter read, be issued a billing statement and have his meter maintained in good operating condition. Those activities represent costs to UP&L. We find that a customer charge, as opposed to a minimum billing, allows such costs to be recovered reasonably and properly. The maximum increase any customer on Schedule No. 1 could experience would be 89 cents to 94 cents a month. Similarly, a $1.00 customer charge would reduce the energy rate for Schedules Nos. 1 and 5 only 0.17 cents to 0.058 cents. We conclude that a $1.00 customer charge is appropriate and should be imposed.

Q. What components were included in the calculation of customer charges in that case (84-035-01)?

A. The original customer charge components were first presented by Company witness, Shelley Faigle, in her rebuttal Exhibit No. SRF-2.2 in that case. The components included:

1. Account 903 - customer records/collections expense

2. Account 902 - meter reading expense

3. Account 586 - meter operating expense

4. Account 597 - meter maintenance expense

5. Meter depreciation expense

6. Service drop depreciation expense

7. Account 370 - meter plant

8. Account 369 - service drop plant

9. Meter accumulated depreciation

10. Service drop accumulated depreciation

11. Return on rate base

Similar customer charge components were used by PacifiCorp in this case with a few differences. The current cost components exclude operation and maintenance costs for meters and some customer collection costs and include a credit for billing service revenue.

Q. Why the differences?

A. As mentioned earlier, the list of direct customer cost components included in a customer charge was refined through the efforts of the Division and Committee after July 1985. This is covered later in the discussion of the Commission's April 10, 1992 Order.

Q. What happened to the residential customer charge after the July 1985 order?

A. There were no litigated Utah Power rate cases until the Commission initiated a new case in June 1989. There had been an earlier case that was withdrawn due to the merger of Utah Power and Pacific Power. The residential customer charge had been reduced from $1.00 to 94 cents by a uniform percentage rate reduction of all rate elements as a result of a merger credit. The $1.00 residential customer charge was reestablished by the February 9, 1990 Commission order in Case No. 89-035-10.

Q. What did the Commission next decide regarding residential customer charges?

A. In its April 10, 1992 order in Utah Power Case No. 90-035-06, the Commission stated, "The Division and the Committee presented unrebutted evidence and the Commission finds that residential customer-related costs are $2.15 per customer per month." In this case the Division and Committee agreed on the direct residential customer costs, excluding from the original list operation and maintenance of meters, some collection costs and added revenue credit from billing services. The Commission approval of the $2.15 direct customer costs was based on these adjustments.

The Commission left the customer charge at $1.00 stating, "The Commission attaches greater weight to other rate design objectives including an equal sharing of the schedule revenue reduction by all customers than to the recovery of all customer-related costs in a customer charge."

Q. What has happened since the 90-035-06 case?

A. The Commission made no changes to the residential customer charge in Utah Power Case No. 97-035-01, although the cost components for customer charges established in the previous case were reaffirmed. The Commission also made no changes to the residential customer charge in Utah Power Case No. 99-035-10. The next three Utah Power rate cases (01-035-01, 03-2035-02 and 04-035-42) were settled without any changes to the residential customer charge. The Commission in Case No. 01-035-01 approved a rate design stipulation that introduced a two-block inverted summer residential energy rate effective

November 2, 2001. The residential rate design had been a flat energy rate since 1982. The Commission in Case No. 03-2035-02 approved a stipulation that added a third inverted block to the residential summer energy rate for usage over 1000 kWh effective April 1, 2004. In Case No. 04-035-42, the Commission approved a stipulation that increased all residential summer energy block rates effective March 1, 2005.

Q. Please summarize what happened to the residential customer charge over the past 21 plus years.

A. On July 1, 1985 the Commission ordered a $1.00 residential customer charge, although full cost-based customer charges were approved for non-residential rates. On April 10, 1992 the Commission approved the customer direct costs calculation for all rate schedules, but left the residential customer charge at $1.00 (less than full direct customer costs). The March 4, 1999 Commission Order makes no changes to customer charges. The May 24, 2000 Commission Order makes no changes to the residential customer charge. The November 2, 2001, January 30, 2004 and February 25, 2005 Commission Orders approved stipulated settlements of Utah Power rate cases that included rate design and left the residential customer charge unchanged.

Q. What conclusions do you draw regarding the recovery of residential direct customer costs?

A. The residential declining block rate design prior to 1982 allowed recovery of direct customer costs from most customers. The change to a flat energy rate and no customer charge spread direct customer costs over all kWh and no longer

allowed recovery of all direct customer costs from most customers. The change in 2001 to an inverted two-block summer energy rate and the addition in 2004 of a third inverted block to the energy rate accentuated this problem. If the customer charge had been increased to include the full direct customer costs, these costs would be recovered from all customers.

CONTINUATION OF COMMENTS ON RONALD J. BINZ'S TESTIMONY

Q. Mr. Binz on pages 14-15 of his direct testimony recommends the residential customer charge be increased to $2.50 instead of the $3.40 proposed by the Company so that the impact on commodity rates will be more gradual. Do you agree with his concern about the impact on the commodity rates?

A. No. His concern seems to be that the kWh block rates will not be raised high enough since his recommended rates for those blocks are higher than that proposed by PacifiCorp. Even his contingent rates are higher than PacifiCorp for the second and third block rates. In my experience the gradualism principle is normally employed to mitigate the impact of rate increases to customers. His graph of impacts on page 14 of his testimony seems to imply that perhaps his real concern is for customers using less than about 500 kWh per month since his proposal would result in lower percentage impacts than PacifiCorp's proposal. However, higher percentage impacts for small use customers may be small in terms of dollars and cents.

COMMENTS ON ANTHONY J. YANKEL'S TESTIMONY

Q. Mr. Yankel on page 2 of his direct testimony states, "Rate Design should not be done without a sound knowledge of the cost causation principles, as well as a good understanding of other regulatory principles that come into play." Do you agree with this statement?

A. Yes.

Q. Mr. Yankel on page 7 of his direct testimony lists six regulatory principles to be used in rate design. Do you agree with his list of regulatory principles?

A. Not entirely. His list includes many of the objectives I listed earlier and those listed by Dr. Abdulle for the Division. His list does not include revenue stability or nondiscriminatory objectives. His first principle, "Promote economic and efficient use of electricity, while protecting the long-range interest of the consumers to obtain adequate levels of service at the lowest cost practical" appears to have added a new objective with the second part of the phrase. I would agree with the part, "Promote economic and efficient use of electricity" and believe it is included in my list of objectives. The remaining part, "while protecting the long-range interest of the consumers to obtain adequate levels of service at the lowest cost practical" is not quite so clear as to what is intended. If this objective's intent is simply to try to use incremental or marginal costs in the rate design to help send a better price signal, then I would support it. If it has been added to support the Committee's position that direct customer-related costs should be added to energy and demand costs for recovery in a commodity rate to discourage increased energy use, then I would not support it. To me pricing rate

elements at cost is what is needed to promote economic and efficient use of electricity. This sends the correct price signal to consumers for any energy consumption. It tells the consumer what the cost of energy consumption is and lets the consumer make his or her own decisions. To add direct customer costs on top of the demand and energy costs is a distortion of the price signal and tells the consumer that increased energy use costs more than it really does. To do this in order to meet an objective of lower long-range costs to all consumers is akin to making decisions for the consumer instead of pricing the commodity correctly and letting the consumer make his or her own choices. This is not following the cost-causation principle that says costs should be borne by those who cause them to be incurred. It is more like saying that those who cause the costs should pay those costs plus some extra costs (caused by others).

Q. Mr. Yankel on page 17 of his direct testimony describes the disadvantages of a customer charge. Do you agree with his description?

A. No. He states, "The disadvantage of a Customer charge over the Minimum charge is that the more that is collected in the Customer charge from all customers, the less of the total class revenue requirement will be collected in the energy rates." He goes on to say that if the $3.40 customer charge is imposed, $25 million annually would be removed from the energy charges, resulting in the Commission directionally moving away from addressing a growing peak demand problem. Reducing the amount collected in the energy charge does not necessarily correlate to the peak demand issue. He implies that the more costs that are loaded into the energy charge, the better, without regard to any cost basis

for doing so. His testimony does not present evidence that the $25 million properly belongs in the energy charge on a cost basis or that the energy impacted is energy at the time of peak. PacifiCorp has presented evidence to support a cost-based customer charge. A growing peak demand causes demand-related costs. Mr. Yankel has not identified how much these demand costs are. On page 2 of his direct testimony in discussing regulatory principles, he mentions "the importance of cost causation" yet here he seems to stray from that principle. He does not claim that PacifiCorp's calculated $3.40 of direct customer costs is incorrect, yet he says collecting those costs in a customer charge is a disadvantage. I believe having cost-based rate elements in a rate design is an important rate design objective and not a disadvantage when implemented. To do otherwise sends a distorted price signal to customers about their energy consumption. A distorted price signal, lacking a cost basis, does not promote economic and efficient use of electricity.

Q. Mr. Yankel on page 17 of his direct testimony says there is no need for both a customer charge and a minimum charge. Do you agree?

A. If the customer charge is based on the full direct customer costs as I described earlier, then I agree there is no need for a separate minimum charge. If however, the customer charge recovers less than the direct customer costs (as it currently does at 98 cents), then I believe there should also be a separate minimum charge. A separate minimum charge allows for more of the direct customer costs to be recovered from those that cause them to be incurred. With the current customer charge and no minimum charge, customers using little or no energy would be

subsidized more by the other customers than they would with a minimum charge. The use of the minimum charge and a customer charge less than full direct customer costs allows customers using little or no energy to pay less than the cost to serve them. Other customers pick up the shortfall. This subsidization of small use customers will continue until the customer charge includes all the direct customer costs.

Q. Mr. Yankel on 17 of his direct testimony says residential customers have no control over the monthly customer charge. Do you agree?

A. No. Each residential customer made the choice to get electricity from the utility. Once that choice was made, the utility started incurring customer-related costs for that customer. The utility then has very little control over those customer costs, as it is required to provide service and maintain an account and read meters and bill for service. These customer costs do not vary with a customer's energy use but continue as long as the customer chooses to continue service.

Q. Mr. Yankel on page 18 of his direct testimony proposes "that there be no increase in the Customer Charge (consistent with its 20 year history) so that as much emphasis can be placed on the energy rate structure (and preferably the tailblock) as possible." Do you agree?

A. No. He is proposing to place as much emphasis, as possible, on the energy rate without any evidence of a cost basis. He is even proposing to keep most direct customer costs in the energy rate, which if it were cost-based would not include any direct customer costs.

Q. Mr. Yankel on page 19 of his direct testimony says "The average of what other utilities charge should not serve as a basis for increasing the Residential Customer charge in this case". Do you agree?

A. Yes. I think customer charges should be cost-based. Each utility has its own costs. PacifiCorp's current residential customer charge in Utah is less than the direct customer costs and should be increased on that basis alone. The fact that other utilities in Utah have customer charges shows that customer charges are common and customers by now should be more used to them. Questar Gas has had a $5.00 monthly customer charge for many years and it serves most of PacifiCorp's Utah customers.

Q. Mr. Yankel on page 31 of his direct testimony says "the present rates are not sending a strong enough signal" and uses this as a reason to either not change or to decrease the residential customer charge. Do you agree?

A. No. He says the present rates are not sending a strong enough signal, but offers no evidence to support such a claim. In my opinion the proper signal is a cost-based price signal and not one with an artificial increase based on an unproven assumption that the signal is not high enough. He does not say how high the signal should be and does not offer cost data to support such a price. He simply says to keep direct customer costs in the energy rate to keep it as high as possible. He speaks of the importance of cost-causation regulatory principles in rate design, but seems to abandon them with his recommendations.

COMMENTS ON ELIZABETH A. WOLF'S TESTIMONY

Q. Ms. Wolf on page 4 of her direct testimony says PacifiCorp's customer charge proposal is unsound ratemaking because more revenue is guaranteed. Do you agree?

A. No. Common ratemaking objectives include revenue stability as well as intraclass equity. Both of these objectives support a cost-based customer charge.

Q. Ms. Wolf on page 5 of her direct testimony says any increase in the customer charge should be made more gradually. Do you have any comments?

A. She does not challenge the $3.40 residential customer charge calculation, but simply says any increase should be gradual. In 1985 when I first recommended the $1.00 residential customer charge, I fully intended that it be increased in steps of about a $1.00 until all direct customer costs were included. I intended this would happen in just a few years depending on the calculated direct customer costs. That did not happen for various reasons. There was a gap of a few years before there was another Utah Power rate case, then the merger case arrived followed by a period of rate reductions. The Commission in its orders decided not to increase the customer charge in a period of rate reductions. Later several rate cases were presented to the Commission as stipulated settlements with no change in the residential customer charge. It has been 21 plus years since the first $1.00 customer charge was implemented. At that time the Commission found that a $1.00 increase was an acceptable impact on customers. Today after 21 plus years of inflation, an increase of $1.89 per month to the customer charge would have the same impact as the $1.00 increase had in 1985. Also, the movement of

direct customer costs from the energy rate to the customer charge would further reduce the impact on small energy users by allowing a lower energy rate than otherwise. So, an increase in the monthly residential customer charge from $0.98 to $3.40 would have an impact not significantly more than when the customer charge was first implemented in 1985.

Q. Ms. Wolf on pages 6-7 of her direct testimony says increasing the customer charge rather than putting the increased charges in the energy portion of the bill hides the real cost of energy and that this sends the wrong price signal and impedes conservation. Do you agree?

A. No. I believe the appropriate regulatory policy in rate design is to send correct price signals based on cost. I believe in multi-part rates with each rate element based on cost. Having a customer charge that is based on direct customer costs is the correct price signal and improves intraclass equity. She does not challenge the accuracy of the $3.40 direct customer costs. Putting those direct customer costs in an energy rate is hiding the customer costs in the energy rate. The real cost of energy is being distorted by adding in direct customer costs that are not impacted by energy usage. She does not offer evidence as to what the real cost of energy is and therefore what the correct price signal should be. With respect to energy conservation, I believe the best policy is to send a correct price signal by basing rates on costs and letting consumers make their own choices about energy consumption. Even the Public Utility Regulatory Policies Act of 1978 ("PURPA"), enacted in response to a national energy crisis, imposed rate making standards that sought cost-based rates. I was the witness for the Division in 1981

and supported adoption of the PURPA Declining Block Rate Standard, which basically said any declining block energy rate had to be cost-based. The Commission adopted this rate making standard. It seems reasonable to me that an inverted block energy rate also ought to be cost-based.

SUMMARY

Q. Please summarize your conclusions and recommendations regarding the residential customer charge.

A. I believe it is reasonable for the Commission to implement the $3.40 residential customer charge for the following reasons:

1. The $3.40 residential customer charge is based on the direct customer costs that the Commission has previously approved for inclusion in a customer charge. These are the costs that vary directly with the number of customers.
2. The same direct customer cost components have been used to calculate customer charges for the non-residential rate schedules for many years and no party opposes them.
3. No party opposes the calculation of the $3.40 residential direct customer costs.
4. The implementation of a $3.40 residential customer charge will allow elimination of the minimum charge since all direct customer costs will be recovered from all customers. This will simplify the rate design.
5. Impeding conservation is not a valid argument as a cost-based rate sends the correct price signal and allows customers to make their own decisions regarding energy consumption. Even PURPA sought cost-based rates. Even

with a cost-based customer charge, the energy rates will still be increased.

6. Changing of the residential rate design from a declining block energy rate to a flat energy rate without a cost-based customer charge allowed many customers to escape paying all direct customer costs. The introduction of inverted two and three block energy rates accentuated the problem.

7. A gradual movement to cost for the residential customer charge never happened over the 21 plus years since the $1.00 customer charge was implemented for various reasons explained earlier. The current customer charge of 98 cents is actually 2 cents lower than it was in 1985

8. The rate impact in dollars of implementing the $3.40 residential customer charge is not significantly higher than the impact of the implementation of the first $1.00 customer charge due to 21 plus years of inflation. Further gradual movements to cost are not necessary.

Q. Does this conclude your direct testimony?

A. Yes.