

Docket No. 06-035-163  
Docket No. 07-035-04  
Docket No. 07-035-14  
DPU DTT Exhibit No. 1.0 SR  
David T. Thomson  
October 22, 2007

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**BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH**

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| In the Matter of the Application of Rocky Mountain Power, a Division of PacificCorp, for a Deferred Accounting Order To Defer the Costs of Loans Made to Grid West, the Regional Transmission Organization | : |                       |
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| In the Matter of the Application of Rocky Mountain Power for an Accounting Order to Defer the Costs Related to the MidAmerican Energy Holdings Company Transaction   | : | Docket No. 06-035-163 |
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| In the Matter of the Application of Rocky Mountain Power for an Accounting Order Costs related to the Flooding of the Powerdale Hydro Facility   | : | Docket No. 07-035-04  |
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|  | : |                       |
|  | : | Docket No. 07-035-14  |
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**SURREBUTTAL TESTIMONY**

**OF**

**DAVID T. THOMSON  
STATE OF UTAH  
DIVISION OF PUBLIC UTILITIES**

**OCTOBER 22, 2007**

1 **Q. Please state your name and business address for the record.**

2 A. David T. Thomson. My business address is Heber M. Wells Building 4<sup>th</sup> Floor,  
3 160 East 300 South, Salt Lake City, Utah 84114-6751.

4 **Q. Are you the same David T. Thomson who previously offered pre-filled direct**  
5 **testimony in this case?**

6 A. Yes, I am.

7 **Q. What is the purpose of your surrebuttal testimony?**

8 A. In my surrebuttal testimony, I will address the rebuttal testimony of Rocky  
9 Mountain Power (“RMP”). Specifically, I will address the rebuttal testimony  
10 regarding general deferred accounting policy and the rebuttal testimony on the  
11 disputed deferred accounting applications.

12 **DEFERRED ACCOUNTING POLICY**

13 **Q. Mr. Larsen believes that an event must not always be unforeseen to qualify**  
14 **for deferred accounting treatment and that the Utah Public Service**  
15 **Commission (“Commission”) has approved deferred accounting treatment**  
16 **for items unforeseen. What are your observations about the Division’s**  
17 **guideline concerning an event being unforeseen?**

18 A. I agree that there have been some cases where deferred accounting treatment was  
19 granted for foreseen items. The Division’s guidelines (DPU exhibit 1.1) suggests  
20 granting deferred accounting to costs with future benefits subject to certain  
21 conditions as outlined in Item III of those guidelines. However, such costs are to

22 be connected to a rate case. (See item IV of the guidelines). Mr. Larsen's  
23 example of foreseen costs with future benefits being granted deferred accounting  
24 treatment in the 1999 rate case is a good example. Foreseen events that have a  
25 future net benefit would qualify for deferred accounting inside a rate case setting.  
26 That is why the Commission granted differed accounting to Y2K expenditures,  
27 costs associated with the Noel Kempf Climate project, reengineering costs, and  
28 the Glenrock Mine Closure. They were foreseen or known costs in a rate case  
29 setting that met deferred accounting guidelines.

30 It would be normal to have such deferred costs addressed and the  
31 accounting determined in a rate case setting. Also, because it was in a rate case  
32 with a Commission Order implementing a regulatory asset for deferred  
33 accounting, the proper amortization term, starting date for the amortization, and  
34 recovery amount was determined. A separate deferred accounting order is not  
35 needed.

36 As I stated in my prior testimony the Division believes that to qualify for a  
37 **deferred accounting order** outside of a rate case costs must be unforeseen. If all  
38 foreseen costs are included in a rate case filing then there is no need for a deferred  
39 accounting order. Y2K expenditures and the other costs in the 1999 rate case did  
40 not need a deferred accounting order because they were handled properly as  
41 foreseen deferred costs in a rate case with a **historical test year**.

42           In his rebuttal testimony Mr. Larsen, notes that the Utah Supreme Court  
43 established that rates may be adjusted retroactively if an event is unforeseeable  
44 **and** extraordinary. It does not state unforeseeable **or** extraordinary. If it was not  
45 both unforeseen and extraordinary it should be handled through normal  
46 accounting or ratemaking methods and would not require a deferred accounting  
47 order. Another prohibition for retroactively adjusting rates is when the estimates  
48 of cost and revenues prove to be inaccurate and costs are either higher or lower  
49 than predicted. Retroactive ratemaking by retroactively adjusting rates when the  
50 estimates of cost and revenues prove to be inaccurate and costs are either higher  
51 or lower than predicted is prohibited. I believe this is prohibition against  
52 retroactive ratemaking is especially applicable to rates set by a Commission Order  
53 after a rate case hearing using a future test year.

54           In summary, the Company, in the Division's view, is inappropriately  
55 attempting to use deferred accounting to correct a misstep in predicting costs,  
56 revenues, or rates. Disallowing the use of deferred accounting to correct such  
57 missteps, would help to ensure that extra care would be taken so that the future  
58 test year predictions were as correct as possible.

59 **Q. What is your response to Mr. Larsen's rebuttal testimony on materiality?**

60 **A.** I have only two things more to say about materiality. First, I would like to clarify  
61 that the Division believes the burden of proof as to materiality should rest with the  
62 applicant for events under a 5% threshold of income before extraordinary items.

63 Anything over the 5% threshold would most likely be material. Second, the use  
64 of Mr. Larsen's "rule of thumb" as outlined in his rebuttal testimony lines 97-103  
65 would be a considerable help in a deferred accounting order application filed by  
66 the Company to determine if the event's costs are material. In addition, it would  
67 also have been helpful to have the Company's input and thoughts on a percentage  
68 threshold for materiality. However, the Company did make it clear that in its  
69 opinion a 5% threshold was too high. I would like to note, that for Master Data  
70 requests under the last rate case the Company agreed to materiality defined as a  
71 change in requested state revenue requirement equal to or greater than 0.02% of  
72 total state revenue requirement or \$250,000, whichever is greater.

73 As noted above in the 1999 rate case, deferred accounting treatment for  
74 certain events with small materiality levels were granted. The Division believes  
75 that a larger percentage threshold is warranted for deferred accounting orders  
76 outside of a rate case. The Division thought that a 5% threshold was a good  
77 starting point.

78 I would also like to emphasize that a regulatory asset affects expenses and  
79 operating income because the asset cost is amortized yearly into the operating  
80 expenses of the Company.

81 **Q. Mr. Larsen disagreed with two additional guidelines in Exhibit 1.1. What is**  
82 **your response to Mr. Larsen's comments?**

83 A. The Division does not propose that deferrals only be allowed for events that  
84 provide net benefit for ratepayers. Under the guidelines attached to my testimony,  
85 events that are extraordinary and unforeseen would qualify for deferred  
86 accounting. (See Section I of DPU Exhibit 1.1.) The Division believes the  
87 Powerdale flood was extraordinary **and** unforeseen and thus qualifies for deferred  
88 accounting even though it does not have a net future benefit. The amortization  
89 length would be set without matching to future benefits because there are none.  
90 Second, the Division's guideline for earning over the Utility's allowed return is in  
91 its guidelines. (See DPU Exhibit 1.1 part IV items A, B & C.) Under the  
92 guidelines a rate case must be filed for recovery of the deferral to be considered  
93 and the rate case will consider 1. Was the utility earning over its allowed return.  
94 2. Have shareholders been compensated. 3. Insurance or other methods of  
95 recovery. 4. Prudence and reasonableness of expenditures. 5. Rate base or other  
96 carrying cost treatment.

97 **Q. After reading Mr. Larsen's rebuttal testimony under his deferred**  
98 **Accounting Policy Section do you have any additional comments?**

99 Yes, Mr. Larsen's rebuttal testimony has clarified a major problem with deferred  
100 accounting and deferred accounting orders associated with a "black box"  
101 stipulated settlement.

102 **Q. Would you please explain?**

103 A. A little background will help to put my comments into context. In response to the  
104 following question in his rebuttal testimony,

105 Do you agree with Ms. DeRonne's assertion that labor cost  
106 associated with the Company's participation in Grid West are no  
107 longer being incurred while the costs remain in rates? (Rebuttal  
108 testimony lines 296-298).

109  
110 Mr. Larsen answered,

111 No. First, the current revenue requirement was established through  
112 a black box settlement so any reference as to what costs are or are  
113 not included in rates is without foundation. (Rebuttal testimony  
114 lines 299-301).

115  
116 And in response to the following question in his rebuttal testimony,

117 Mr. Thomson, Ms. DeRonne, and Mr. Higgins all suggest that  
118 because the Company filing in the last rate case did not project the  
119 total amount of labor cost savings, current rates are over  
120 recovering actual labor costs. Is this assessment correct? (Rebuttal  
121 testimony lines 375-378).

122  
123 Mr. Larsen answered,

124 No, it is incorrect on several levels. First, as I explained  
125 previously in my rebuttal testimony, the current revenue  
126 requirement was established through a black box settlement so any  
127 reference as to what costs are or are not included in rates, or even  
128 whether a historical or forecasted test year was used, is without any  
129 foundation. (Rebuttal testimony lines 379-383).

130  
131 The Dictionary defines foundation as a basis upon which something  
132 stands or is supported.<sup>1</sup> Thus, something without any foundation has no basis to  
133 stand upon or is unsupported. I will now quote from various parts of Mr. Larsen's

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<sup>1</sup> The Merriam –Webster Dictionary. 1998 Copyright.

134 rebuttal testimony and add my comments based on the above answers. Mr. Larsen  
135 stated:

136 Rather, only the amortization expenses and the remaining  
137 unamortized balance of a deferred expense or revenue that carry  
138 through to the test period (whether it is historic or forecast test  
139 period) in the utility's next general rate case will be included in the  
140 revenue requirement at that time. (Rebuttal testimony lines 145-  
141 148).

142  
143 I note that any deferred expense or revenue amount that is carried forward from a  
144 black box settlement is unknown and is without any foundation. Any remaining  
145 unamortized balance is unknown and if any amount is chosen or used it is without  
146 foundation.

147 Mr. Larsen also said:

148 If amortization of the assets begins during the current rate effective  
149 period, as is proposed by the Company in the case of Grid West  
150 loans and the MEHC severance costs, the utility foregoes any  
151 opportunity to recover the portion of those costs that are booked to  
152 expense during the period. (Rebuttal testimony lines 141-145).

153  
154 In response to that statement, I comment that the assumption that assets exist for  
155 the above events and that the Company is foregoing any opportunity to recover  
156 the portion of those costs for a rate effective period using a black box settlement  
157 is unknown and without foundation.

158 Additionally, Mr. Larsen said:

159 A normalized level of cost includes not only the deferral of  
160 unusual expenses incurred during a given year, but also the  
161 amortization of unusual costs that occurred in previous years.  
162 (Rebuttal testimony lines 180-182).  
163



164 In response to this statement, I comment that if the previous years were covered in  
165 a black box settlement, then whether there were unusual costs that occurred in  
166 rates is unknown and the setting up and amortizing such costs is without  
167 foundation. What was booked to expense during the period is unknown and  
168 without foundation.

169 Next, Mr. Larsen stated:

170 To the contrary, the Company is simply requesting to defer and  
171 amortize an expense that would normally be properly amortized  
172 over a period of time, as opposed to being absorbed in a single  
173 period. (Rebuttal testimony lines 227-229).  
174

175 In response I note that under a black box settlement whether or not a cost was  
176 absorbed in a single year or not is unknown and to assume that it was or was not  
177 included is not known along with the expense amount and to make any  
178 assumption otherwise is not possible and to do so is without foundation.

179 Also, Mr. Larsen stated:

180 Future rates will only be impacted to the extent any remaining  
181 deferred balances and associated amortization expense continues  
182 through the test period of the next general rate case. (Rebuttal  
183 testimony lines 240-242).  
184

185 I must respond that continuing any assumed deferred balances and associated  
186 amortization expense amounts from a black box settlement to the next general rate  
187 case is without foundation and to try and do so is not possible because the proper  
188 amounts can not be determined.

189 Finally, Mr. Larsen stated:

190 This proposed deferral and amortization of these costs are the same  
191 as if they had been included in the last rate case. The only  
192 difference is that the amortization expense is not being recognized  
193 in current rates and may not have been considered by parties in  
194 their settlement positions. When new rates are set, the amount of  
195 remaining unamortized costs to be considered for recovery will be  
196 the same as if the deferral had been (sic) included in the last case.  
197 (Rebuttal testimony lines 243-248).  
198

199 I note that because of the black box settlement, one does not know whether the  
200 costs to be deferred and amortized were included in the last rate case nor is the  
201 cost amount known. So any comment from that point on in the answer is without  
202 merit and foundation.

203 It appears to the Division, based on the above comments, it is not possible  
204 to “roll” costs or revenue amounts for specific items out of a black box settlement  
205 unless such costs are specifically addressed in the stipulation. Could this be the  
206 reason that regulatory assets that were set up prior to the stipulation were  
207 specifically address in the stipulation per Company request? - In Appendix I of  
208 the Commissions Report and Order - Docket 06-035-21 under the heading *Terms*  
209 *of Stipulation* – item 14 - it states,

210 Regulatory Assets. Certain expenses incurred by the Company  
211 have been deferred as regulatory assets on the Company’s balance  
212 sheet. This Commission has previously issued orders allowing the  
213 deferral and amortization of regulatory assets and subsequent  
214 recovery in rate proceedings. This Stipulation does not alter or  
215 impair the recovery of these regulatory assets previously deferred  
216 by Utah Commission orders under FAS 71.  
217

218 If this provision was not in the stipulation then one could argue that any  
219 regulatory assets and their related amortized costs that “rolled” into the stipulation

220 could have been altered or impaired by the black box settlement. Not knowing  
221 whether they were altered or impaired would have called any further accounting  
222 and expense amortization into question because such amounts would be without  
223 foundation. However, since they were mentioned in the stipulation they were able  
224 to “roll” into and out of the black box settlement. The only events that would not  
225 have this “without foundation” dilemma are events that are extraordinary and  
226 unforeseen or items and events specifically mentioned in the stipulation.

227 If not mentioned in the stipulation, Commission authority is required to  
228 roll them out of the black box. The Company is aware of this dilemma. In Mr.  
229 Larsen’s rebuttal testimony he states the following,

230 This supports the rationale for the Company’s request. Because the  
231 stipulation in the last case did not call out specific revenue requirement  
232 elements, including the deferred accounting treatment of the severance  
233 costs, separate Commission authority is requested to establish a regulatory  
234 asset. All the Company is requesting for this portion of the severance  
235 costs is to formalize the treatment that was requested in the last rate case.  
236 (Rebuttal testimony lines 328 to 333).

237  
238 It is the Division’s position that this is not a simple request but raises numerous  
239 concerns for the Division. Would this not be single item ratemaking? Would this  
240 not be retroactive ratemaking? It is the Division’s opinion that this is opening up a  
241 black box settlement to “cherry picking” by formalizing specific items out of a  
242 settlement that have no foundation unless given such by the Commission, after the  
243 fact of settlement, through a deferred accounting order. Once the black box is  
244 opened, for fairness, all parties to the black box settlement should now be given

245 opportunities to revisit costs and revenues of the settlement for proper cost  
246 recovery due to new information or missed costs or missed projecting that comes  
247 to light after the settlement was signed. Couldn't this be interpreted as a back  
248 door approach to opening up a black box settlement? Shouldn't all parties accept  
249 the inherent risks of a back box settlement and move forward with the agreed  
250 upon amount with out modification?

251 The Division believes that the Grid West costs and the severance costs  
252 were not extraordinary and unforeseen. Being foreseen, the timing is such that  
253 their costs should be in the black box settlement period. If not, then there was a  
254 regulatory misstep and to address such costs now in a deferred accounting order  
255 application is not proper (retroactive ratemaking) and not possible if such events  
256 had a starting point and projected costs (whether under or over projected it  
257 matters not) that were in a rate effective period covered by a black box settlement.  
258 The deferred accounting applications should be denied due to the simple fact that  
259 there is no foundation for the accounting that would be required under the order.  
260 The settlement provides no foundation for costs and revenue details but only takes  
261 into account a total revenue requirement amount.

262 If deferred accounting was granted, parties could, and probably would,  
263 argue that the formalized treatment was unfair unless all parties could argue rate  
264 recovery as part of the process. In actuality, some of that has already gone on in  
265 these dockets, making them not a simple matter of approving a deferred

266 accounting order but have grown into a mini-rate case. All parties have put forth  
267 arguments on why the Grid West and MEHC severance costs qualify or don't  
268 qualify for rate recovery, suggested amortization terms and start dates, and other  
269 regulatory matters and policy even though the applications started out by simply  
270 asking for a deferred accounting order.

271 The deferred accounting applications for Grid West and the MEHC  
272 severance costs in the Opinion of the Division have the following problems. First,  
273 it is a back door method to open a black box settlement and is cherry picking costs  
274 that were not affirmed in the original black box settlement stipulation and moving  
275 them out of the black box to a future rate case. Second, it is retroactive  
276 ratemaking if additional costs are trying to be recovered in future rates that were  
277 missed or not outlined in the black box settlement. Third, to open a black box  
278 settlement in this matter is bad regulatory policy because to determine the amount  
279 to be affirm by the Commission would require a mini-rate case (because of the  
280 without foundation problem) so that all parties could argue recovery amount,  
281 deferred guidelines, amortization starting point, and amortization terms. This is  
282 basically single item ratemaking. Fourth, it undermines the good faith efforts of  
283 the parties to the settlement and calls into questions all kinds of concerns as to  
284 risk and risk shifting under a black box settlement. Fifth, if this was not a black  
285 box situation there would be no need for a deferred accounting order. The  
286 deferred costs in the filed future test year rate case would be affirmed in a

287 Commission order after hearings and the accounting would then carry on to the  
288 next rate case.

289 The deferred accounting from the “black box dilemma” is such a major  
290 problem that it overshadows all other deferred accounting considerations.  
291 Therefore, the Division will not address its individual responses to rebuttal  
292 comments from the Company for the Grid West and MEHC severance  
293 applications. Because of the above reasons that any deferred accounting for the  
294 Grid West and MEHC severance costs rolling out of a black box settlement would  
295 be without foundation, would violate numerous regulatory prohibitions and that  
296 application or implementation would probably prove not possible or unworkable  
297 without moving forward with a mini rate case scenario that sets recovery amount,  
298 starting point and term for the deferred amounts trying to be rolled out of the  
299 deferred accounting order, the Division reiterates its position that the Grid West  
300 and MEHC severance cost applications should be denied.

301 **Q. Does the Division have any additional comments pertaining to the PowerDale**  
302 **application?**

303 A. No, not at this time. As stated in its direct testimony, the Division will review the  
304 Company’s deferred accounting for the Powerdale application in the next rate  
305 case and will issue its comments about such accounting at that time.

306 **Q. Does this conclude your Testimony?**

307 A. Yes.