BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

In the Matter of the Application of Rocky Mountain Power for Approval of its Proposed Energy Cost Adjustment Mechanism)	Docket No: 09-035-15
In the Matter of the Application of the Utah Association of Energy Users for a Deferred Accounting Order Directing Rocky Mountain Power to Defer Incremental REC Revenue for Later Ratemaking Treatment)	Docket No: 10-035-14

TRANSCRIPT OF HEARING PROCEEDINGS

TAKEN AT: Public Service Commission
160 East 300 South
Salt Lake City, Utah

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TIME: 9:02 a.m.

REPORTED BY: Kelly L. Wilburn, CSR, RPR

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Ric Campbell
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WITNESSES

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AUGUST 17, 2010 9:02 A.M.

P R O C E E D I N G S

CHAIRMAN BOYER: This is the time and place duly noticed for the hearing of portions of Phase II of Docket No. 09-035-15, captioned: In the Matter of the Application of Rocky Mountain Power For Approval of Its Proposed Energy Cost Adjustment Mechanism.

The focus on this portion -- we divided, or bifurcated if you will, portions of Phase II in this docket at the request of the parties. And today we'll be hearing testimony on hedging and reliance on market purchases. And then the next phase we'll deal with design elements as we move forward in this particular docket.

I guess we'll conduct this hearing like we normally do, beginning with the Company as the moving party. And we will hear then from the Division witnesses, Office witnesses, and WRA, and UAE, and UIEC, I guess. In that, in that order. Just because it's easier for me to keep track of people that way.

Let's take appearances for the record, please, beginning Mr. Monson and Ms. Hogle.

MR. MONSON: Gregory Monson and Yvonne Hogle for Rocky Mountain Power.

CHAIRMAN BOYER: Thank you. Welcome.

Ms. Schmid?

MS. SCHMID: Patricia E. Schmid, with the Attorney General's Office, for the Division of Public Utilities.

CHAIRMAN BOYER: Okay. Mr. Proctor?

MR. PROCTOR: Paul Proctor on behalf of the Office of Consumer Services.

CHAIRMAN BOYER: Thank you.

MS. HAYES: Sophie Hayes on behalf of Western Resource Advocates and Utah Clean Energy.

CHAIRMAN BOYER: And how is that spelled, H-a-y-e-s?

MS. HAYES: Uh-huh.

CHAIRMAN BOYER: Okay. Mr. Dodge?

MR. DODGE: Gary Dodge on behalf of UAE.

MR. EVANS: William Evans on behalf of the Utah Industrial Energy Consumers.

CHAIRMAN BOYER: Very well. Since there are no preliminary matters let's begin with the Company's first witness. I should tell you, though, in terms of how we're going to unfold, we have a teleconference at 3:00. So we will at least be planning on taking a short recess at that point in the afternoon.

And with that part of the interruption, Mr. Monson or Ms. Hogle?

MR. MONSON: Our witness is Greg Duvall. And are we not gonna re-swear people, I guess, because we're still in the same docket?

CHAIRMAN BOYER: We are still in the same docket, although I don't know that all witnesses have been sworn.

MR. MONSON: Okay.

CHAIRMAN BOYER: I think Mr. Duvall has.

THE WITNESS: I certainly have.

CHAIRMAN BOYER: You certainly have.

He's been sworn and sworn at.

GREGORY DUVALL,
called as a witness,
having previously been duly sworn,
was examined and testified as follows:

DIRECT EXAMINATION

BY MR. MONSON:

Q. Mr. Duvall, please state your name and your position?

A. My name is Gregory M. Duvall, and I am the director of long-range planning and net power costs.

Q. And have you prepared, for this portion of the case, rebuttal testimony that has been filed with the Commission, including one highly-confidential exhibit and also your testimony is highly confidential; is that right?

A. That's correct.

Q. Do you have any corrections you wish to make to that testimony?

A. No, I do not.

Q. If I were to ask you the questions that are set forth in your testimony today, would your answers be the same as provided?

A. They would.

THE REPORTER: I don't think, I don't think his microphone is on. If you could check that, please?

THE WITNESS: Is it on now? It's on now, yes.

Q. (By Mr. Monson) Do you have a summary of your testimony?

A. Yes, I do.

Q. Please present that.

A. On July 20, 2010, I filed rebuttal testimony on the issues raised by the Commission in its February 10, 2010, report and order on Phase I of this proceeding. Namely, is the Company's use of natural gas hedging and the level of and reliance on market energy affected by the use of an ECAM.

On market reliance, the level and the

reliance -- the level of and reliance on market energy has delivered significant cost savings to Utah customers that are already reflected in rates.

The Company's level of reliance on market purchases was reduced in the 2008 IRP update as compared to the 2008 IRP. It's also consistent with the level of -- that was forecast in establishing base net power costs in our last general rate case.

Part of the evidence that I present is from the 2008 All Source RFP and is highly confidential, so I won't discuss the specific results in this summary. However, review of the evidence demonstrates the customers will realize substantial net present value benefits from the Company's decision to cancel the Lakeside II project that was selected as a result of the 2012 RFP, and instead rely on market purchases during the bridging period.

On hedging, the Company's hedging program has provided benefits to Utah customers by reducing the risk of net power costs being substantially higher than forecast, and the benefits are already reflected in rates.

The Company's provided substantial information regarding its hedge -- hedging program previous -- previously in this docket and other dockets through testimony and workshops. This information demonstrates that the Company has a sophisticated and well-managed hedging program that reduces customer exposure to power and fuel price volatility.

None of the parties have demonstrated that the Company's level of market reliance on its hedging for its hedging programs have harmed customers in the past or will likely harm them in the future. Mr. Wheelwright, however, presents an analysis in his surrebuttal testimony that attempts to show that there was some harm.

I claim that that analysis is misguided. It is only looking at swaps, it's not looking at all of our hedges. If you look at all of the hedges -- which his testimony actually purports that it does, but it doesn't. If you look at all of them you'll find that there's been substantial gains.

Since current rates already reflect the Company's market reliance on hedging, an ECAM is merely a mechanism to true up the actual amounts of market reliance and hedging to what's already in rates.

As directed by the Commission in its acknowledgment order of the 2008 IRP, the Company is committed to evaluate both of these issues in its 2011 IRP. And agrees that Mr. Wheelwright's suggestion that there be annual review of hedging in conjunction with fewer IR -- future IRPs is a sensible plan.

The 2011 IRP is scheduled to be filed on March 31st of 2011, or just seven months from now. I recommend that no further studies need to be conducted prior to implementing the ECAM.

Because of these facts I recommend the Commission conclude that there is no need to require the Company to adjust its reliance on market energy and its hedging program with the adoption of an ECAM.

I further recommend the Commission reject the suggestions of the other parties that an ECAM not include all front office transactions, hedging costs, or natural gas fuel costs. Exclusion of these highly volatile and interrelated components of net power costs from an ECAM would defeat the purpose of the ECAM.

I recommend the ECAM be run as a pilot program through 2013, with a review that would take place during 2013 allowing it to become permanent in 2014 with any adjustments that may be ordered by the Commission as a result of that review proceeding.

The remainder of my testimony addresses a number of issues raised by the parties that I simply did not want to leave unrebutted, but did not necessarily believe were germane to this phase of the ECAM.

For example, I point out that the determination of whether the Company's level of market reliance and hedging strategies are optimal, which is a focus raised by other parties, is not necessary to a decision to include them in ECAM.

Parties will have an opportunity to review our purchase and transaction costs, both in rate cases and in the ECAM review cases. The Company's ECAM filing was consistent with Commitment U-23, approved by the Commission, and its order -- report and order issued June 5, 2006, in Docket No. 05-035-54 that required an ECAM to be filed at least three months prior to the filing of a general rate case.

This was done so that there would be an opportunity in the general rate case for the Commission to determine the appropriate level of net power costs.

As all parties essentially acknowledge, the best place to consider changes to the Company's level of market reliance and hedging strategies is the IRP process. As I already mentioned, the Company is committed to fully cooperating with the review of these issues in the IRP.

Including market purchases and hedging costs in the ECAM does not foreclose the IRP review. This concludes my summary.

MR. MONSON: We would offer Mr. Duvall's rebuttal testimony and its exhibit. I want to apologize, I didn't prepare a sheet with the listing of our exhibits. But -- and in part -- well, that isn't the reason.

But we had trouble deciding how to number things in this case. Do you have a suggestion, Mr. Chairman?

CHAIRMAN BOYER: And with my suggestion and a dollar you could buy a soft drink. But perhaps use Phase II Part 1 in your identification of the exhibit.

MR. MONSON: So we would offer Mr. Duvall's rebuttal testimony as Rocky Mountain Power Exhibit 1 Phase II Part 1. And his -- and it's -- I note again, it's highly confidential testimony. And also his exhibit, which is highly confidential, as Rocky Mountain Power Exhibit 1 -- I'm sorry, make it 1R, I guess, because it's rebuttal testimony. And his exhibit to his testimony as Rocky Mountain Power Exhibit 1.1R Phase I Part 1.

CHAIRMAN BOYER: Phase II Part 1.

MR. MONSON: Phase II Part 1, sorry.

CHAIRMAN BOYER: Are there any objections to the admission of Mr. Duvall's prefiled written testimony, together with exhibits?

Very well, they are admitted.

(Exhibit Nos. RMP-1R Phase II Part 1 and RMP-1.1R Phase II Part 1 were admitted.)

MR. MONSON: Thank you. Mr. Duvall is available for cross examination.

CHAIRMAN BOYER: Ms. Schmid, any cross examination of Mr. Duvall?

MS. SCHMID: A few.

CROSS EXAMINATION

BY MS. SCHMID:

Q. Good morning.

A. Good morning Ms. Schmid.

Q. The Company's 10-K report and its risk management policy indicate that the use of options is allowed under the current hedging program. Has the Company used options in the past?

A. It's, it's not used financial options, and to a very limited extent we've used some physical options. I think they've been subject of a -- in the rate cases. The Nebo heat rate option, for example, the Morgan Stanley option.

Q. To your knowledge has the Company ever been denied recovery of option costs?

A. I don't think so. Maybe once in, in Oregon. But it's certainly been a subject of controversy in testimony before this Commission on the net power costs.

Q. If we turn to line 279 of your rebuttal testimony you indicate to the effect that the current market is dynamic and requires continual analysis and study. You also indicate that you would like to wait to discuss options as part of the next IRP process. How do you reconcile these two positions?

A. Well, I think they're completely separate. I mean, the conditions change all the time. I think the important thing about options is that they have premium payments to them. And you would be in a situation where we'd have to make sure that we understand that we could pay a premium.

The option may never actually be -- ever be in the money. And the question is, is that premium useful? Is that recoverable? And I think the Company would at least like to have those discussions, you know, before we launch out using a lot of options.

I think in terms of the expected outcome, whether to use options or swaps? You know, if everything turns out the way you'd have expected it to turn out, everything would -- the economics would be identical.

Q. Is there a premium associated with hedging?

A. Well, "hedging" is a, is a word that I think has been confused in this docket. So hedging, hedging is really -- and I'm not sure what you're asking in terms of hedging.

But in my view, hedging includes anything that we do to purchase either gas or electricity prior to the time that we actually need it.

Q. Using that definition, and to the extent that you can state without treading into any confidential waters, has the Company paid more because it has hedged into the future?

A. As, as opposed to?

Q. If it had purchased on spot market? Or not had the long-term contracts?

A. No. In fact, if you -- in my testimony I have a footnote on that somewhere. I think I see it. No.

Anyway, we had presented some evidence that, that if you look at all of the, all of the hedging and the gains and the losses of the hedges versus if you had just gone to spot market, that that benefit was a hundred million dollars to the, to the good.

The analysis that was presented in the surrebuttal testimony of Mr. Wheelwright only looked at a subset of our hedging, which was swaps. It completely left out the physical forward contracts that we do, mainly on the sales side, that are also hedges.

Q. Come back to that. Turning now to TEVaR, the new metric. And am I pronouncing that correctly?

A. Sounds right to me.

Q. Okay, good enough.

A. Have you got a page number there?

Q. No. I just have some general questions about TEVaR.

A. Okay.

Q. Does TEVaR represent the value of the contracts as of a particular point in time based on the anticipated forward price curve?

A. Well, it's the -- it looks at the value of the whole portfolio, not particular contracts. But it's the -- to the expir -- expiration of the contracts.

Q. As the forward price curves change do the value of those contracts change?

A. Well, the measure of the TEVaR changes.

Q. Okay. That's better.

A. Yeah. It's not only forward price curves, but it's everyday the forward price curves and the volatilities and the correlations are updated.

Q. Using the TEVaR can I find an indicated -- could someone with more mathematical skills than I find an average price for MMBTU for natural gas contracts?

A. Well, this is beyond my level of expertise. I don't --

Q. Then I'll withdraw the question --

A. I don't compute the TEVaR.

Q. -- because it was beyond mine, too.

A. Yeah.

Q. Does the Company have approved ECAMs in place in other states?

A. We have a, I guess starting with California we have a dollar-for-dollar -- it's called the ECAC, but it's the same thing -- dollar-for-dollar true up in our California service territory. We have an ECAM in our Idaho service territory, which is a, it's a 9010. It's got some other features to it.

We have a PCAM in Wyoming, which was actually the result of a settlement of some disputes we had there. We are now in the process of revising that and we have proposed an ECAM pretty similar to Utah, the Utah ECAM, in Wyoming as well.

We don't -- we have an annual update of our net power costs in Oregon, but it's not a true up to actual so it's a little bit different. We have nothing in Washington and nothing Utah.

Q. Now let's move to a few hypothetical questions. To start, we have Utility A. Utility A has an ECAM and a hedging practice. Utility B has a hedging practice but no ECAM.

If hedging A, with its ECAM and hedging practice, lost more money with hedging than Utility B, which hedged but had no ECAM, would the public interest be served by the program of Utility A with its ECAM and hedging practice?

A. Well, I think the important thing here is to understand that an ECAM is not put in place to make money or to lose money. I mean, it's -- you can't actually call the market, it's the same as buying and selling stocks.

You know, if you -- you have no way to actually determine whether you can make money or not. It's all about hedging risks. And, you know, mitigating the risks associated with the volatility of the market.

So if, if, you know, measuring you -- I think your question was if you, if you measure the gains or losses. And, and I wouldn't measure the gains or losses because that's not what a hedging program is about.

Q. Do you think the public interest is -- just one moment.

Is the purpose of an ECAM to make the utility whole?

A. Well, the purpose of the ECAM is to -- for the -- it's to have, you know, customers pay the actual cost of providing service.

MS. SCHMID: Thank you. Those are all my questions.

CHAIRMAN BOYER: Thank you Ms. Schmid. Anything further?

MS. SCHMID: No.

CHAIRMAN BOYER: Okay. Mr. Proctor?

MR. PROCTOR: Thank you Mr. Chairman.

CROSS EXAMINATION

BY MR. PROCTOR:

Q. Mr. Duvall, I have just one question of clarification. You were discussing the chart that Mr. Wheelwright included in his surrebuttal, I believe, that showed that the -- and I'm not certain about it either for myself, so that's why I'm asking you.

That was a comparison of your swap costs with what?

A. Well, just the swap costs.

Q. Okay.

A. So it's all of the -- with, with the swap you have, you have -- it's a financial instrument where one party pays a fixed price, the other one pays a floating price. That floating price would be a market index.

And so if, if -- for gas, for example, if the fixed price were $5, and we were the fixed-price payer and the market came in at $8, then we would receive the difference -- we would pay the $6 and we would receive the difference on the swap between the $8 and the $5. So we get an extra $3.

So, in essence, we're always paying the $5. And I think that's stayed with the same numbers.

Q. Would it be fair to state -- to describe them to be transaction costs?

A. No, it's the settlement costs.

Q. All right. And is Mr. Wheelwright's chart correct that over the period of time that he was measuring your swap costs your settlement costs were, in fact, significant?

A. The -- and I would, I guess, refer to -- it's DPU-SR Exhibit 2.1. And I believe that's, that's what I was talking about. And how that comes up with a number that he pulls into his testimony.

Q. What's his number? And by the way, is his number confidential?

A. That's what I was looking at.

MS. SCHMID: Yes.

THE WITNESS: It appears to be, yes. But it shows up on, on page 1 of his testimony, and on line 26.

Q. (By Mr. Proctor) And that's of his surrebuttal or rebuttal?

A. Of his surrebuttal, correct. Which is the same number that shows up on exhibit -- his exhibit -- Surrebuttal Exhibit 2.1, in the top left-hand box under the total.

MR. MONSON: May I, may I interrupt for just a second?

MR. PROCTOR: Certainly.

MR. MONSON: I hope this will help. These numbers in their total amounts per year are not confidential. So if you want to talk -- say the numbers, you can. As long as we don't get into the detail of them and the backup behind them.

Q. (By Mr. Proctor) If --

A. Okay. So I was, I was pointing to the --

Q. What was the total number, then?

A. It's the 59.5 million per -- number.

Q. And that, that was a cost rather than a gain?

A. Yeah, that was a net cost.

Q. Net cost?

A. Of the -- net of all the swaps. Which, in my mind, makes absolutely no sense because it's only a subset of the hedging.

Q. Whether it makes sense in your mind, sir, are those numbers correct? Not quarrelling with whether or not you believe they should even be used, are those numbers correct as a reflection of your costs, your settlement costs?

A. Yeah. I would, I would say yes, subject to check. We --

Q. Well, where are you gonna check them?

A. Well, these, these numbers were presented in the surrebuttal testimony that we got just recently. And we've, we have looked at them, and I would -- I -- my sense is they're correct. And they're also presented in the direct testimony of Mr. Peterson in the next phase of this, so we will certainly address them in rebuttal.

Q. Would those numbers have come from discovery responses provided by the Company?

A. Yes, they did.

Q. Okay. And were you a part of the preparation of those discovery responses?

A. I reviewed them.

Q. And are these the numbers that you provided to the Division?

A. Well, the -- here's, here's what the concern is, is because the question says --

Q. Excuse me Mr. Duvall, I didn't ask you what your concern was. I'm sure your counsel will have the opportunity to ask you that. Are these the numbers that the Company provided to the Division?

A. Not for hedging costs.

Q. But were the costs --

A. And the question --

Q. -- misused by Mr. Wheelwright? The swap costs, the settlement costs, are those the numbers you provided?

A. Yeah. His, his question says he's, he's -- that he's referring to hedging costs, yet his answer is just the swap costs.

Q. Okay. And those are the swap cost numbers you provided, correct?

A. Yes, they are.

Q. Now, you provided a number of approximately a hundred million dollars, just moments ago, as being the benefit from comparing spot purchases to your hedging costs? Did I hear that correctly?

A. Well, it's, it's looking at all hedging costs, not just swaps. And in fact, in the responses cited in Exhibit 2.1, the 14.14 had all of, all of the costs. Mr. --

Q. What page -- what line are you referring to?

A. In the, in the heading of the exhibit he says DPU data request 4.14, 8.1, and 8.2. And so 4.14 had not only the swap costs, but all the costs associated with the physical hedges, and added up to the hundred million dollar benefit.

And he chose to ignore anything except the swap costs. And in 8.1 and 8.2 alls he asked for was the additional swap costs. He didn't ask for all the hedge costs.

Q. And you gave him accurate numbers and answered his questions, did you not?

A. Yes, we did.

Q. Now, you described swap costs and physical hedging costs. Are there any other costs or benefits associated with your comparison that you described as resulting in a hundred million dollar benefit?

A. No.

Q. What are physical hedges?

A. Well, if you, if you want to sell forward, for example, typically what we had done up until about four years ago, before we started using swaps, was everything was a physical forward. So we could, today, sell a 2011 contract for power.

And that's really a combination of -- that has a financial hedge in it as well as the physical delivery. If we were to do that through a spot, the financial part of it would be through a swap and the physical part would be through an indexed sale.

So there -- it's -- the market has evolved from always just doing physical forwards to using swaps and index deals. And what that allows is actually more counterparties. And it's actually been a more of a traditional way of doing business on the gas side for years.

Q. Does your company have a definition of a physical hedge within its policy?

A. I don't recall if it's within our policy, but we -- when we -- in my rebuttal testimony there was a question about describing all of the instruments we use, and I certainly described it there.

Q. Where within your testimony did you describe it?

(Pause.)

MS. HOGLE: If you will look at page 21.

THE WITNESS: Twenty-one, thank you.

Yes, starting on -- I'm on line 459. Well, actually 455:

"Question: Mr. Gimble states it would be useful for the companies and parties to understand the various types of standard market products that are currently available to the Company and how they might differ by market hubs."

Q. (By Mr. Proctor) And the -- and you used the phrase "fixed price physical transaction"; is that correct?

A. That's correct.

Q. What is, then, a fixed price physical transaction?

A. It is what probably within the grid world would consider a short-term firm sale. So it involves a price, a fixed price, and it involves, you know, power. Or on the gas side it would be a fixed price and the commodity.

Q. And would it include both sales from the Company to a third party, as well as purchases from a third party to the Company?

A. Yes, it would.

Q. Of either fuel or energy?

A. Correct.

Q. Correct? Is there a transaction in fuel or energy with a fixed-for-floating financial swap transaction?

A. Yes. That's what we call a swap.

Q. There's a physical exchange of either ener -- of energy or fuel?

A. No, there's not. That's, that's purely a financial deal.

Q. That's helpful, Mr. Duvall. You testified just moments ago that options have been a subject of controversy before this Commission and other commissions, did you not?

A. I did.

Q. And so this Commission has explored, in general rate cases, the use by the -- of the -- by the Company of options?

A. Well, to a limited degree. They, they have never investigated the use of purely financial options.

Q. The two options you mentioned, one was Nebo and I forget the other.

A. Morgan Stanley.

Q. And Morgan Stanley. What does Morgan Stanley option consist of?

A. Well, it's a, it's a call option. So it has a monthly premium. And then if, if it's in the money, then we will use that.

Q. Use, use what? You get fuel or energy?

A. We get, we get power.

Q. Okay.

A. Right.

Q. And the Nebo, you used two words to describe that?

A. Nebo heat rate options?

Q. Yes. And what is that?

A. Yeah, Nebo is actually a generating facility that we had the option to run the fuel through. And we would do that when it was in the money. But we paid a fixed premium to have the right to do that.

Q. And that's a gas plant?

A. Yes, it is.

Q. And it's located...

A. In Utah.

Q. In Utah right off the freeway, is it not?
A. Beats me.
Q. Somewhere down in -- have you not been there?
A. I have not been there.
Q. Well, I may be wrong which one it is, but there's something there. So the Company -- and those are -- would you describe those as physical transactions?
A. Yes. They, they involve the commodity.
Q. But this Commission has never considered a financial option in a general rate case?
A. We, we have not presented any.
Q. Have you used any?
A. No, we have not.
Q. But how long have you been engaging in the swaps?
A. Well, my recollection is we didn't have swaps until about, I would say four years ago.
Q. Well, let me ask it this way. Fixed for floating financial swap transactions, how long have you engage -- has the Company, pardon me --
A. To the best --
Q. -- been engaging in those?
A. Yeah. To the best of my knowledge, we've been engaging in those maybe for four years. Maybe a

little longer. But I -- they -- I, I -- my recollection is through the net power cost study where we pull in swaps into the, you know, short-term firm purchases and sales.

And it turned up, I would say about four years ago, that we started having spot transactions as well. So that's my understanding.

Q. Mr. Wheelwright's chart based upon the Company's numbers that we spoke about just moments ago, it covered the time frame I believe from 2005 to 2009; am I correct?

MR. PROCTOR: Mr. Chairman, may I ask Mr. Wheelwright the time period for his?

CHAIRMAN BOYER: Yeah, go ahead.

MR. WHEELWRIGHT: 2006.

MR. PROCTOR: Through 2010, or?

MR. WHEELWRIGHT: Through May of 2010.

MR. PROCTOR: Okay.

Q. (By Mr. Proctor) So Mr. Wheelwright mention -- said that his -- the numbers that you gave to him that he's used in compiling his own testimony was 2006 through May of 2010; is that correct?

A. Yes.

Q. And so that's about the entire time you've been engaging in fixed-for-floating financial swap

transactions?
A. Pretty close, yes.
Q. Has the Commission ever examined those transactions in a general rate case?
A. The -- I'm sorry, which transactions?
Q. The fixed-for-floating.
A. They have been included in the net power cost studies --
Q. Didn't ask you if they were included, asked you if they've ever considered them.
A. Well, they've -- I'm not sure --
Q. As an in -- well, that's a bad question. As an independent component to net power costs?
A. So I, I don't -- I'm not sure what you mean by "considered." Did they address it in an order, or?
Q. Well, let me ask it this way. Did you present to this Commission, at any time in that four-year period -- almost four years -- any fixed-for-floating transaction the same way you presented the Nebo physical transaction? That was subject to controversy?
A. Well, the -- they're all included in the net power cost study, in that all of the -- all of them we had provided discovery to all the parties on.
The Nebo and the, and the Morgan Stanley were

actually raised by, by the Office witness. And his, his position was that because they weren't exercised in the power cost study, that the customers shouldn't pay the premium.

Q. And so your answer is that, indeed, the fixed-for-floating financial transactions have not been independently litigated in front of this Commission in any general rate case?

A. No one has brought any kind of issue with them. They've been included in the cases. No one's challenged them. No one's said that they are not -- nobody's put testimony in saying they shouldn't be allowed.

Q. So your answer is no, they have not been litigated?

A. They have not been an issue before this Commission.

Q. Okay. Your purpose here, though, is to establish that in the judgment of the Company, financial transactions are an appropriate component of an ECAM?

A. I believe they are, yes.

Q. And is that in part because you believe that the Company's hedging practice, or hedging policy, is a sophisticated one?

A. No. I --

Q. It's not sophisticated?

A. Yes, it's sophisticated, but that's not the reason that I would agree -- that would, would say that swaps ought to be in the, in the ECAM.

Q. Well, you would say because it provides some comfort or some hedge against volatility within either the energy or the fuel market?

A. No, I would, I would say they are, are included first of all because they're a replacement or a -- similar to a power sale or a power purchase. It's just a different way of doing it. The power -- a power sale or a power purchase includes the financial hedge as well as the physical commodity.

When you, when you do it separately with a swap and an indexed commodity deal you get the same answer, it's just two different products.

Q. And so since 2006, up until May of 2010, those have been included in rates? Those financial transaction costs have been included in rates?

A. They have, yes.

Q. And presumably they would remain in rates until such time as the next general rate case, correct?

A. Just like any other element of net power costs.

Q. And at that time they could be scrutinized by this Commission. Parties could raise them. Conduct discovery upon them. Determine whether or not, in the parties' judgment, they're an appropriate component of net power costs; is that correct?

A. I think that they could do anything they want.

Q. And the Commission would have the opportunity to evaluate the various positions and come to a conclusion about the inclusion of those financial costs in, in rates at that time, could they not?

A. They could. They could also do that in an ECAM review proceeding.

Q. Well, but if they did it in ECAM isn't it true that rather than a scrutiny through a general rate case, which you acknowledge can be controversial because of your option testimony, and subject to discovery, correct?

A. That's correct. And I would imagine that the ECAM would also be subject to discovery and scrutiny by the parties.

Q. But one thing that would not be subject to scrutiny if they would be placed in an ECAM as proposed now would be the Company's policy or practice of hedging; isn't that also true?

A. No, it's not.

Q. Well, where do you propose that this Commission have an opportunity to examine and scrutinize the Company's hedging practices and the propriety of including those hedging costs -- and again, we're talking about fixed-for-floating financial transactions -- within rates?

A. The ECAM review proceeding would look at whether the costs included in the ECAM are prudent or not prudent.

Q. Have you ever -- has the Company ever presented to this Commission, for their approval, your fixed-for-floating hedging practice, or policy, or manual?

A. No, we've not, but they've been included in net power costs for the last several years.

Q. Which have never been litigated. You've already admitted that, right?

A. Well, they haven't -- I mean, that particular issue has not been raised by any party. The net power costs have certainly been litigated.

Q. But your policy itself has not?

A. Well, the policy has been provided in discovery and no one's taken any kind of issue with it.

Q. Your proposal is to include such an examination in an IRP, is it not?

A. Well, we've been, we've been ordered by the Commission to evaluate both the hedging and the market reliance in the IRP, and we intend to do that.

Q. But you want to also include it in an ECAM before you've done that evaluation in an IRP, don't you?

A. They're already included in base rates. So we're just changing how you do the ratemaking from a base rate to a true up.

Q. Do you want -- I mean, you -- and I apologize for saying "you" because I know, Mr. Duvall, that it's the Company. And I'm not trying to direct anything towards you personally, understand, please.

The Company's position is that the examination of its hedging practices or policy will take place in an IRP, but in the meantime we're going to adjust those general rates based upon the inclusion of financial hedging in an ECAM. Is that the Company's position?

A. The Company's position is that the, the hedging policy is already -- and all the hedging instruments are already built into the base rates.

And that we have, we have provided a massive amount of evidence before this Commission that the hedging has provided benefits to customers in terms of reducing the risk of costs going too high.

Q. Isn't that also true with your market reliance practices? That they're included in base rates now, but your market reliance practices or policy has never been, itself, examined by this Commission?

A. Well, market reliance has -- and the front office transactions have always been part of the Integrated Resource Plan since, I believe, about 2004.

Q. Does the integrate -- does an IRP acknowledgment or any order from this Commission pertaining to an IRP result in a change in rates?

A. No.

Q. Is the Company bound to modify its rate structure and its ratemaking practices as an out -- as a result of an order -- any order from this Commission pertaining to an IRP?

A. No, it's not.

Q. And in fact the Company takes the IRP outcome -- acknowledgment, non-acknowledgment, whatever -- and translates that into a business plan; is that correct?

A. Well, the business plan and the IRP are usually developed -- or developed in conjunction with each other.

Q. Is the business plan provided to the Commission for their approval?

A. No, it's not.

Q. Is it provided to the Commission for their scrutiny in their official capacity?

A. Not that, not that I'm aware of.

Q. And it's the business plan that defines the Company's operations in the future, is it not?

A. Well, the IRP is the -- the IRP and the business plan -- the IRP develops the resource portfolio for the business plan.

Q. But they do vary on occasion, do they not?

A. Very slightly.

Q. But they do vary? They can?

A. Well, they, they can, but it would probably be a matter of timing.

Q. Well, it would also be a matter of the discretion of the Company, would it not?

A. No.

Q. The Company's not in charge of its business plan which it does not submit to this Commission?

A. It is, but the Company also is the one who determines what its IRP is. We, we make the IRP and we file it.

Q. And you ask other, other parties to comment upon your IRP, correct?

A. We do.

Q. You invite them to participate in your public process as well as the process before this Commission, do you not?

A. Yes, we do.

Q. Do you invite other company -- other parties to prepare their own IRP alternative to submit to the Commission?

A. No, we don't.

Q. In fact, the IRP process does not provide for that, does it?

A. No, it doesn't.

Q. Where within the IRP process, in particular the standards and guidelines, is an examination by this Commission of the Company's fixed-for-float -- for-floating financial transactions provided for?

A. Well, it was in the order in the 2008 IRP.

Q. Where within the guidelines, the specific guidelines for the preparation of an IRP, is hedging -- financial hedging provided for?

A. I don't believe it's specifically called out

in any guidelines.
Q. You are currently engaged in the preparation of a 2011 IRP?
A. Yes.
Q. And you would expect that to be completed or at least published when?
A. March 31, 2011.
Q. Have IRPs ever been -- the publishing date, have they ever been extended?
A. Yes, they have.
Q. For six months, for example?
A. I don't recall any for six months. Last year we asked for two months, I believe.
Q. And for what period of time would you anticipate the Company covering in its IRP that you hope to be submitting in March of 2011?
A. Well, the primary focus is on the first ten years.
Q. And the secondary focus?
A. Well, the, you know, beyond ten years we tend to use generic resources and so on. But it's -- the first ten years is then used to develop the action plan which we use for the actions that we want to take over the next, you know, one to two years.
Q. And that ten years would begin in what year?

A. Probably 2011.

Q. Now, the financial swap transactions that are presently in, in rates, those are a product of transactions that go through what period of time? In other words, right now the Company, I assume, has certain financial contracts for which it is obligated in order to smooth out the volatile market, as I think you described?

A. Correct.

Q. How long are those trans -- those -- are those transactions? Oh, contracts, I'm sorry.

A. I believe they're -- that we have contracts out through the next four years.

Q. So through 2014, roughly?

A. Pretty close.

Q. So if these transaction costs, the financial transaction costs were included in an ECAM, they would be based upon contracts that already exist, that you're already obligated to, and that won't change as an outcome of any IRP study until 2015; isn't that true?

A. Whatever contracts we have in place are contracts we have in place.

Q. And no IRP examination of your financial hedging practices or policy is gonna change that, is it?

A. I'm not sure what you're asking. Would change what?

Q. Change anything. Change the rates. Change how much the contract is. Change what you are allowed to commit to. Any limits on -- or caps on mark -- on hedging. None of that's gonna change because you have absolute contractual obligation through, in some instances, 2014?

A. The, the IRP will not change any contract terms.

MR. PROCTOR: Okay. Thank you Mr. Duvall.

CHAIRMAN BOYER: Thank you Mr. Proctor.

Ms. Hayes, questions for Mr. Duvall?

MS. HAYES: Yes, thank you.

CROSS EXAMINATION

BY MS. HAYES:

Q. Sorry to make you turn. You stated in your summary that front office transactions have been reduced in the 2010 IRP business plan update; is that correct?

A. The 2008 IRP update.

Q. Okay. Can you point me to a table in that update that illustrates that?

A. I don't actually have a table number, but the -- over the, the 2008 IRP, the average over all the years was 809 megawatts. And in the 2008 IRP update it was 687 megawatts. And there's, there's tables in both of those documents that you can look at to get those numbers.

Q. Are those Tables 5.5 and 5.7?

A. I don't know offhand what their numbers are.

Q. All right. Well, if I could just direct you to 5.5 and 5.7.

MR. MONSON: Could you, could you provide him with copies? I don't think he has them.

Q. (By Ms. Hayes) Oh, you don't have the IRPs?

A. I don't have them, no.

Q. Okay.

(The witness and Counsel are talking too quietly.)

THE REPORTER: Do you want to keep your voices up, please, if you want it on the record?

MS. HAYES: Oh, sorry. I'm just pointing out in these Tables 5.5 and 5.7 where it lists the front office transactions.

THE WITNESS: Okay.

Q. (By Ms. Hayes) Isn't it true that the changes in front office transactions depicted in those tables are not quite accurate, because they reflect the changes between the business plan, the October 2009 load forecast, and a portfolio developed using the November 2008 forecast -- which is the 5B_CCCT_Wet -- not the final preferred portfolio developed with the February 2009 forecast?

A. I didn't follow you at all, sorry.

Q. All right. Well, I'm trying -- the numbers in those tables are -- I just don't know if they're accurate, because they are not -- it's not the -- they're not comparing the front office transact -- transaction reductions based on the preferred portfolio identified in the IRP process. They are compared to a portfolio developed using the November 2008 forecast.

A. The preferred portfolio out of the 2008 IRP used the November 2008 forecast, I believe.

Q. I think the preferred portfolio was developed with the February 2009 forecast?

A. My recollection -- and I don't have it in front of me. But my recollection is that we did a sensitivity on the February forecast, but the preferred portfolio itself was based on the November 2008 forecast.

MS. HAYES: Okay, thank you.

CHAIRMAN BOYER: Is that all, Ms. Hayes?

MS. HAYES: Yes, thank you.

CHAIRMAN BOYER: Okay, thank you Ms. Hayes.

Mr. Dodge?

MR. DODGE: No questions, thank you.

CHAIRMAN BOYER: Mr. Evans?

MR. EVANS: Thank you Mr. Chairman.

CROSS EXAMINATION

BY MR. EVANS:

Q. I have a couple of questions, Mr. Duvall, good morning.

A. Good morning.

Q. We are in a difficult position here to have you look at me while I ask questions, but if you can try, that would be great. If you can't, don't hurt your neck trying. We'll keep this short and kind of broad, I think.

On May 25th the Company offered a presentation to the Commission and others about a change to a TEVaR metric and a new -- introduction of a new hedging program. Were you, were you at that presentation?

A. I believe I was, yeah.

Q. I've got a couple of questions about the new hedging program that was introduced. First, has the TEVaR been implemented? Are you currently using it?

A. Yes, we are.
Q. And the new hedging program as well?
A. I'm not sure what you mean by the new hedging program.
Q. Well, I think I was under the impression at that meeting that the Company was gonna change its hedging practices in some way using this TEVaR metric. Was I wrong in thinking that?
A. Well, the TEVaR metric just was a replacement for the, for the fixed volume limits. Sort of the -- or the targets for hedging for both natural gas and electricity. The rest of the program remained the same.
Q. So there was really no -- been no change in the hedging program itself as a result of implementing the TEVaR metric; is that correct?
A. The hedging program didn't change very much. It was just the metric that you could use to see how the, how the open position affected net power cost. It was a much more informative way and useful way to look at it.
Q. So as far as hedging goes, you're using the same fixed and -- or physical and financial products as you used before; is that correct?
A. That is correct.

Q. And you're using it in the same way?

A. Well, it will vary over time, but essentially there wasn't any material change.

Q. And there's not been any plan to terminate or otherwise dispose of any of the existing physical or financial products as a result of this move to the TEVaR metric?

A. No.

Q. So really it makes no difference in the hedging program? Is that what you're -- is that what I'm hearing?

A. It's just a different way to measure the, the targets.

Q. Thank you. Without belaboring it, I want to follow up on a conversation you had with Mr. Proctor a few minutes ago about these fixed for -- fixed-for-floating financial swap transactions. That's -- we're, we're just talking natural gas here, aren't we, for those?

A. No, natural gas and electricity.

Q. Natural gas and electric both? Let's call them "swaps" for short. Because it's different from your other hedging which may include physical or other purchases, right? Can we call those "swaps"?

A. That's what they are, is swaps.

Q. Okay. It's just a piece of the hedging, right?

A. It's one, one tool to use to hedge.

Q. Okay. What is it you actually get for the hedging dollars that you've got in rates right now? Those swap dollars? What's the deliverable?

THE REPORTER: What's the what? I'm sorry.

MR. EVANS: Deliverable.

Q. (By Mr. Evans) Do you get a commodity for that?

A. No, swaps are just a financial transaction.

Q. You don't get any gas?

A. No, we do not.

Q. Or power?

A. Not under a swap.

Q. You don't get security of supply either, do you?

A. They're, they're only intended to hedge the price.

Q. So you have to go out and buy the physical in a separate transaction; is that correct?

A. That's correct.

Q. So when I look at the, when I look at the statute that authorizes the ECAM? I'm curious about what you -- how you think this all fits. What I, what

I see here is that an energy balancing account is for some or all of the components of incurred actual power costs, including two things.

One of them is the less wholesale revenues, but the other is the three things that we're concerned about: Fuel, purchase power, and wheeling expenses. You look at fuel for your settlement dollars on your swaps, do you?

A. We, we get a, you know, price guarantee. In fact, all of these swaps -- the fuel-related swaps are actually recorded in fuel accounting -- in the fuel account. And the power purchase swaps are actually recorded in the power purchase accounts as well.

Q. Although -- well, they're recorded in the accounts but you don't actually get fuel or power for the, for the dollars, do you?

A. We, we don't get the commodity, no.

Q. So which one of these categories: Fuel, purchase power, wheeling expenses?

MR. MONSON: Are you asking for a legal opinion?

MR. EVANS: I'm asking where he thinks these costs ought to go.

THE WITNESS: Where they, where they do go, if it's a swap dealing with fuel it'll go in the fuel account. If it's a swap doing -- dealing with wholesale purchase or sale it will go in the, in the wholesale purchase or sales accounts.

Q. (By Mr. Evans) Okay. But what you're really buying is insurance against the price of the fuel, right?

A. You're, you're buying the, the price, I guess hedge, that's normally part of a, a physical deal. So if we -- like I described before, if we, if we buy gas at $5 a MMBTU and it's -- it could be a physical deal, where we get the gas and we get the hedge.

Or we could do it by buying index gas, that floats all over with whatever the index is, and buy a swap. The swap and the index deal together are the same as a physical transaction.

Q. The counterparties are different, aren't they? Why do you say that's one transaction? It's two transactions.

A. They're two separate transactions that get the exact same result as one physical transaction.

Q. Well, one gets gas and the other gets nothing. Just a price guarantee.

A. A price, a price on either gas or electricity.

Q. Right, okay. Let's move on. In your

rebuttal testimony at lines 207 to 210 -- and you say this throughout and I think that you don't need to turn to it. You understand that the issue in this portion of Phase II should be, and I'll quote this:

"Whether the Company's hedging and reliance on market energy should be changed in the context of an ECAM."

Do you see that?

A. Sounds familiar. Yes, I do.

Q. You are aware, of course, that others here disagree that the issue should be that narrow?

A. Yes, I, I do.

Q. Is it, is it your, your -- let's say the Company's position that the Commission here is somehow confined to looking at whether hedging and reliance should be changed in the context of an ECAM?

A. No, it's not my position that they should be confining at all.

Q. Okay. So the Commission could decide that no level of market reliance or hedging costs should be allowed in an ECAM?

A. They can make whatever decision they wish to make.

Q. One more follow up on Mr. Proctor's cross examination. He was talking about the IRP and the way it integrates with the Company's business plan. And you seem to say that the Company's business plan adheres to the IRP. Is that always the case?

A. Yeah, we -- in recent years we've worked on aligning the business plan and the IRP. It may not have been the case years ago, but we try to make that the case as much as we can.

Q. What are the consequences if the Company's unsuccessful in aligning the business plan with the IRP, for whatever reason?

A. I'm sorry, I didn't -- I missed the question.

Q. What are the consequences if the Company is not successful in aligning the business plan with the IRP?

A. Well, I, I guess the -- one of the consequences is that we would probably not be in compliance with the Utah -- one of the Utah IRP rules.

Q. Would it, would it mean disallowance of some costs and rates?

A. No, it would not.

Q. Would there be -- has the Commission ever issued an order enjoining, or rather compelling the Company to do something that was in its IRP that it wasn't doing?

A. No. The, the Commission basically -- I think it's probably summarized best in their response to the 2007 IRP order. And that's where they, they basically said -- and I was just referring to page 4 of Mr. Gimble's surrebuttal -- that the Company bears the risk of any unreasonable costs to ratepayers associated with its decision -- decisions to change the quantity and type of resource it procures based on asserted but unexamined risks.

And so essentially the, the policy is that the Company makes its decisions based on the input it gets from folks. And it takes the risks that it would bear the risk of the unreasonable costs. My reading of that is that as long as the costs are reasonable, then that's fair for customers to bear that risk.

Q. And if it turns out there are unreasonable costs the disallowance wouldn't be in the IRP, it would be in the rate base, wouldn't it?

A. That's correct.

Q. Just a couple of questions of clarification in your testimony, if you don't mind. I'm looking at line 740 in your rebuttal, where you talk about a spark spread. Can you tell me what a "spark spread" is, please?

A. Yeah. Essentially the spark pr -- spark spread is the difference between the market price and the gas price as, as converted to a market price by the rate of the gas unit.

Q. So there are two pieces of it. One was the conversion factor from the gas to electricity, and the other compared with the market price for electricity. And do you use that spark spread on a daily -- when you're looking at daily purchases between -- when you're making decisions between burning gas or buying power daily, you look at that spark spread?

A. That's correct. It's an indication of whether your gas plants are in the money.

Q. And how far out can you determine whether your gas plants are in the money by using the spark spread?

A. Well, you can, I guess, determine it as far out as you want. Obviously as long as you have a gas price and a market price you can determine -- and a heat rate of your gas plant you can determine the spark spread.

But, you know, it certainly becomes less useful the further out you go, just like anything else.

Q. So when you're, when you're engaging in your hedging practices and you're setting up your natural gas supplies you don't use that spark spread for buying these swaps, do you?

A. The, the spark spread is built in to the, the TEVaR metric, for example. It looks at those, those sorts of things. But again, you're pushing on the edge of my expertise here.

Q. One more. One more question. And this is to follow up. You have said throughout your testimony that the purpose for hedging is, I thought, to -- as a means to reduce volatility in prices. Is that pretty much accurate?

A. Well, this was brought up by Mr. Wielgus, I believe, in his testimony, his surrebuttal. Where he claims that we have switched our position from market volatility to -- or the volatility in the prices to market exposure.

There is no switch involved at all. Those are really one and the same.

Q. So you're not contending that these -- the current hedging practices insure or work toward obtaining fuel and power supplies at the least cost, are you?

A. The hedging is not intended to reduce cost or increase cost, it's intended to reduce volatility.

MR. EVANS: Okay, thank you. No more questions.

CHAIRMAN BOYER: Thank you Mr. Evans.

Let's turn now to the commissioners. Commissioner Allen? No questions?

Commissioner Campbell?

COMMISSIONER CAMPBELL: Just a few. When you look at that $59 million that we've talked about in swap costs, how does that compare to the swap costs that -- or net power cost over that time period; do you know?

THE WITNESS: Yeah, I, I would imagine that on a year-by-year basis they were pretty close. It depends on the test year and whether all the -- whether there was a future piece of the test year. But anything that would have been historical would have been included in the test year. We get that information out of the net power cost studies.

COMMISSIONER CAMPBELL: So let's talk about how hedging relates to rates for a minute. I want to understand this interaction. After rates are set in a general rate case how would customers be exposed to market prices for natural gas or electricity?

THE WITNESS: Under ECAM?

COMMISSIONER CAMPBELL: No, under our current method.

THE WITNESS: Under the current method, once rates are set, then that's the rate that goes to retail customers. And any changes in market prices are borne by the, by the Company.

COMMISSIONER CAMPBELL: And so in a rate case when we do net power costs, customers I guess are exposed to market prices to the extent that the Commission estimates wrong, or -- you made a statement that hedging is there to reduce customer exposure to the market.

I'm trying to understand that. Because I -- as I look at the current system for you all in comparison to Questar -- I understand how Questar, with their pass-through 191 account, how their hedging costs are borne by customers. Or how customers benefit from that hedging.

Under our current system isn't the Company the primary beneficiary of the hedging that takes place?

THE WITNESS: Well.

COMMISSIONER CAMPBELL: I'm trying to understand how customers benefit from the hedging.

THE WITNESS: Yeah.

COMMISSIONER CAMPBELL: I mean, I understand -- doesn't the hedging really help the Company stabilize revenue? And I'm not saying that

that doesn't help customers in the sense that you have an opportunity to earn your return and so forth.

But generally isn't it fair to say that your current hedging program under current regulation in Utah primarily benefits the Company, not the customers?

THE WITNESS: I, I would say that it -- I don't know -- the word "primarily" threw me off there. I think it benefits both customers and the Company, because a lot of the hedging is already included in the net power cost study.

What's not included, though, is as we move through the test period, or the year when the rates are in effect, and the loads, and resources, and prices move all over, you know, in the way that they do, then that's, you know, what the, the Company bears right now. But, you know, and a lot of it depends on the test period.

For example if we have a, you know, a test period that's, that's a future test period then we will -- as we prepare the net power cost study we will do an extract from our system and we'll pull out all of the hedges, whether they're swaps or whether they're the physical forwards.

You know, every, every contract we have done will be included in the net power cost study. And so it's only the ones that we, we didn't do -- that we did after the time we prepared the net power cost study that wouldn't be included in rates.

COMMISSIONER CAMPBELL: Well, let's limit this discussion then just to the financial swaps. Because I understand that you've always, under a least-cost environment, sold surplus power forward, to the benefit of customers. Or to get lowest cost to utilize your generation capacity.

So let's just set that aside and let's just limit ourselves to the financial piece. And it's probably because I'm dense, but how does the financial hedging benefit customers?

I mean, when you say that it reduces customer exposure to the market I'm still struggling with how, under the current regulatory method -- I understand how it happens in Questar's case with their 191 account.

But under our current method of regulation for your company, how does -- how do the financial hedges benefit customers?

THE WITNESS: In the same way that physical hedges do. It locks in the price so that it limits the volatility. So if, if, on the gas side if we, if we lock in at a $5 per MMBTU and, and the market goes to $10 or it goes to $3, the customers are still paying the $5.

It creates rate stability. And the same thing on the wholesale sale side.

COMMISSIONER CAMPBELL: Okay. It doesn't affect rate stability between rate cases. You're suggesting that it affects rate stability right when rates are established?

THE WITNESS: Yeah, I think that's a fair statement.

COMMISSIONER CAMPBELL: I'll -- I still don't see how that, how that -- you -- all right, thank you.

CHAIRMAN BOYER: Just a couple questions, Mr. Duvall. One is tempted -- and indeed some of the parties were tempted -- to evaluate the efficacy of hedging activities by looking backwards and seeing how much you actually saved over, you know, some other technique. Relying on the stock market or whatever.

And you've indicated that that, that's not the function of hedging anyway. But does it depend -- if one were to do that. If one were to Monday night quarterback your hedging activity, so to speak. Would it depend on what kind of a -- the environment in which you find yourself?

I mean, if you're in an environment where fuel costs are relatively stable or declining, then the hedging activities might not look as attractive as if they were in a different environment. Is that a fair statement?

THE WITNESS: Well, it's, it's a little more complex with our company, because we hedge both wholesale power -- long wholesale power, so we're hedging sales, and we're short gas and so we're hedging gas.

And while you may, in a declining market -- which is the example that everybody's looking at. They're looking at a declining market and the dis-benefit associated with hedging gas and not picking up on that declining price.

But on the flip side, we're hedging the sales and high prices.

CHAIRMAN BOYER: You've locked in higher prices on the sales?

THE WITNESS: We have, yeah. And you have to look at the whole picture to understand the, you know, what the result is.

CHAIRMAN BOYER: And so with that in view, is the -- are your hedging practices a fluid or kind of a dynamic process? I mean, do you -- like you're pretty well hedged right now, 90 or 100 percent. Does that change over time, depending on the economic circumstances in which you are operating?

THE WITNESS: Well, it would, it would -- I think if it were to change it would take a review -- a manage -- senior management review to change the policies as to what those are.

CHAIRMAN BOYER: Okay. Thank you Mr. Duvall.

Mr. Monson, back to you for redirect.

MR. MONSON: Thank you.

REDIRECT EXAMINATION

BY MR. MONSON:

Q. Mr. Duvall, there's -- I think there's been some confusion about how swaps relate to physical hedges. When, when the Company buys gas two years in the future does it agree to pay a fixed price, or does it agree to pay an index price, or both?

A. If you're speaking of the commodity, we could do it either way. But I think typically we buy the, the commodity on an index basis.

Q. So, so you're not agreeing that you're gonna buy it for $5 per MMBTU. You're agreeing to buy it for whatever the market is when it's delivered, right?

A. On the, on the physical side, yes.

Q. Okay. So then how does a swap, a swap relate to that?

A. Well, then the swap will protect against if the, if the market price goes to $15, like it did in 2008, if we had a swap at $5 or $6 then we wouldn't be exposed to that $15 market.

Q. And is that the basis for your statement that the two transactions together add up to the same thing as the former one transaction?

A. Yes, it is.

Q. Why does the Company use swaps but not options right now?

A. Well, the options, I think what we've talked about is we have, we have had a little bit of experience with them. And we've had some pretty fierce opposition from some of the parties that, that want to at a -- an option comes with a premium payment. And you may actually never do anything with the option.

And so the question is, should customers pay this, this premium if you never used it. So that if -- an example of that would be that if you, if you buy -- you could buy a gas swap at $5. Or you could buy a cap at $5, which is an option.

And, and, but the cap you'd have to pay a premium. And let's say you paid a $2 premium. So as long as gas came in at $5, under the swap you'd pay $5, but under the cap you'd pay $7. Because it would be the $5 for the gas and the $2 for the premium.

If gas fell to say $3, then under the swap you'd still pay $5. But under the cap you'd pay the $3 plus the $2 premium, so you'd pay $5. You'd be in the same situation.

So -- and I think it's pretty important to go through that and make sure that the parties and the Commission really understand what all the moving parts are of options before we move rapidly into them. And that's why we recommended a staged approach.

And we'd like to make sure that it's clear what the -- what all the parameters are associated with, with options before we would propose doing that.

Q. Commissioner Campbell asked you about the benefit to ratepayers of hedging in the current scheme with no ECAM. And I think -- I don't want to beat a dead horse, maybe you've said all you can on that subject.

But do you -- what is -- do you have anything else you want to say about the benefits to customers from hedging in the current environment?

MR. PROCTOR: Objection, it calls for a narrative. It's an inappropriate direct examination.

CHAIRMAN BOYER: Well, it does follow on what the cross examination was. But he did, he did have an opportunity to elucidate his thoughts on that. Maybe you could ask it a different way, your question.

MR. MONSON: I can ask it a different way.

Q. (By Mr. Monson) How does hedging in the current ratemaking environment benefit customers?

A. It -- the main benefit is that it provides -- it limits rate volatility. And in fact if you look at the testimony of Dr. Schell, for example, who's recommending that we reduce the amount that we hedge, she admits that -- or just identifies that when you do that you're gonna increase rate volatility.

So that the benefit of hedging -- so it's really how much rate volatility or lack of rate volatility is desired.

Q. You were also asked a question about whether the -- what -- whether changes -- or, or questions regarding whether hedging was prudent or not would be resolved in an IRP process or in a rate case.

When you say "rate case" are you referring simply to general rate cases, or are you referring more broadly to ECAM adjustment proceedings as well?

A. More broadly.

Q. So you consider an ECAM adjustment proceeding to be a rate proceeding?

A. Yes, I do.

Q. You were also asked about the guidelines and whether the guidelines talk about hedging. When were -- do you know when the guidelines for IRPs were prepared? Do you have any, do you remember?

A. I should know.

Q. Would you accept that it was in 1992?

A. I would accept that.

Q. Does it surprise you that the guidelines prepared in 1992 wouldn't discuss hedging?

A. No, it wouldn't surprise me, since that was really before electricity was a commodity.

MR. MONSON: That's all.

CHAIRMAN BOYER: Okay. Thank you Mr. Duvall, you may be excused.

Let's take a ten-minute recess and then we'll hear from the Division's witnesses.

(A recess was taken from 10:25 to 10:40 a.m.)

CHAIRMAN BOYER: Okay, let's go back on the record now and we'll hear from the Division's witnesses.

Mr. Peterson, were you sworn in Phase I?

MR. PETERSON: I believe so.

CHAIRMAN BOYER: Do you want to make sure?

MS. SCHMID: I would feel very comfortable if he could be re-sworn.

THE WITNESS: Okay.

CHAIRMAN BOYER: Let's just be sure.

(Mr. Peterson was sworn.)

CHAIRMAN BOYER: Thank you, please be seated.

Ms. Schmid?

MS. SCHMID: Thank you.

CHARLES E. PETERSON,

called as a witness, having been duly sworn,

was examined and testified as follows:

DIRECT EXAMINATION

BY MS. SCHMID:

Q. Good morning Mr. Peterson.

A. Hello.

Q. Could you please state your name, your employer, and your position?

A. Charles E. Peterson. I work for the Division of Public Utilities. And I'm a technical consultant.

Q. Have you participated on behalf of the Division in Phase II of this ECAM docket?

A. Yes, I have.

Q. Did you assist in the preparation of Division witness Mr. Douglas Wheelwright's testimony, which he filed in this phase in this docket on June 16th?

A. Yes.

Q. But you didn't submit any testimony on that date in your name in this docket, did you?

A. That's correct.

Q. However, on August 10th you did file testimony in this docket, in this phase, under your own name. And that testimony has been marked for identification as DPU-4.0SR; is that correct?

A. Yes.

Q. Why did you file this testimony on August 10th?

A. Based upon -- well, it was specifically in response to Mr. Duvall's rebuttal testimony that he had filed earlier. And it was based upon my experience in working in the IRPs particularly since 2007. And, and my general knowledge of issues related to front office transactions as they relate to the IRPs.

Q. So with this you are the Division's witness on market purchases; is that correct?

A. Yes, in terms of responding to Mr. Duvall's rebuttal testimony.

Q. Thank you very much.

MS. SCHMID: The Division would like to offer Mr. Peterson's testimony, marked as DPU Exhibit

No. 4.OSR, filed on August 10th, into evidence.

CHAIRMAN BOYER: Is there any objection to the admission of Mr. Peterson's surrebuttal testimony?

Very well, it is admitted.

MS. SCHMID: Thank you.

(Exhibit No. DPU-4.OSR was admitted.)

Q. (By Ms. Schmid) Mr. Peterson, do you have a summary to give this morning?

A. Yes, I do. In this part of the ECAM docket I've provided surrebuttal testimony in response to Mr. Duvall's testimony. Specifically, as I said earlier, I'm responding to his remarks regarding front office transactions, or FOTs.

The Division understands FOTs to be essentially power purchase agreements made primarily in the wholesale markets. And they're for a limited period of time. Usually no more than about a year, but they may be up to three years.

Mr. Duvall has made a number of claims regarding FOTs, or front office transactions, in his rebuttal testimony. The Division does agree with some of the positions taken by Mr. Duvall. Perhaps the most significant one is that the Division has consistently had the -- taken the position in this docket, or the ECAM docket, that it is not necessary to resolve the questions that have been raised revolve -- revolving around front office transactions before designing and implementing a power purchase -- or excuse me, a power adjustment mechanism for the Company.

The Division also agrees that -- with Mr. Duvall that building -- that by building generation capacity it is possible that ratepayers could become at risk if a lull falls such that the capacity -- that the Company has overcapacity, and the Company -- or the ratepayers may still be obligated to pay for the excess capacity. However, there's no current evidence that such an outcome is likely to happen anytime soon.

The Division remains concerned, as we've expressed in our comments in various IRP dockets and in this matter, with what it considers to be relatively high-level front office transactions engaged in by the Company. Particularly to cover its load in lieu of constructing its own generation plant.

The Division, however, does not re -- deem it prudent that the Commission order the complete elimination of front office transactions, or to hastily order the diminishment of front office transactions.

The Company's generation portfolio, as it currently exists, cannot be modified substantially in a short period of time. However, the Division does agree with the general idea expressed in the 2008 IRP by the Company that the Company should work towards reducing its reliance on front office transactions.

The Division believes that Mr. Duvall has, in places, mischaracterized the testimony of the Division. In particular, the Division does not believe that the IRP is necessarily the best place to resolve the issues concerning front office transactions, although it is one place where the issue may be discussed.

The Division also does not, as implied by Mr. Duvall, the Division does not recommend the elimination of, of front office transactions. Or -- the Division does not agree with Mr. Duvall's testimony in his rebuttal that an ECAM would -- or that, that an ECAM does not affect the incentives the Company has to build or otherwise deploy generation resources.

We believe that there are reasons to believe that an ECAM could encourage or incentivize the Company, in at least a small way, to avoid purchasing additional or otherwise acquiring additional generation capacity. And in my surrebuttal testimony I outline two or three ways that that could occur.

In sum, the Division believes that the Commission could explore, if not in this docket in another docket, a way of giving teeth to any level of front office transactions that the Division may deem appropriate upon further investigation.

And in my direct testimony filed on August 4th in regards to the design part of Phase II the Division has recommended a possible way or a possible mechanism of bringing in -- or connecting front office transactions to the ECAM in a way that would give some teeth to the Division -- or the Company's IRP goals for front office transactions.

The con -- otherwise the Division does not believe that Mr. Duvall has rebutted any of its testimony or positions regarding front office transactions.

And we continue to support our previously-stated positions that we are concerned that ratepayers are incurring that at risk, and it may not be sufficiently modeled in the IRP as it's been currently performed. With that, that's my summary statement.

MS. SCHMID: Thank you. Mr. Peterson is now available for cross examination.

CHAIRMAN BOYER: Thank you.

Thank you Mr. Peterson.

Let's go to the Company first for cross examination. Mr. Monson?

MR. MONSON: Thank you.

CROSS EXAMINATION

BY MR. MONSON:

Q. Mr. Peterson, am I supposed to ask you the questions about market reliance that relate to Mr. Wheelwright's direct testimony, or am I -- can I reserve those for him?

A. You may ask me those questions that are related to front office transactions or market reliance.

Q. Okay. Well, in Mr. Peter -- Mr. Wheelwright's direct testimony, on lines 92 to 95, he makes a statement about modeling related to front office transactions. Do you have his testimony?

A. Yes, just a moment. Which lines were you referring to again?

Q. Ninety-two to 95. It's on page 4.

A. Yes, I have them.

Q. You have that? Do you see there he says the --

"While there are some benefits to the Company using these front office transactions as part of its strategy, the concern for the Division is that the Company has not been adequately modeling the potential risks it and ultimately ratepayers face by being subject to the whims of a potentially volatile and costly energy market."

With regard to Commissioner Campbell's question regarding the current ratemaking regime and structure with no ECAM, how would customers be -- have risks from the whims of a potentially volatile and costly energy market?

A. The customers potentially have the risks in that the Company may be incurring higher net power costs and report those costs in their rate case applications due to their reliance on front office transactions.

In other words, it is a potential that the Company -- there's two ways this could happen. The first way is that, that the wholesale markets could end up being higher than what the Company could generate power for.

And if the Company needs to buy power in those markets, then ratepayers are at risk that way. The other method is one that has been discussed in the IRPs, and that is is that the Company in its modeling -- it's an either/or situation. They either have front office transactions, or they have generation capacity.

And the Company is not able -- would not be able to make an economic choice between generating power or purchasing on the market, depending -- if it had -- if it did not have the generation capacity to make that choice. It would be just subject to whatever the markets are.

Q. But if rates are set in a rate case and then the market goes up, do ratepayers bear the risk of that?

A. Not immediately, but it could happen in -- when the Company immediately files for a new rate case in order to cover that -- those higher costs.

Q. Thank you. This statement suggests that, that the Company has not been adequately modeling the potential risks. Are you familiar with the stochastic analysis that use - that is used by the Company in the IRP process?

A. Well, in general terms I'm familiar with it. I know that they have a model where they, where they allow certain variables to fluctuate.

Q. And one of those variables would be price for the commodity, right?

A. Yes, electricity price is one of them.

Q. So in that modeling don't they take into account, through a Monte Carlo analysis, what might happen if the price is higher than is anticipated in the future?

A. Well, they, they model what the cost would be based upon the generation -- based upon the portfolio that's assumed to -- that the Company is assumed to have at that time in that par run. So to some extent they are modeling some of the risks, but they're not modeling all of them at the detail that I'm suggesting. At least that is my belief.

Q. Are you suggesting that they ought to use only a high-cost scenario in deciding how to plan for future resource needs?

A. No, I don't think they should use only a high-cost scenario. I think that the, the first and best scenario would be the middle-of-the-road scenario or a best-guess scenario. But the stochastic model, as I understand it, only shows what the effects of a given portfolio would be given the variability that's built into the stochastic model.

And then of course, you know, the usefulness of that is based upon the inputs into that model and how many variables are allowed to fluctuate. So there are limitations in this modeling.

Q. Well, and that's what I was getting at. I mean, if the Company -- if in their model one of the cases is the case where there's high, high energy costs or high fuel costs, either one, and they've got a level of front office transactions in that portfolio, aren't they, aren't they testing, essentially, the risk associated with an increase in price?

A. Well, they're, they're testing the level of front office transactions that they, they have assumed in a given portfolio. And -- but that does not answer the question about the risk of what happens if front office -- if they have the option, for example, of running plant or running -- or buying on the market.

I do not believe the stochastic method drills down in that detail, for example. And the other risk that it may not be covering has to do with reliability. And what happens if the Company -- if there's a major transmission outage that affects the ability of the Company to purchase on the, on the grid. On the wholesale market. Or if there's unexpected outages.

Those are rely -- those reliability issues are not covered in the grid model, since -- or the par model, since it's a very high-level model.

Q. Wouldn't a lack of transmission affect both purchased and generate -- loan-generated resources?

A. Not necessarily, it depends on where the outage is.

Q. Okay. In your surrebuttal testimony on lines 29 to 33, related to what you were just talking about, you say:

> "The Company, if it has owned plant, can choose between running its plant and purchasing on the market, depending on which is most economic. If it does not have the owned plant to cover its load, the Company has no choice but to purchase on the market and thereby subject itself and ratepayers to the risks of the wholesale market."

Is your point here that the Company has more flexibility if it has own -- if it owns capacity?

A. Yes. That's always been the point in the Division's comments in the IRP as well.

Q. Okay, but aren't there costs associated with owning capacity?

A. Well, of course there's costs. But there's costs in purchasing on the open market, too.

Q. Okay. But if you own capacity don't you have the cost of the plant which is included in rate base?

A. Well, of course.

Q. And if -- and you also have the O&M associated with the plant that's presumably included in setting rates?

A. Of course.

Q. So the flexibility that you're seeking here comes at some cost, right?

A. Well, there's always a cost to do something. Nothing is cost free. In one way or another there is going to be a cost. But the question is, is whether the -- this gets to the point of the risk that the Company faces.

And if they have generation capacity, then they can make an economic choice. Whoever is selling the power to PacifiCorp on the open market also presumably has a plant, and has O&M, and has fuel costs, and these other things.

So the question is, is whether it's going to be better -- whether the Company has flexibility to make an economic decision, or whether it has locked itself in to reliance on a market that we know can be variable, for various reasons, which may not have anything to do with the underlying fuel or O&M costs.

Q. Okay. Let, let's take a hypothetical here to test your -- what you're saying. Are you suggesting that the Company should have gone ahead with the Lakeside II proposal last year so that it would have capacity available for this flexibility?

A. Well, are you talking about in terms of 20/20 hindsight, or in terms of the time that it was under consideration?

Q. Why don't you deal with both of them. First deal with 20/20 hindsight.

A. Well, with 20/20 hindsight I think it's, it's clear that in the short run at least that the Company may probably make the right decision. In the short run again. In the long run it's less clear. And at the time the decision was made it certainly wasn't clear to the Division that that was the proper course.

Q. If you were to follow your position to its logical conclusion, wouldn't the Company want to buy -- own resources in excess of its load requirements, because then it would have more flexibility in dealing with changing market conditions?

A. Well, obviously there's a point where it wouldn't be prudent to cover all of the potential peak loads and everything that may come into play. The Company has to make a rational choice on that.

The Division does not claim that it knows what the optimum level of front office transactions are. Or what the optimum of -- amount of peaking plant is. However, we have raised this concern consistently.

And the Company has even admitted in its 2008 IRP that it basically agrees that front office transactions increase the risk -- their own analyses show that -- to customers.

And their own analyses -- the Company's own analyses show that there's a negligible increase in the, in the cost of the portfolios that have fewer front office transactions, and noticeably less risk than the portfolios the Company seems to want to choose.

Q. So you're talking about a comparison between portfolios and the IRP?

A. Yes, I am. The Company -- that's, that's where this discussion has originate -- has originated from in the IRP dockets. Or IRP processes. And in 2007, and again in 2008, parties raised the issue of their concern.

In 2008 the Company finally admitted that their own analyses show that in general, as a generalized statement, the parties' concerns are well placed. That front office transactions increase risks noticeably, with little or no increase or negligible increase in cost.

Q. Let's turn to lines 190 and 208 -- through 208 of your surrebuttal.

A. Excuse me, 190 which?

Q. One ninety through 208. It's a pretty long section.

A. Okay.

Q. It's just an answer. It's a paragraph there.

A. I have it, yes.

Q. And in that you're talking about Mr. Duvall's testimony that an ECAM wouldn't reduce the Company's incentive to invest in new plants because the Company only earns a profit on rate base and not on expenses; is that right?

A. Yes.

Q. You're responding to that? And you agree in that answer that a rate base regulated utility would have a natural propensity, as you say, to build it in theory, right?

A. Right.
Q. But on lines 194 and 195 you state that this natural propensity has not spurred the Company in recent years to an aggressive generation acquisition program; is that right?
A. Right.
Q. Are you aware that the Company has added approximately 1,500 megawatts of gas-fired plants in recent years?
A. What do you mean by "recent years"?
Q. Starting in -- from 2005 to the present?
A. You mean starting with the Lakeside and Currant Creek plants?
Q. Right.
A. And then the Chehalis acquisition?
Q. (Moves head up and down.)
A. That would add up to approximately 1,500 in -- well, I guess the construction would have had to have started before 2005, but the last six or eight years.
Q. Okay. And it's added 1,500 megawatts of wind resources since MEHC bought the Company?
A. At least in terms of nameplate.
Q. And the Company's currently involved in an RFP for additional capacity?

A. Well, it's been involved in an IRP for additional capacity for several years now.
Q. Okay. But it is currently involved in one?
A. Well, yes.
Q. Okay. And -- but you say that's not aggressive? There's not an aggressive acquisition program?
A. That has not reduced the front office transactions that the Company admits is -- puts ratepayers at additional risk. It's admitted it in its 2008 IRP. And an aggressive acquisition or construction program would be to bring the, the generation capacity of the Company more in line with its expected load.
Q. But as we've already discussed, you wouldn't necessarily want to do that if the prices for new capacity didn't indicate that it was -- made sense to do it at a given point in time; is that right?
A. Well, I -- well, of course there's going to be decisions that are going to have to be made. And whether they're based on -- completely on economic decisions or -- that are right or wrong, then I guess we can either -- we can always second guess.
But yes, the, the Company needs to construct or acquire generation capacity in a prudent manner. I

would agree with that as a general statement.

Q. Okay. And you talked about second guessing. If an ECAM's in place we can second guess, can't we? Because aren't we looking historically at what the Company did and knowing whether or not it made sense in an ECAM review proceeding?

A. Well, that remains to be seen whether we can effectively second guess what the Company does, or whether we should. Presumably the Company would want an ECAM to be -- or the results of an ECAM to be implemented into rates in a fairly timely manner and not be bogged down for months or years in an investigation of its prudence.

On the other hand, the regulators and I do not see any way that we can second guess the Company on all of the thousands of transactions and decisions that it makes during a year of operating its system. So I think the -- an ECAM does not necessarily put the Company at risk for second guessing.

Q. But at least there will be a hindsight review; is that right?

A. Well, there will be some hindsight review, but it -- again, it remains to be seen how effective that review will be.

Q. In the case of Questar Gas with its gas balancing account, isn't it the fact that they file for a change in rates and then the rate -- that change is usually granted on an interim basis?

A. That's correct. And --

Q. And sometimes the audits aren't completed on that for two or three years?

A. That's my understanding.

Q. I know there's an effort to speed that up, but that's the way it's been sometimes recently, hasn't it?

A. Again, that's my understanding. I'm not intimately involved in the passthrough account with Questar.

Q. And until the audit's completed they aren't final rates and therefore could still be subject to change; is that right?

A. They could be subject to change.

Q. Okay. You know what the -- one reason the Company might not act in accordance with its natural propensity to, to add rate base is that the parent holding company might have alternative investments which would promise a higher rate of return; is that right?

A. That's something I discuss in my testimony, yes.

Q. And if -- the way that would happen would be that they -- the parent would take money from the utility to use for these alternate investments, right?

A. Well, there's various methods that might happen. The most obvious would be that the Company would -- the parent would have the Company dividend to -- money. The Company could withhold further contributions which it has made.

The Company could otherwise cause the utility to postpone or otherwise spread out its capital expenditure program. So those would be mechanisms by which the parent company could affect the capital expenditure program of, of the utility.

And there may other ways that I'm not thinking of right now, but those are some of the more obvious ones.

Q. But if the, if the parent wants to use those funds to invest in a more profitable venture it would have to, have to get a dividend of those funds, right?

MS. SCHMID: Objection, calls for speculation.

CHAIRMAN BOYER: Let's let him answer that question. Overruled.

THE WITNESS: Well, there's different methods that the Company could -- the parent company could,

could get funds from the -- more effectively get funds from the utility. One -- the most straightforward would, of course, be dividends.

The other method that would be more indirect would be borrowing money against -- meaning the parent company borrowing money against the assets of the utility. And using that money to fund its own -- well, its other projects. Although that may run up against certain ring fencing provisions.

And the third way mentioned is that they could, of course, withhold the funding. And they may at some point increase the fees that go to the parent company.

Q. (By Mr. Monson) If there was an increase in fees, that would be something that would be scrutinized in a rate case, right?

A. It's -- well, potentially all of what I'm talking about can be scrutinized in a rate case. But how effective it would be in changing behavior is an open question.

Q. Now, with regard to the borrowing, as you mentioned, that would be prohibited by commitments and conditions for approval of the merger, right?

A. Potentially it could be, although I wouldn't guarantee that (inaudible - the witness is speaking too softly) found by clever attorneys.

THE REPORTER: I'm sorry, can you speak up and repeat that?

THE WITNESS: I'm sorry, I didn't want to speak too loudly on that. I said that I wouldn't guarantee that, that the parent company may not find ways around the ring fencing prohibitions.

Q. (By Mr. Monson) And -- well, we're -- and maybe clever accountants too, right?

A. Clever accountants, maybe even a clever economist.

Q. Yeah, okay. Just so we include everybody.

A. Yeah.

Q. All right. But you're aware that the Company -- the parent of Rocky Mountain Power hasn't received any dividends since it acquired the Company; is that right?

A. That's correct.

Q. And so it's actually allowed the Company to retain 1.8 -- 1.9 billion, essentially, in retained earnings since it acquired the Company. Are you aware of that?

A. Well, I'll accept your $1.9 billion. I don't know the exact number.

Q. And, and with regard to withholding

investment -- which is another point you raised -- the parent company's invested over $1 billion in the Company since it acquired it?

A. I believe that's mostly correct, more or less.

Q. So at least the alternative investment opportunities of the parent is apparently not the reason the Company hasn't been more aggressive in acquiring new plants?

A. At least not to this point. I can't -- that was raised as a hypothetical potential. And it was not meant to accuse the parent company of, of engaging in that sort of behavior to this point.

Q. You talked about the prudence review and the problems with reviewing all of the Company's transactions. Let me just pose a hypothetical to you. Suppose the Company were relying heavily on front office transactions and the price of electricity, or gas, or both went up in such a way that the net power costs just increased astronomically compared to what had been presented in the general rate case.

Do you think that would require a detailed review of transactions, or do you think the Division and other parties would simply object to it as being unreasonable?

A. Well, again, it would depend on the exact situation. It's certainly conceivable that the parties would simply object as -- and again, it would -- the objection would be that the Company was imprudent in having the level of front office transactions that it was engaged in. Which, in part, is part of the concerns that we're raising.

Q. So the Division has an opportunity when the Company files a general rate case, in reviewing the net power costs, to review the level of front office transactions that are included in the, in the net power cost study in that case, right?

A. The Division and other parties, of course, have that opportunity.

Q. And so you can review it on a projected or forecast basis in that situation; is that right?

A. Yes.

Q. And then when the Company seeks to adjust the ECAM, in an annual proceeding I guess is what we're talking about, the Division can review the actual purchases of power and the actual purchases of gas in that context, right?

A. It could.

Q. So you'd actually have -- with an ECAM you'd have two bites at the apple; is that right?

A. Well, it depends on how quickly the proceeding goes. If you're going to imagine that the audit process can go on for years with interim rates, then I suppose that would be true. There would be two bites at the apple.

MR. MONSON: I think that's all I have. I'm just trying to see if I had any other questions for Mr. Wheelwright on market reliance. I don't think I did, so.

CHAIRMAN BOYER: Okay. Thank you Mr. Monson.

Mr. Proctor? No questions.

Ms. Hayes, questions for Mr. Peterson?

MS. HAYES: No questions.

CHAIRMAN BOYER: Mr. Dodge?

MR. DODGE: No questions.

CHAIRMAN BOYER: Mr. Evans?

MR. EVANS: Just a couple, Mr. Chairman.

CROSS EXAMINATION

BY MR. EVANS:

Q. Good morning Mr. Peterson. Dr. Peterson?

A. Mister.

Q. Mister, okay.

A. Although it could be an honorary title.

Q. You note in your testimony that the Company's paid out 173 million as a result of being on the wrong side of its electric and natural gas swaps.

THE REPORTER: Keep your voice up please, Counsel.

Q. (By Mr. Evans) Give me -- I'm getting there.

A. Okay, where --

Q. That, that's line 105.

A. Of my surrebuttal?

Q. Of your August 4th testimony.

A. Oh, of my August 4th testimony. Okay, I'll accept that it's that.

MR. MONSON: Can I just -- I don't know if I want to object or I want to just note that we're now talking about testimony in Phase II Part 2.

MR. EVANS: Okay. Well, that --

MR. MONSON: Is that --

MR. EVANS: Well, and maybe, maybe I'll just keep the questions general, because I think part of that August 4th testimony does pertain to what we're talking about here today.

Q. (By Mr. Evans) So let me just ask you some questions generally, without specific references to your testimony. It sounds like you think that in -- the Company could do better in its front office transactions and hedging practices; is that accurate?

A. Well, with regard to front office

transactions the Division has raised concerns about the level and what we see as the added risks that ratepayers are facing.

We're not proposing at this time that we know a better front office transaction than what the Company has been doing. Although we think -- and we agree with other parties -- that there is a concern there and that the -- there's a need for further investigation.

With regard to the hedging, this is, this is part of the problem that the Division has faced -- and perhaps other parties as well -- is getting our arms around what is -- what exactly is going on with the Company's hedging.

We heard earlier today, for example, that Mr. Duvall complained that Mr. Wheelwright, in his analysis, only included swaps. To some extent we consider that -- the financial swaps to be of peculiar interest.

And we -- at least I have understood in the past that the Company has represented that the financial swaps -- the electric swaps and the gas swaps -- are supposed to more or less offset one another. And what is of interest to me is that historically they don't appear to have been.

Now, Mr. Duvall suggests -- or seems to suggest in his testimony this morning that we need to, we need to expand our vision of what is included in the, in the hedging practices of the Company. And that may be true, but it highlights the difficulty that the Division has had in trying to understand this rather complex situation that comes under the rubric of hedging.

Q. Let's -- let me ask you a question, then, just about the financial swaps. If these were to be disallowed in the ECAM would that create a problem, as far as you are concerned, for the Company's incentives?

A. Well, it would, it would create an incentive to the Company to perhaps reduce or eliminate its hedging program. Any -- anything that they're not going to receive recovery for is going to be an incentive of one form or another.

Q. And when you say "hedging program," let's just confine it to the swaps.

A. The swaps, yes.

Q. Okay. So it would be a disincentive to continue its current practice of buying these swaps?

A. That would be my, at least initial evaluation of the incentives. Whether or not that would actually cause the Company to reduce or eliminate its financial swaps is another question. But certainly there's incentive there that would tend toward that action.

Q. And so that, that would be the reason that you would say, Let's not eliminate swaps altogether from an ECAM?

A. Well, that's why in my August 4th testimony that I say that the Division decided that we were not going to try to pick and choose specific items within the NPC at this -- at least at this time because it could create incentives that we may not want it to create.

Q. And you are aware, of course, that the Company is hedged on its natural gas swaps almost fully for the next two years?

A. Yes.

MS. SCHMID: I'll object. I believe these questions are more properly for Mr. Wheelwright on the amount of hedging.

MR. EVANS: Okay. Well, I -- let me, let me finish with incentives, if I might.

MS. SCHMID: Okay. It's up to the Commission, of course.

Q. (By Mr. Evans) If the Company --

MR. EVANS: Well, it's just a follow up to his answer, if the Commission doesn't mind.

CHAIRMAN BOYER: Mr. Peterson, seems well versed up to this point in all the questions you've asked, so go ahead.

Q. (By Mr. Evans) So if it were the case that the Commission disallowed swaps into the ECAM, and that -- and if it were also the case if that were an incentive for the Company to reduce its purchase of swaps, that would -- we wouldn't see any impact for two years, would we?

A. Well, we could see a, an impact -- well, it wouldn't -- I'll have to think through this.

If the, the swaps were eliminated from the ECAM, then there would not be an ECAM adjustment that would reflect the activity of the swaps. However, that may not preclude the Company from asking for recovery in a rate case.

Q. They have, now, a rate case.

A. -- well, they have the -- their forecast --

Q. Correct.

A. -- what they forecast their net swap position would be in the rate case. So.

Q. So the question was --

A. I don't, I don't know if I'm answering your question.

Q. The question was any, any significant impact over the next two years on Company -- on perverse incentives to the Company. It wouldn't see the impact for at least two years, would it?

A. Well, the Company has entered into contracts that would require them -- that they would be required to fulfill. And then -- so the Company wouldn't see any impact on its costs for at least two years. Or at least minimal impact.

However, whether they get to recover those costs or not, they may see an impact more, more quickly than two years. Based upon what happens in the next general rate case, for example.

Q. They would, they would be at risk for recovering the amount that's currently in rates?

A. Well, the -- for the -- to the extent that the swaps are currently in rates, then as long as those rates remain in effect then they're not at risk. But if they -- if we get into another general rate case then they would be at risk for recovery.

Q. So I think I'm hearing no impact.

A. Well, I guess the -- I'll be the typical economist and say, Well, it depends. On what your assumptions are.

Q. Okay.

A. But if -- poten -- I guess potentially, you're right that there may not -- there's potential that we wouldn't see an impact for two years.

Q. If we completely left the swaps out of the ECAM?

A. Right.

Q. Okay. Thank you.

CHAIRMAN BOYER: Anything further, Mr. Evans?

MR. EVANS: That's all I have. Thank you, Commissioner.

CHAIRMAN BOYER: Thank you.

Commissioner Allen?

COMMISSIONER ALLEN: Thank you Mr. Chair.

Mr. Peterson, I think, having read the testimony and listened to the hearing so far today, I've got some clarity when it comes to the risks and benefits to customers, consumers.

Looking at the other side of my regulatory hat, I've got some questions that popped in my mind here about the Company's health and how this might affect them long term.

I think we have some previous testimony from you in other cases that the Company has probably been underperforming in terms of their allowable rate of return. Is that -- is my memory correct?

THE WITNESS: Yes.

COMMISSIONER ALLEN: And has that still been the case as far as the recent information you have, or have they made improvements?

THE WITNESS: It's generally been the same. They -- their return on equity has typically been less than 10 percent.

COMMISSIONER ALLEN: And as we move forward and we look at these issues that deal with front office transactions and hedging are these tools in their tool box to improve that rate of return? Or are they minimal? Can they be maximized? Is one more helpful than the other?

THE WITNESS: Well, the -- front office transactions is a method that -- of -- in one -- in the first instance it allows the Company to delay, postpone purchasing or acquiring, building, own generation capacity. And maybe it would be prudent for them to do that into perpetuity.

It does not necessarily affect their ability to earn their allowed rate of return, except to the extent that where here in Utah we have forecast test years. If the forecast is wrong about the cost of front office transactions, then they're, then they're at risk that they could incur additional expenses that were not in rates, so to speak.

Or the flip side could happen where the -- they could have over-forecast the cost of front office transactions and they would reap a benefit that way.

To the extent that their forecasts are unbiased -- that is, that they tend to be equally high or low over time -- then it would be rather, then it would be rather neutral. The hedging program is supposed to be neutral in terms of whether they earn their allowed rate of return or not.

The swaps have historically been, apparently they've been underwater. And so it has been a drag on their earnings on a historical basis.

COMMISSIONER ALLEN: So I guess what I'm hearing you say is that they're tools. But they're not significant because they're supposed to, when properly run, net out to everyone; is that correct?

THE WITNESS: At least over time. Any, any one year, of course, they could be high or low. You know, in the money or out of the money, so to speak. But over time they should be neutral. At least that's the intent.

COMMISSIONER ALLEN: Would there be -- yeah, one final question. Would there be -- in the long run. If I'm looking at the long-run performance.

Would there be an advantage -- you mentioned front office transactions maybe in the short run being a better setting.

But wouldn't there -- is it possible there would be an advantage to building plant, and properly proving up the new revenue requirement, and then getting that rate of return? Is that better than front office transactions in the long run? Or, like you say as an economist, does it depend?

THE WITNESS: Well, as Mr. Monson had me point out -- or he highlighted in my testimony, in the traditional rate based regulated company -- which PacifiCorp more or less is still -- it's to the advantage of ratepayers -- or not ratepayers, stockholders to build plants, to acquire assets and put them in rate base, because that's what they earn their rate of return on.

The caveat I highlighted is, is that earning 10 percent rate of return on your investment, as an example, is well and good. But if you have an opportunity to earn 15 percent somewhere else, then there will be a tendency to want to invest somewhere else.

COMMISSIONER ALLEN: Okay, thank you. That helps, thank you.

CHAIRMAN BOYER: Commissioner Campbell?

COMMISSIONER CAMPBELL: I think I just have one question, but I'm gonna perhaps lay some context for that question. I understand in the IRP process that they're planning a single system, yet you have differing states with differing viewpoints of the world.

For example, let's assume that Utah is a, kind of a steel-in-the-ground state, where we like to see capacity. And Oregon and Washington are perhaps states that are more trustworthy of front office transactions, or historically have been. And Utah was along for a number of years, and then we had that power crisis when we were actually short and kinda saw what reliance on the market could potentially do to us.

Yet in the Northwest, as I try to understand why they're more comfortable with front office transactions, they seem to have access to very liquid markets up there with the Mid-C market and others.

My question to you is, do you think the Division viewpoint or policy as far as own capacity might change as the Gateway system is built out, and we have like Gateway West, and we have greater, greater ability to access the markets that the

Northwest has been able to access for a lot of years?

THE WITNESS: That's a possibility. Certainly if we have access to power from a wider geographical area, then that diminishes the potential for ending up being short. So that is definitely a possibility that our viewpoint would change.

Of course it would depend on whether or not, in surveying those markets, there appear to be adequate capacity to cover potential demands. You know, is there a 12-or-15-percent planning reserve margin, so to speak, on the entire Western grid?

If there is, then maybe we would be more comfortable. And I'm just bringing that up as a -- the 15-percent planning reserve margin as an example. Maybe not a good one. But yes, I think you're right, it could change.

COMMISSIONER CAMPBELL: Do you know if, in the IRP, the Gateway project affects, at all, the front office transactions? I mean, does the IRP calculate if there's greater liquidity for, for the Eastern side of the system with the Gateway project in the IRP?

THE WITNESS: If it does, I'm not familiar with how that would work. My knee-jerk reaction would be to say at this point it does not. I -- but I haven't, I haven't seen evidence that it does. At least, I can't recall.

CHAIRMAN BOYER: Okay. Thank you, Mr. Peterson.

Any redirect, Ms. Schmid?

MS. SCHMID: Yes.

REDIRECT EXAMINATION

BY MS. SCHMID:

Q. Just a couple of questions related to the questions from Mr. Evans. If swaps are disallowed from an ECAM, will natural gas costs still be in?

A. Yes.

Q. Would those natural gas costs be solely un-hedged?

A. Well, they would be, they would be -- they could be hedged in a physical sense, in that they've purchased -- they could purchase gas ahead of a specific price. Mr. Duvall mentioned that.

Q. To what extent would that pass on gas price volatility to customers?

A. I'm sorry, which -- what would pass on?

Q. The physical, the physical hedge. To what --

A. Well, it's -- physical hedge, if it's, if it's tied to an index, then it would pass on to customers the -- whatever volatility -- or potentially reflect the price or the volatility of the price in a rate case as the Company tried to forecast its, its natural gas costs.

Although once the rates are set, then the customers would no longer see volatility.

Q. Are you aware that the Company is planning on filing a rate case in January?

A. That's what the Company has indicated, yes.

Q. If the Commission disallows swaps in an ECAM, could that affect how the Company files its next rate case?

A. Well, whatever -- there's a lot of things that -- well, the answer is yes, it could. But I have no knowledge of what the Company might do.

MS. SCHMID: Thank you.

CHAIRMAN BOYER: Okay. Thank you, Mr. Peterson. You may be excused.

THE WITNESS: Thank you.

CHAIRMAN BOYER: Let's begin with Mr. Wheelwright, Ms. Schmid.

MS. SCHMID: Okay.

CHAIRMAN BOYER: And we'll see how far we get before lunch.

Mr. Wheelwright, you have not been sworn in this proceeding, have you?

MR. WHEELWRIGHT: No.

(Mr. Wheelwright was sworn.)

CHAIRMAN BOYER: Thank you, please be seated.

DOUGLAS D. WHEELWRIGHT,

called as a witness, having been duly sworn,
was examined and testified as follows:

DIRECT EXAMINATION

BY MS. SCHMID:

Q. Good morning. Could you please state your full name, position, and employer, for the record?

A. My name is Douglas D. Wheelwright. I'm employed by the Division of Public Utilities as a utility analyst.

Q. On behalf of the Division have you participated in this Phase II of the ECAM docket?

A. Yes, I have.

Q. Did you prepare testimony premarked for identification as DPU Exhibit No. 2.0, both a confidential and a redacted version, and testimony marked as DPU Exhibit No. 2.0SR, your surrebuttal testimony, both confidential and redacted, with its accompanying DPU Exhibit No. 2.1SR, both in confidential and redacted form?

A. Yes, I did.

MS. SCHMID: The Division would like to move into evidence DPU Exhibit No. 2.0, in both confidential and redacted form, 2.0SR, and 2.1SR, also in confidential and redacted form.

CHAIRMAN BOYER: And you've had no corrections to those?

THE WITNESS: No. No corrections.

CHAIRMAN BOYER: Are there any objections to the admission of Mr. Wheelwright's direct and surrebuttal testimony, together with exhibits?

Okay, they are admitted.

MS. SCHMID: Thank you.

(Exhibit Nos. DPU-2.0, 2.0SR, and 2.1SR were admitted.)

Q. (By Ms. Schmid) Mr. Wheelwright, do you have a summary you would like to present today?

A. Yes, I do.

Q. Please proceed.

A. Thank you Commissioners. The purpose of my testimony is to present information and recommendations relating to PacifiCorp's current hedging policy and practices and how it relates to the proposed ECAM.

The current hedging program has been a concern of the Division and other parties for some time. Issues relating to the amount and the duration of the Company's hedging program have been raised in this docket and in the last two general rate cases.

There's been a lack of understanding concerning the amount and the duration of the current hedging program, as well as the extent and price fluctuation in the existing contracts. Some parties have questions -- questioned the need or appropriateness for an ECAM, primarily based on the structure and the extent of the current program.

The Division is concerned that the current hedging strategy has been conducted without the scrutiny or approval of regulators, and has not been determined to be in the best interest of the Company or its ratepayers.

It puts both the Company and ratepayers at risk. The Company is at risk for non-recovery of a portion of net power costs if it is determined that the hedging program has not been prudent. The ratepayers are at risk if the Company is required to pay significantly higher prices compared to the current market price.

The Commission should provide guidance to the Company concerning the direction and the appropriate goals for a hedging strategy. There should be an understanding of the priorities for price stability versus minimiza -- versus cost minimization from the perspective of both the Company and the ratepayers.

The existing hedging program has been designed to reduce the volatility in the price of natural gas commodity paid by the Company. The current program does not result in the least cost, but does provide a degree of stability for ratepayers.

Due to the structure of the long-term transaction, the Company has not been able to take advantage of the drop in the natural gas prices that has occurred during the past two years. The Company has acknowledged that hedging is a dynamic issue, and that market conditions are constantly changing.

However, the Company has also acknowledged that it has not modified the risk tolerance position in the hedging program for several years. Based on the forward price curve provided by the Company and outside sources, it appears that the price for natural gas will remain near the current level for some time.

This would make a review of the current hedging program appropriate and would allow for some comparison to other utilities. The Division and other parties have made recommendations that the Company prepare an analysis that would include the use of options or other financial products that have specific price bands.

These products could limit the exposure to wide swings in the commodity price, and could certainly protect the Company from rising prices and allow ratepayers to participate should prices fall. The Company has agreed to look at the possible use of options, but would like to delay any further review until the next IRP process.

Delaying a focused review of the Company's hedging practices until the 2011 IRP would needlessly delay a review of this issue. And would require parties to obtain updates to the substantial information concerning the Company's hedging practices that has already occurred.

In addition, it would put review of this issue into the IRP process, where parties would not be allowed to question the Company or other witnesses under oath. It would also put hedging into an acknowledgment process, where there is no clear Commission approval. And where the Company is under no clear obligation -- or no clear legal requirement to follow the direction provided by the Commission.

A better solution would be to use the existing hedging docket, 09-035-21, and proceed with a comprehensive look at the current program and allow parties to present alternatives. If changes are recommended a revised strategy could be submitted to the Commission for approval, with implementation by the end of 2011.

Once a hedging strategy has been established, the strategy would be reviewed by the Commission every two years under a separate docket.

The Division has recommended that the Company separate the financial and the physical hedges in future reporting, and separate the natural gas and electric hedging strategies. This will allow parties to review the performance of the hedging strategy of each commodity independently and determine if there -- if changes are needed.

While the Company has agreed to separate the physical and financial hedges, it does not want to separate the two commodities due to price correlation and spark spread.

While there is a correlation, the dollar value of the offset between the natural gas and electric swaps is not equal. A review of the two commodities should be independent of each other, since the desired outcome would likely be different.

As a consumer of natural gas, the Company would want to protect against a possible increase in the commodity price. As a seller of electricity, the Company would want to stabilize revenue and protect against possible price decrease.

The Company's expressed concerns relating to the different requirements and guidelines for the various states in which it operates. This concern has some validity, but should not impact the hedging decision of this Commission since none of the states in which PacifiCorp operates has provided guidance concerning hedging or the use of options.

Since Utah represents over 40 percent of the PacifiCorp load, the responsibility to establish a hedging policy and direction should begin within this Commission. In the event that another state provides hedging requirements in the future, the Company could present any conflicts to the Commission.

As stated before, the current hedging program has been a concern of the Division and other parties for some time. As evidenced by the discussions this morning, there still is a -- quite a bit of confusion on this issue.

The issue should be specifically addressed by the Commission in order to provide guidance and direction to the Company. And to protect, not only the Company, but also ratepayers. Thank you.

CHAIRMAN BOYER: Thank you Mr. Wheelwright.

Mr. Monson, if -- are you interested in pursuing cross examination before we break for lunch, at the risk of being interrupted mid-stride?

MR. MONSON: Whatever is your pleasure. I mean, I can either start -- I don't think I'd finish before lunch.

CHAIRMAN BOYER: All right. Let's take an hour and-a-half recess for lunch and then we'll commence with cross examination.

Thank you Mr. Wheelwright.

(A recess was taken from 11:44 to 1:18 p.m.)

CHAIRMAN BOYER: Let's go back on the record.

Mr. Monson, you were about to commence your cross examination.

MR. MONSON: Thank you.

CROSS EXAMINATION

BY MR. MONSON:

Q. Mr. Wheelwright, would you open your direct testimony to lines 211 and 212?

A. Yes, I have that.

Q. Okay. And there you say:

"The Company is unable to respond to short or even intermediate-term changes in markets."

Is that right?
A. Yes.
Q. Now, you're aware that the company updates its models every day based on changes in loads, markets, market prices, and spark spreads, right?
A. Yes.
Q. And so -- and you -- are you aware that these changes affect the Company's position, whether it's long or short, or open or closed, or whatever?
A. Yes.
Q. And so as load forecast and prices change, the Company is able to have -- to some degree to respond to the market, isn't it, in its hedging program?
A. No, I don't believe it is. Because if they're hedged a hundred percent two years in advance, they can't do anything -- if the prices go down, they're locked into that price. And can't take advantage if there's a drop in the price.
Q. Okay. Are they ever, are they ever hedged a hundred percent two years in advance?
A. According to the information, yes. Pretty close to. According to the year-end 2009 information, I think they're about 97 percent hedged.
Q. The year?

A. With financial hedges.

Q. Okay, financial hedges. And are you saying -- in which year were they hedged?

A. They're -- well, I can get you the specifics.

Q. Is it what you tes -- is it from the 10-K?

A. Yes.

Q. That you talked about? Okay, we're gonna talk about that in a minute, so.

Okay. So you're talking about financial hedges. And you're talking about one to two years in advance, right?

A. That's -- yeah. If they're locked in at nearly 100 percent up to 24 months in advance, they can't take advantage if there is a drop in the price of natural gas.

Q. Okay. Now refer to your direct testimony, lines 218 and 219, please.

A. Okay.

Q. You say:

"There has been no information presented to indicate that the current level of hedging has been determined to provide the best protection for the Company or for ratepayers."

Right?

A. Yes.
Q. Okay. But you do agree in your testimony that hedging -- the hedging program has reduced the volatility of prices?
A. Yes.
Q. And that's a benefit to both the Company and the customers, right?
A. It's, it has reduced the volatility of the prices, yes.
Q. Okay. What information could the Company present that would show that its hedging program provides the best protection for customers?
A. Well, I, I think, in looking at some of the other utilities and what they've done, they've presented multiple scenarios and multiple options that are available in the hedging programs.
We have one program. It's -- that's the way it's been done. We have not looked at any alternatives, or the use of options, or anything else, other than the way it's been done today.
Q. Okay. So you're talking about maybe a process somewhat like the IRP process, where there's a variety of hedging approaches presented and then the Company compares the results of those, or something like that?

A. I'm saying -- well, it would -- I think the Company should prepare, prepare an analysis to look at some different scenarios of what it -- what are some different hedging strategies. What would it do? How would it, how would it affect the net power costs?

Are there some, some ways that we could take advantage and get out of some of these long-term contracts if the price of natural gas drops?

Q. Okay. Now look at lines 200 to 202. You say here that -- you're talking about the goal of hedging:

> "Should the goal give priority to (on the existing extreme) to cost stability, or (on the other extreme) to cost minimization."

When you talk about cost minimization are you talking about lowest cost of net power costs? Is that what you mean by "cost minimization"?

A. Yes.

Q. You state the Division believes the Company has leaned too heavily towards cost stability, right?

A. Yes.

Q. And you say that the Division also doesn't believe that cost minimization should be the goal of the hedging program either, right?

A. Say that again.

Q. Do you also agree that the -- that cost minimization should not be the, the sole goal of the hedging program; is that right?

A. Yes, that's true.

Q. You believe there should be a balance?

A. Yes.

Q. Okay. Does this mean that the Division advocates that hedging should be used, in part, to try to beat the market?

A. No.

Q. Then what do you mean by "cost minimization"?

A. We're looking at two extremes. One is, if you do no hedging at all, you subject the ratepayers to extreme volatility.

That's not what the Division is recommending. We're not recommending the Company go out and try and beat the market. We're trying to determine what's the best solution to minimize exposure to ratepayers, and to benefit the Company.

This -- what we're recommending is -- would be of benefit to the Company as well. The reason we're here today is because there's concerns about the hedging program. Nobody understands that. The Commission has never approved that program, and so we have questions today on what the Company's done.

If we had an approved program, the Company could move forward and not have to worry about these issues.

Q. Are you aware of any hedging program the Company could adopt that would guarantee cost minimization?

A. No.

Q. And that -- is that because we can't predict the future?

A. You can't predict the future.

Q. Okay. You mentioned earlier, in your summary I think, that there's indications that the price of gas -- well, the price -- the prices are low and will remain low for quite a long time; is that right?

A. Based on the projection we've seen, yes.

Q. Okay. So do you think the Company ought to accept that as a premise in its hedging program, that prices aren't gonna change much for several years?

A. No. I think there's, there's always risk that -- we don't know what the future holds.

Q. So you're not suggest the Company should hedge when prices are rising, but not hedge when they're falling?

A. No. We don't know when that is.

Q. Okay. So I guess I still have a concern, though, about what you believe the object -- objective of a hedging program is. Isn't the objective of hedging to reduce the risk that power -- net power costs will be significantly higher than was anticipated?

A. The -- let me qualify that -- state that again. Let me, let me see if I understand what your question is.

Q. Isn't the, isn't the objective of hedging to reduce the risk that net power costs will be significantly higher than was anticipated when rates were set?

A. The, the purpose of the hedging program as, as the Company has set it up is to minimize any increase in price, yes. As far as the Company's concerned.

Where I'm concerned is there's no provision to benefit ratepayers if the price of natural gas goes down. We're locked into a price today.

Q. Okay. But isn't the purpose of hedging only to assure that the price doesn't rise too much? Or that the, that the ratepayers and the Company are protected if the price rises? It doesn't even address what happens if the price goes down.

A. That's your definition of hedging. I think you need to, to determine what the risk is to both the Company and the ratepayers.

Q. Okay. Now, in the gas hedging docket there was a technical conference held on June 3, 2009, right?

A. Yes.

Q. And the Commission arranged -- or maybe the Division, I don't know -- arranged for Ken Costello of NRRI to make a presentation?

A. Yes.

Q. Do you recall that? Who did arrange that, do you know?

A. I don't know.

Q. Okay. And Mr. Costello provided an article to the participants prior to that conference, right?

A. I believe so.

Q. And I think -- I'm not sure. I think you refer in your testimony to studies by Mike Gettings, and Pace --

A. Yes.

Q. -- and so forth, right?

A. Yes.

Q. Is this article one of the things you were referring to?

A. Yes, it is.

Q. Okay. Could you turn to page 4 of the article and read the sentence I've got highlighted, please?

MR. PROCTOR: Excuse me, Mr. Chairman, but I don't believe there's a foundation for, in effect, placing this matter into -- this particular study -- and I only have one page of it -- into evidence.

And secondly, I think there may be a problem if, in fact, this witness -- or the people who authored this document were retained by the Commission, or on behalf of the Commission, or at their direction at a technical conference, and then to enter it into evidence with respect to this witness's testimony as cross examination I think may cross the line between a technical conference and the gathering of evidence.

So if, for example, the Commission sponsored this particular presentation, now we're using Commission-sponsored information as evidence. I don't know if it's incorrect or not, but I think it should be pointed out to the Commission and they should decide that.

MS. SCHMID: And I would like to point out to the Commission that I echo Mr. Proctor's concerns about the cover sheet and one page only of the article being presented to the witness.

CHAIRMAN BOYER: Mr. Monson?

MR. MONSON: I'd be happy to provide a full copy. I did provide a full copy to Mr. Wheelwright. And I just didn't want to copy that many pages for everybody. But I --

MR. PROCTOR: That's -- I'll accept that.

MR. MONSON: -- I'm happy to do that. And I've got a full copy here, and if anybody else wants to see it I'm happy to let them see it.

CHAIRMAN BOYER: I was just gonna say we could take administrative notice of it. Because I did read this, and I did attend that conference, and I do recognize this particular statement.

MR. MONSON: Okay. And in response --

CHAIRMAN BOYER: But you haven't offered it into evidence at this point.

MR. MONSON: No, I haven't.

CHAIRMAN BOYER: You're just asking him questions --

MR. MONSON: But in response to the other part of the objection, I mean, it's -- first of all, he cited this article in his testimony so he apparently regards it as a reliable source. He's purporting to be an expert witness on the subject of this article. It's totally fair to ask him if he agrees with a statement in this article.

CHAIRMAN BOYER: Well, I think I agree with Mr. Monson.

Q. (By Mr. Monson) So I just wanted you to read that statement and I was gonna ask you if you agree with it.

A. It says:

"So why hedge? The answer is to mitigate the disproportionate pain associated with dramatic price increases, not to 'beat the market.'"

Q. So do you agree with that statement?

A. I agree that -- yes.

Q. Okay.

A. We're not trying to beat the market with hedging.

Q. Okay. And then could you also turn to page 3? Which I haven't passed out, I'm sorry. I didn't anticipate this, but. I'll be happy to get a copy for anybody.

But you have it, right, page 3?

A. Yes.

Q. Could you read the first sentence under the heading: "Why hedge at all?" I mean not the first sentence, the first paragraph.

A. "When the question 'Why hedge at all?' arises, one will often hear discussions of whether or not one can 'beat the market.' Those discussions miss the point, so they will not be debated here. Let us accept that anyone who has confidence in beating the market would not be writing papers about it."

Q. Okay. So I think we already established that you don't think the Company ought to be trying to beat the market --

A. No.

Q. -- with its hedging program? Okay. And then the article goes on to discuss the fact that prices are typically skewed upward, right? Right --

A. Yes.

Q. -- after the thing you read. So based on these statements, at least according to these authors and according to the Company, isn't the purpose of hedging to mitigate the risk of increases in prices above what was anticipated?

A. It is, but I think you need to go to the rest of the article because it has a specific section on contingencies. And while you may plan for an increase in the price of natural gas, you need to plan for a contingent that if the price goes down you need to have a plan in place to how you will handle that. That's what I don't believe the Company has in place now.

Q. Okay.

A. So if you look at rest of the article it includes that.

Q. Let's see. And one of the costs of hedging -- of having a hedging program is that if prices do turn out lower than was anticipated then customers will pay more than they would have paid if they just bought on the spot market, right?

A. Say that again.

Q. If -- one of the costs of having a hedging program to mitigate risk of increased prices is that if prices do go down customers will actually be paying more than they would have paid if the Company had just relied on the spot market or the short-term market, right?

A. If they go down and they're hedged they will pay more; is that what you said?

Q. Yes.

A. That is correct.

Q. Okay. So --

MR. MONSON: I'd offer this article. And I'm -- and like I said, I'll be happy to provide a full copy to anybody who wants it. This is Cross Exhibit 1. I guess RMP Cross Exhibit 1.

CHAIRMAN BOYER: Let's see if Mr. Proctor maintains his objection.

MR. PROCTOR: Well, yes. And for different reasons. You want to introduce the whole thing? Fine. Certainly this witness testified there's a lot more in this article than that one page.

It would be misleading and inappropriate to introduce it unless the whole thing is available. Not only to the Commission, but to everybody else. Not later, now. That would be my objection.

MR. MONSON: Can we use a copy machine? I've got the whole thing here.

CHAIRMAN BOYER: Let's -- do any of the other parties have any objection to the admission of the entire Pace article?

No one seems to. Why don't we --

MR. MONSON: Can we do it during a break?

MR. PROCTOR: Mr. Chairman, we don't -- we --

CHAIRMAN BOYER: I mean, I don't know that you really need it. I mean, you've got your expert witness here, who's already said he agrees with the statement and so on and so forth.

MR. MONSON: I agree.

CHAIRMAN BOYER: Nonetheless, the article is interesting and it does have, you know, additional commentary on other aspects of ECAMs.

MR. PROCTOR: I'm sure Mr. Monson will provide you with a full copy at the appropriate time. I have no question about that. If he enters the whole thing, then my objection is taken care of. It's just that maybe we ought to better plan things.

MR. MONSON: I'm just trying to be green. That's the only reason. Well, and it's heavier to carry 15 copies of the whole thing.

MR. PROCTOR: Well, and I, I agree, but.

CHAIRMAN BOYER: So is the motion then to admit the entire article into the record?

MR. MONSON: We'll do that, yes.

CHAIRMAN BOYER: There's no objection to that, so it will be admitted.

(Exhibit No. RMP Cross-1 was admitted.)

CHAIRMAN BOYER: And you can substitute -- or give us a copy of the --

MR. MONSON: I'll do that.

CHAIRMAN BOYER: Give us -- let's make copies for those who want it.

MR. MONSON: Okay.
CHAIRMAN BOYER: And those who would rather save the trees.
MR. MONSON: Okay.
CHAIRMAN BOYER: You know. Thank you.
Q. (By Mr. Monson) Just to conclude this, any attempt to beat the market would really be speculation, wouldn't it?
A. Yes.
Q. And there are people who do that, right? There's people who are speculators. In fact, some of the counterparties the Company deals with are probably speculating about what the market is gonna do; is that right?
A. I would agree with that.
Q. Others may have more gas than they need or more electricity than they need so they may just be doing a transaction. But -- there's speculators out there but you aren't suggesting the Company ought to be a speculator?
A. Absolutely not.
Q. Okay. And you wouldn't support recovering rates of costs associated with trying to beat the market?
A. No.

Q. Okay. All right. Can you turn to your direct, lines 353 to 356?

A. Okay.

Q. Here you're talking about the 10-K report. And I think this is what you were referring to earlier; is that right?

A. Yes.

Q. Okay. And it says that the Company reported it economically hedged 95 percent of its financial exposure and 53 percent of its forecasted physical exposure for 2010. And 87 percent of the financial and 26 percent of its physical exposure for 2011?

A. Yes.

Q. Okay. And this was in the December 31, 2009, 10-K report. So 2010 was the next year. And 2011 was two years out, right?

A. Right.

Q. So would those numbers be -- would you amend your earlier statement --

A. Yes.

Q. -- consistent with those numbers?

A. Yes.

Q. Okay.

A. Yes. Two years out we're about 87 percent hedged.

Q. Financially?
A. Financially.
Q. Right. Okay. And then on line 365 you note that the level of hedging is different between physical and hedges. And I think you're referring to that statement, right?
A. Yes.
Q. So you recognize that the Company's hedging program includes both physical and financial hedges?
A. Yes.
Q. Now in your direct on lines 659 to 660, and this is your Chart 8. You have a table or a chart which shows, shows the cost/benefit by year of PacifiCorp's hedging program, right?
A. Yes.
Q. From 2004 to 2009?
A. (Moves head up and down.)
Q. Okay. And this includes both physical and financial hedges, true?
A. This chart was based on the technical conference that the company held. This is, this is the information that was provided in that information in that, in that conference.
Q. Okay. So do you not know whether it includes physical and financial?

A. I do not know.
Q. Okay. Well, let me represent to you that it includes all hedging. All the Company's hedging. So it includes both physical and financial. Do you -- and would you accept that subject to check?
A. Subject to check, yes.
Q. Okay. During this period the chart shows a substantial cumulative net benefit from the hedging program, right?
A. That's what it shows, yes.
Q. And in fact if you add up the numbers -- which I haven't done, but we can do it quickly -- you've got two years where it's negative, right? The first two years. It's about -- so you're say 40 million in the hole.
A. (Moves head up and down.)
Q. And then you're 88 ahead, so you're 48 ahead. Then, then 5 million, so 53. Eleven million, 64 roughly. And then 129 million ahead, so 193 million to the good, right? Roughly?
A. I believe it is.
Q. And you have, you've done an analysis, but you cut off 20004 and 2005, right?
A. The analysis that I did was based on information we received from data requests that --

where we asked the company to provide the specific information on the settled contracts for the previous years.

Based on the information that was provided, that's why we -- how I put together this table.

Q. Okay. And, and it goes from 2006 through May of 2010?

A. Yeah. They didn't provide anything prior to 2006.

Q. Okay. Did you ask for it? Didn't you ask for it from 2006 on?

A. I think we did, yes.

Q. Okay. And that information -- now, first of all, the information that's on Chart 8 was provided in response to another data request, 14.1 -- well, let's look. Four point fourteen, right?

A. I believe so.

Q. Okay. So you had this information. And then you asked the follow-up question you just wanted information about the swaps, right?

A. We asked -- and I have the information, the wording that's what we asked in the data request. It says:

"In response to DPU Request 4.14(d)(2) include a detailed

spreadsheet of electric hedging
contracts from July 2006 through
August 2009. Please provide the same
monthly information from September
through December 2009, and the monthly
information for 2010."

We asked for all the specific information on hedging contracts. Which I assume would have included both the physical and the, and the swaps.

Q. But it was a follow up to another question apparently, you said?

A. Well, it was -- the information from 4.12 only went -- included a portion of 2009. What I was asking for was the remainder of 2009, September through the end of the year, and then the year-to-date 2010 information.

Q. Okay. But in any event, your, your table and your testimony -- your exhibit cuts off 2004 and 2005, right?

A. Yes.

Q. So if you just look at Chart 8 and you cut off 2004 and 2005 you're essentially adding 40 million to the benefit, right? That would be shown on that chart?

A. Yes.

Q. Okay. And --
A. Well, let me look at that again. What -- say that again.
Q. If you cut off 20004 and 2005, which were the two negative years --
A. Right.
Q. -- that's about $40 million. I mean roughly, round dollars.
A. Forty million dollar loss.
Q. Loss. So if you take that away you can actually increase that amount -- 190 million or something -- by 40 million, right?
A. Right.
Q. Because that was included in the total. Okay. So do you understand that the difference between this chart and the chart in your testimony is the chart in your testimony is just gas swaps and electric swaps and is not all hedging instruments?
A. I didn't know that until today.
Q. Okay.
A. I don't -- and I'm still not a hundred percent convinced that's the case.
Q. Well. But given what we've just talked about Chart 8, wouldn't you expect that the net benefit would increase that's shown on Chart 8 if you had

comparable data in your, in your exhibit, rather than decrease and go negative?

A. Say that again.

Q. Wouldn't you expect, based upon what we've just discussed about Chart 8, cutting off the first two years that are negative, wouldn't you expect if you, if you do an analysis from 2006 through May of 2010 that the benefit would increase?

A. If I'm looking at Chart 8 only, yes, that's true.

Q. Okay.

A. If I cut off two years.

Q. Now, do you know whether or not there was a net cost from all hedging in the first five months of 2010?

A. It -- according to my chart? It looks like it's a positive.

Q. Okay. So even just looking at swaps it's positive --

A. Yes.

Q. -- right? Okay. So then by adding those additional five months you'd even expect the benefit to increase further, wouldn't you?

A. I don't know. If it doesn't include everything, I don't know what it would show.

Q. Okay. But you agree that your, your Exhibit 2.1 only includes financial swaps?

A. I don't know what it includes, because we asked for all the specific settled contracts and this is what we received from the Company.

Q. Okay. If you only look at swaps do you understand that you're leaving out a lot of wholesale electric transactions in which the Company had -- was in the money during this period?

A. Yes. And I've gone back -- I went back during the lunch period and looked at the electric. I believe all of the electric information is included. The only question that I have is whether or not the natural gas physicals are included. But I believe all the electric is in there.

Q. Okay. If we -- the numbers, the numbers from 2006 to 2009 are on Chart 8, right?

A. The information --

Q. About --

A. Yes.

Q. -- the net benefit or cost of hedging. So the only thing we're missing is the first five months of 2010; is that right?

A. Yes.

Q. Okay. I've prepared an exhibit that includes that information as well. And I'd like to show that to you.

A. Okay.

(Pause.)

Q. (By Mr. Monson) Now, if you'll compare the numbers for 2006, 2007, 2008, and 2009 I believe you'll see that they're the same numbers that are on Chart 8; is that right?

A. Yes.

Q. Okay. So I'm gonna represent to you that the numbers for January through May of 2010 are derived from the same source and they're the same numbers. Are you willing to accept that, subject to check?

A. Sure.

Q. Now, I don't know how they compare with your numbers for 2010. Looks like they're similar. Let's see, the gas hedges are the same, right? But the electric hedges are different, right?

A. Yes.

Q. Okay. So apparently there's something in electric hedging that isn't reflected on your Exhibit 2.1.

Would you accept, subject to check, that this shows that during the same period as covered by your Exhibit 2.1 there's actually been a positive benefit to ratepayers from hedging during this period of $303 million?

A. Yes, but I would want to look at this in more detail. And the other thing I think it points out is the dramatic swings that can occur within the hedging program. That we can have dramatic swings in the net power costs.

Q. Right. And in fact you made a point in your testimony that, that in a down market, when the prices are falling, that maybe hedging isn't such a good idea or it's not as valuable, right? It may be a bad thing to be doing?

In other words -- I, I don't want to put words in your mouth. But was it your view that the Company isn't taking advantage of a down market in its hedging program?

A. If you're hedged to a very large percent, and the price -- and you're locked into a price that's above the current market price, and you don't need to buy any more quantity, you can't take advantage of a drop in price.

Q. Okay. What does this exhibit show about that? When did the market turn down?

A. About 2008.

Q. Okay. Since 2008, if we look at these numbers, we see that there was a big negative on natural gas in 2009. But there was even bigger upsides on electric hedges in 2009 and 2010; is that right?

A. On the power side, yes.

Q. So would this indicate to you that in this down market the Company's hedging program has actually been beneficial to ratepayers?

A. I think the -- say the question again just a moment.

Q. Would this indicate to you that, that in this market where the prices have fallen, that the hedging program has actually been beneficial to customers more than it was before?

A. The -- again, I think if you want to narrow the position down very tightly, you could say yes. But I want to point out the dramatic swings that are available in those, in those commodities.

That the natural gas -- and if you look at the -- your information, we went down $221 million over the, over the, you know, the price that was, that was available. What they, they purchased that gas for.

Q. Right.

A. So I guess the question is, had the program been separated and things been done a little bit differently, could they have taken advantage and reduced that loss -- reduced the loss of $220 million?

Q. Do you have any idea how they could have done that?

A. I think by changing the, the hedging program.

Q. How?

A. Looking at some contingent options. Looking at some other strategies to get out of these long-term deals so they're not locked in.

Q. Okay.

MR. MONSON: We'd like to offer this exhibit as Cross Exhibit 2. RMP Cross Exhibit 2.

MS. SCHMID: And I'll object to the extent that there's a lack of foundation, with particularity as to the 2010 numbers.

THE WITNESS: Can, can I ask a question on this?

CHAIRMAN BOYER: Go ahead and ask the question, Mr. Wheelwright.

THE WITNESS: They continue to exclude their Hermiston contract in the analysis, and a lot of the in -- a lot of the information. And if that's a portion of the hedging costs, it ought to be included.

Q. (By Mr. Monson) Do you know whether or not

the Hermiston contract's in the money?
A. I don't.
Q. Would you accept, subject to check, that even with the decline in prices it's still in the money?
A. I have no idea.
Q. Okay. You don't know whether it's -- how you could check that?
A. But I don't know why they continue to exclude their Hermiston transactions.
Q. Well, how long is the Hermiston contract; do you know that?
A. It ends in 2011, I believe.
Q. But do you know how long its --
A. I don't know.
Q. What its duration's been? Okay.
CHAIRMAN BOYER: Any other objections to Cross Exhibit -- RMP Cross Exhibit 2?
I mean, we do have a foundational issue. I mean, Mr. Monson has represented that he prepared it. He's not a witness.
MR. MONSON: And actually, I didn't prepare it. I couldn't prepare this.
CHAIRMAN BOYER: You caused it to be prepared?
MR. MONSON: It was prepared by Company --

the same people who provided the other data and responded to the data requests and the whole deal.

MR. PROCTOR: Well -- and Mr. Chairman, I have an objection as well. From the content of the examination and the answers, this is obviously reflecting financial hedging. Which the evidence is that isn't energy and it isn't fuel. And yet their bottom row is listed as "Net energy."

I believe that's misleading. So to that extent -- and since there's been no testimony certainly from this witness or about this exhibit that defines net energy in relationship to their hedging practice, I don't think that this exhibit should be admitted.

Now, if they want to go back and properly describe it, then yes, perhaps it's appropriate. But not, not this format. And the person who prepared it needs to be here to establish exactly what that means.

MR. MONSON: We'd be happy to call a witness if you want to take the time. The reason we didn't put this on in Mr. Duvall's summary was because we expected objections because it was new evidence.

But it happens to be responsive to testimony that was filed last week. Surrebuttal testimony. And we're happy to put a witness on if you want to take the time to do that.

MR. PROCTOR: Well --

MS. SCHMID: I think that it contains significant foundational errors. And I urge the Commission either to not accept it into evidence, or award it the proper weight of such an exhibit with its noticeable foundational errors, which would be nil or little.

CHAIRMAN BOYER: I'm inclined to deny admission. But in fairness to Mr. Monson, I think you could probably get this same type of testimony just by asking Mr. Wheelwright an appropriate question.

For example, does he have personal -- you could find out if he has personal knowledge of what the net benefits or detriments were for the five months in 2010. See if he knows that. And then if he knows that, find out how much he knows it.

And then you've got your evidence in if he can. If he doesn't, then he probably ought not to be testifying about it.

MR. MONSON: Okay.

Q. (By Mr. Monson) I -- well, first of all Mr. Wheelwright, every number on this chart except for 2010 is on your Chart 8 in your testimony, right?

A. Yes.

Q. And I already -- I think I did ask you about if you knew about the first five months of 2010. And you said that your numbers show there was a positive benefit, right?

A. Yes.

Q. And your 40 -- even the 44 million number is on your, is on your Exhibit 2.1. So the only number we don't have verified is the 113,863,078; is that right?

A. Yes.

Q. And your, your exhibit shows -- instead of 113,863,078 your exhibit shows 74,155,016; is that right?

A. Yes.

Q. And I've explained --

A. On electric?

Q. Oh, sorry. Yeah, on electric, right.

A. Yes.

Q. And, and I've explained to you that the difference is that this includes physical hedges, where yours doesn't. Do you understand that?

A. Yes.

Q. Do you have any reason to doubt that that's an accurate representation?

A. If you exclude Hermiston, I, I assume that

that's correct. But I, I don't know. I don't have any information to verify if this is correct or not.

Q. Well, haven't you been given this information in response to the discovery requests?

A. I --

MS. SCHMID: Objection, argumentative.

THE WITNESS: The, the last information I have not been given, no. The subject you're asking about now, information in 2010, I do not have information -- that information.

Q. (By Mr. Monson) Okay. So on, so on exhibit -- I mean in data request 414 you were just given information through the end of 2009?

A. Four fourteen goes through, I believe it's September of 2009.

Q. Okay.

A. Eight point one four continues through the rest of 2009 and the first few months of 2010.

MR. MONSON: I'd still offer it, your Honor.

CHAIRMAN BOYER: Okay. We'll, we're not going to admit it. But I think you've made your record clear.

MR. MONSON: Okay. That's all I have.

CHAIRMAN BOYER: Okay. Thank you Mr. Monson.

Let's see. Mr. Proctor, any cross

examination of Mr. Wheelwright?

MR. PROCTOR: Yes.

CROSS EXAMINATION

BY MR. PROCTOR:

Q. Mr. Wheelwright, what is your understanding of the purpose of this particular part to Phase II in the ECAM docket?

A. It's my understanding that the, the purpose of this phase is to look at the hedging and front office transactions in relation to including those in an ECAM.

Q. In other words, would it be fair for me to describe it as to consider the dependent relationship between an ECAM and hedging?

A. Yeah, I would, I would say that, yes.

Q. Now, is it the Division's position that the financial hedging, the fixed, flowing hedging -- financial hedging transactions and the costs should be included in the ECAM that is to be designed in the subsequent proceeding?

A. I think the design phase has been identified by Mr. Peterson in his testimony in -- but he has not recommended excluding the hedging from the ECAM.

Q. So does that mean that the Division's position is that it could be or should be included?

A. I think it could be included. It has not been, been articulated in the -- and that's part of Mr. Peterson's design phase.

Q. Now, you were kind enough to provide me with a written copy of your comments -- summary comments given this morning. And I have some questions in particular about your choice of language and your -- in your summary.

The first thing that you stated -- or one of the first things was that the Division and other parties have been concerned for some time about the amount and the duration of the Company's hedging program; is that correct?

A. Yes.

Q. And there has been a lack of understanding concerning the amount and duration of the current hedging program, correct?

A. Yes.

Q. Including the extent of price fluctuation in existing contracts?

A. Yes.

Q. Are you discussing there the financial hedging?

A. Yes.

Q. Not physical hedging?

A. More the financials, yes.

Q. Well, do you have a similar concern -- does the Division have a similar concern with respect to physical hedging?

A. I don't believe to the same extent, because they're not going out as far into the future with the physicals as they are with the financials.

Q. So what you're talking about, then, is including in a ECAM is what you have described in your summary as a hedging strategy that has been conducted without scrutiny or approval of regulators; is that correct?

A. Yes.

Q. And that it has not been determined to be in the best interest of the Company. You said that?

A. Uh-huh.

Q. Nor in the best interest of ratepayers. You said that?

A. Yes.

Q. And that's the one that could be included in an ECAM?

A. Yes.

Q. You criticized the Company's program because there should be an understanding of the priorities for price stability versus cost minimization from the perspective of both the Company and the ratepayers.

And this leads to some of the questions Mr. Monson was asking you, and in particular about this article that was presented in a technical conference. Were you present during Mr. Duvall's testimony?

A. Today?

Q. Yes.

A. Yes.

Q. And did you hear Mr. Duvall describe that the purpose of the Company's hedging -- financial hedging was not cost minimization?

A. Yes, I did.

Q. That they're looking at it purely from the standpoint of managing the risk of volatile pricing, correct?

A. That's correct.

Q. Were you also present when Commissioner Campbell asked the question of how the Company's financial transaction hedging program benefits ratepayers?

A. Yes, I was here then.

Q. Can you answer that question, how does it benefit ratepayers?

A. I think the, the hedging program minimizes the volatility of natural gas prices if they were to -- as compared to if they were to purchase on the spot market. So I believe it does benefit in that way.

Q. Does that benefit ratepayers?

A. Yes.

Q. Okay. Looking at Chart 8, which is on page 28 of your direct testimony. I think June 16th testimony?

A. Yes.

Q. I want you to look at 2009.

A. Okay.

Q. Let's look at the -- and mine is just pure yellow, so if there were color differentiations you'll have to help me out with those. The number, a positive 351,056,101, what does that represent?

A. Power hedges.

Q. In other words, they were able to -- what? Buy power at a price that was?

A. They were able to -- the current market value of those hedges is $351 million higher.

Q. And cons -- and accordingly, or comparatively, the $221,785,835 was the amount they paid for natural gas in excess of the market, correct?

A. That's correct.

Q. What is the Company's system-wide net power cost, let's say dealt with -- or for which they were allowed recovery in the last general rate case?

A. I don't have that. I'm not -- I don't know.

Q. Would you say about a billion point two?

A. That sounds about right.

Q. Well, just roughly, what percentage of a billion 2 is 351 million 56 dollars and?

A. About 3 percent, I believe.

Q. Three hundred fifty-one million --

A. Or --

Q. It's more like 30 percent?

A. Thirty percent. True, yeah.

Q. And roughly the excess cost they paid in 2009 for natural gas is roughly 20 percent of their total net power cost, as found in rates from the last general rate case, correct?

A. Yes.

Q. I want you to turn to Table 1 on page 13 of your June 16th testimony.

A. Say that again. Where am I?

Q. Page 13 --

A. Page 13.

Q. -- Table 1. This was the table reflecting the percentage for which the Company had hedged both physical and financial in 2007 through 2011, according to their SEC filings; is that correct?

A. Yes, it is.

Q. I want you to look at 12/31/08, financial hedging for 2009.

A. Okay.

Q. Okay? They list it as 94,000 -- or excuse me, 94 percent, correct?

A. Um.

Q. Am I reading that improperly?

A. Are you looking at the year end 2008?

Q. July 31, 2008, says Financial. Come over underneath the column --

A. Yes, 94 percent.

Q. Ninety-four percent. And what does that represent?

A. Ninety-four percent of their -- the quantity that they would need for natural gas that's been hedged with financial products.

Q. And they were going to hedge, in 2010, 85 percent?

A. They had already hedged 85 percent of their 2010 need.

Q. Now go down to 12/31/2009, Financial. And go over to 2010. Now you have a 95 percent hedge?

A. Yes.

Q. Why did it go -- change from 85 percent to 95 percent for 2010? Why? Do you know?

A. Well, they're, they're hedging even more in the, in the current year.

Q. Why did they hedge more?

MS. SCHMID: Objection, I think that this question would be more properly asked of the Company witness, since the information was based on the Company's 10-K.

MR. PROCTOR: That is not an objection. My question is why. And if he doesn't know, he can say that.

CHAIRMAN BOYER: Why don't you ask him if he knows, first.

THE WITNESS: I don't know, I would -- I don't know.

Q. (By Mr. Proctor) Did you ever ask the Company?

A. No. The, the purpose of the hedging program is to hedge amounts during the -- well, I'll leave it at that.

Q. Did you ever review their SEC report, the 10-K, to determine if there was any explanation for that difference?

A. I reviewed the 10-K, yes.
Q. Did it explain, at all, the difference between their end-of-year 2008, and their end-of-year 2009 hedging policy for 2010?
A. No.
Q. Have you reviewed the Company's description of its hedging policy?
A. Yes, I have.
Q. And within that hedging policy does it provide any guidelines for analysis or evaluation that would explain their changing the hedging from 85 percent to 95 percent over a period of one year?
A. It doesn't specifically identify that, no.
Q. Okay. And would that be consistent with your, your conclusions that in fact their hedging program is really not well understood or understood at all by the regulators?
A. I would agree with that. That's the reason why we're here today.
Q. And that's the type of hedging program that the Division believes could be included in an ECAM?
A. That's the current program that's in place today, yes.
Q. Yeah. So the Division's policy is, Yeah sure, cool, go ahead and put it in an ECAM?

A. There's some provision --

MS. SCHMID: Objection, argumentative.

MR. PROCTOR: It was.

Q. (By Mr. Proctor) Is the Division's position that that particular misunderstood, poorly understood, or not-understood-at-all hedging program could be included in an ECAM?

A. I believe the information on what's going to be included in the ECAM would be better addressed by Mr. Peterson.

Q. Well, but unfortunately you're the one sitting in that stand today.

A. That's true.

Q. Is that the Division's position?

MS. SCHMID: Objection, beyond the scope of this witness. What will be in the ECAM is delineated as Phase II Part 2 of this docket, I believe.

CHAIRMAN BOYER: Well, you know, I'm a little confused on the question as well. Are you -- the Division -- I think Mr. Wheelwright has testified that -- several times, in fact -- that hedging could be included in an ECAM. But they have concerns about the current hedging practices of the Company.

So you -- are you --

MR. PROCTOR: His answer -- yes, that's the one that could be included would be -- that's his answer. If he -- if that is his answer, he should say that.

CHAIRMAN BOYER: Is that your answer, Mr. Wheelwright?

THE WITNESS: The -- we can't change the program as it stands today. That's the Company's program. So I -- if it's included in the ECAM -- if in the next phase it's determined that, that hedging would be included then it would be included, yes.

Q. (By Mr. Proctor) And, and the reason that it can't be changed is because that's the program that has been used, without scrutiny or approval of regulators, since its inception, correct?

A. Yes.

MR. PROCTOR: No more questions.

CHAIRMAN BOYER: Okay. Thank you Mr. Proctor.

Ms. Hayes, questions for Mr. Wheelwright?

MS. HAYES: No questions?

CHAIRMAN BOYER: Mr. Evans?

MR. EVANS: Thank you.

CROSS EXAMINATION

BY MR. EVANS:

Q. Good afternoon Mr. Wheelwright.

A. Good afternoon.

Q. Just to follow up on something Mr. Proctor was saying. Your -- it's the Division's recommendation that the hedging program ought to undergo a review; isn't that right?

A. Yes.

Q. And in your testimony you propose -- I'm looking at page 34. It's lines 828, that question and response there. You propose a process by which the current hedging goals and strategies could be reviewed by the Commission; isn't that right?

A. Yes, it is.

Q. And my, my questions are really to help us understand what this process would be. You have suggested by the -- by March 31 of each odd-numbered year, beginning on 2011, there could be the commencement of this review?

A. Yes.

MR. MONSON: Mr. Chairman, I, I want to object to this line of questions. I know this isn't my witness. But I think Mr. Evans is violating the Commission rule that he can't try to make his case through cross examination, and I think he's also engaging in friendly cross. So I object to this line of questions.

MR. EVANS: Well, may I respond?

CHAIRMAN BOYER: Please, Mr. Evans.

MR. EVANS: It's not really friendly cross. I'm -- it's clarification. I'm not encouraging him to reiterate his testimony. I'm asking him questions to help clarify.

CHAIRMAN BOYER: Yeah, let's hear a few more questions.

You may answer, Mr. Wheelwright.

THE WITNESS: Say the question again, would you?

MR. MONSON: He actually already answered before I objected.

CHAIRMAN BOYER: I don't think Mr. Evans is finished yet.

MR. EVANS: But in fairness to Mr. Monson, he objected to the whole line of questions, so there's just a little tying up to do.

Q. (By Mr. Evans) I'm wondering, you're not seeing that inside the IRP process, though, are you?

A. No.

Q. How does this process occur? Is it a separate proceeding, a separate docket?

A. Yes, it would. A separate docket. The Company would file information on what they would propose to use for a hedging strategy. Then intervening parties could also present information concerning their recommended hedging strategies. And then it would be, be hearings before the Commission.

Q. And what would the result of this proceeding be?

A. Ideally it would be an approved program that the Commission had reviewed and approved, and the Company could go forward with that.

Q. And how would then -- say the Company approves it. And let's -- for hypothetically let's say the Company approves 85 percent natural gas supplies hedged on swaps instead of 100, okay?

A. Okay.

Q. That, that's the program they decide (Counsel is speaking too softly.)

THE REPORTER: I'm sorry, Counsel, that's the program they decide?

MR. EVANS: Is prudent and that the Company should go forward with.

THE REPORTER: Thank you.

Q. (By Mr. Evans) How does that get into rates and ECAM after this proceeding's over and the decision's been made. Then what?

A. Well, I think it's just -- it's the same as, as the program today. The Company would know how to proceed and how to, to build their, their IRP, and what, what costs would be associated with that.

Q. Okay. But the cost of the 85-percent swap on natural gas wouldn't really be implemented in rates until the next rate case, would it?

A. That's correct.

Q. And it wouldn't be implemented in ECAM until the ECAM proceeding following the rate case, following the Commission's decision; isn't that right?

A. That's true. I wouldn't think that going forward we'd have dramatic changes in the -- in an approved plan. There might be some minor adjustments, but I don't think we'd have major fundamental changes from year to year.

Q. But, but any changes at all wouldn't be implemented in ECAM until after they've been determined by the Commission to be prudent, and then after there's been a rate case, and then after there's been another ECAM proceeding?

A. I believe that's correct.

Q. So we're not looking at an immediate change in anything as a result of a change in the approval of the hedging process?

A. No.

Q. Okay.

MR. EVANS: I think that's all I have for Mr. Wheelwright, thank you.

CHAIRMAN BOYER: Thank you Mr. Evans.

Commissioner Allen?

COMMISSIONER ALLEN: Thank you. I believe in your testimony, Mr. Wheelwright, that you had referred to the -- a number of data requests. And it started leading me to believe that a hedging program or hedging program guidelines could be achieved in the next couple of years. Did I understand that correctly?

THE WITNESS: Yes.

COMMISSIONER ALLEN: And in the process of doing that -- I'm just curious. I don't want to answer the question today about what it might look like. But were you able to discover how many other states' commissions are actively pursuing program guidelines or programs? Did you get any feedback as to whether or not we're breaking new ground here, or?

THE WITNESS: No, we're not breaking new ground. Based on the information that I've looked at, most of the other utilities file a fuel cost docket with their Commission in advance. And they review that periodically.

I don't think we're breaking any, you know, blazing any new ground here. I don't think -- mostly the commissions do have some kind of a program where they will review the fuel cost of the utility.

COMMISSIONER ALLEN: Okay. Thank you.

CHAIRMAN BOYER: Commissioner Campbell?

COMMISSIONER CAMPBELL: I'd like to just spend a few minutes on the stability question. And in response to Mr. Proctor you said that ratepayers benefit from stability through the natural gas hedging. Was that your answer? Is that -- is my recollection right?

THE WITNESS: Yes. It is more stable than buying on the spot market.

COMMISSIONER CAMPBELL: So if you go to Chart 8 on page 28 of your, I believe it's your direct testimony. And we'll do the little, the little math exercise, I guess, that Mr. Monson put you through, but I'm gonna go through that just on the natural gas hedges.

THE WITNESS: Okay.

COMMISSIONER CAMPBELL: So if we look at the first year, you're 32 million plus. Second year you're 55 million plus. Third year you're 45 million plus. And then we go 102 negative, 78 million negative, and 221 negative. And I haven't added all those up in my mind. I guess I can do it quickly. Say roughly 100, 130.

And you're -- so, so I think I can honestly say you're over 200 million to the negative in natural gas to the ratepayers based on their natural gas hedging. How -- was it worth it? I mean, what was the benefit ratepayers got by paying over $200 million more than market for natural gas.

A. I think that's the reason we're here, because we don't have information on the benefit to the ratepayers. The Company has not been able to provide that. The -- this -- the financial hedges are fairly new, relatively, compared -- you know, we restyled the financial hedges beginning 2006, escalating in 2007.

So we really don't have a benefit and -- when we look at the cost of the natural gas hedging.

COMMISSIONER CAMPBELL: So we, we understand what the cost of natural gas hedging is and we understand what the cost of the financial hedging is, because you did that on your SR-2.1.

And I'm -- so in a sense we know we're, we're to the negative on those two areas. And the Division doesn't have an idea of what the benefit is for those costs.

THE WITNESS: The benefit I think would be more stability to -- instead of purchasing on the spot market. More stability in rates for the ratepayers.

COMMISSIONER CAMPBELL: Well, let's talk, let's talk about that. I understand stability for the Company. But once rates are set in a rate case rates are stable for the ratepayers, no matter what happens in the market.

THE WITNESS: That's true.

COMMISSIONER CAMPBELL: So where do they gain the stability? And, and the only other option then is in a rate case. And you're just doing a point estimate.

You're not, you're not compare -- you're doing a point estimate on the costs of those products of natural gas. So I'm still struggling to figure out, under the current hedging program, where the stability for ratepayers lies.

THE WITNESS: I think what -- the way that the Company has structured this, they want to fix their costs essentially two years in advance. And that's the reason why they, they hedge to -- well, 85 to 90 percent two years in advance, is because that is the year that they're going to use for the test year to set rates.

So by doing that and hedging two years in advance, essentially, they can lock in the price of the natural gas to determine the rates.

COMMISSIONER CAMPBELL: And maybe the way to ask the question is if they didn't do that, what would they do? How would we set the price of natural gas in a rate case?

THE WITNESS: I believe they'd have to estimate what the cost would be, based on the forward price curve.

COMMISSIONER CAMPBELL: Okay. So you have an estimate of a forward price curve or you have a lock-in price. It's one estimate or another, is it not?

THE WITNESS: That's true.

COMMISSIONER CAMPBELL: So how does that generate stability?

THE WITNESS: I, I -- creates more stability for the Company --

COMMISSIONER CAMPBELL: Okay.

THE WITNESS: -- than I believe it does for the ratepayers.

COMMISSIONER CAMPBELL: Okay, I think I understand that. And that gets me to my bottom-line question here as it relates to this hearing and this docket.

If the current hedging program provides stability for the Company, for their earnings -- and that's not necessarily a bad thing. I mean, there could be ratepayer benefits there. It allows an opportunity to earn their return, and so forth. There may be some intangibles there that are not so direct.

But let's say it provides stability for the Company. Now we're going to an ECAM. And if we put hedging in an ECAM for customers -- now, now we're no longer hedging solely for the Company but we're hedging for customers, what changes?

And I, I -- in all the testimony I can't find, from anyone, what changes with, with the dramatic change in the incentive -- incentives as it relates to hedging.

I mean, has the Division thought about if we're hedging today for the Company, and tomorrow we're hedging for the ratepayers because it's gonna be -- I mean, the ratepayer perspective I assume is gonna be perhaps different than what the Company's perspective is as far as tolerance for risk and so forth.

The question is, is there anywhere in this docket where we talk about how that changes? Or is that something we would do in this study that you've talked about?

THE WITNESS: I think that's something that would be, that would be done in the next study and looking at how this affects the ratepayers. The -- by including this in the ECAM the Company will recover more of its costs.

They've also testified they're not going to change the hedging program if the ECAM is adopted. So we asked that in a data request, if they would be adjusting anything, and they indicated they would not.

COMMISSIONER CAMPBELL: Let me just ask a question about physical hedging. Is it your understanding that, under the physical hedging program, that part of that amount is not just purchases of power but does that also include the sales of -- sale of electric power?

THE WITNESS: Yes, it does.

COMMISSIONER CAMPBELL: So I'm gonna go back to the old days now, and -- before we actually called it "hedging." When the Company had surplus power -- they had power, they had shoulder power, whatever -- to minimize costs for ratepayers they would go to the market and sell that.

Is that what's happening in some of this physical -- what we now call "physical hedging"? Is it just the normal operation of the utility where they sell excess power on the market?

THE WITNESS: Yes. Part of that is their transactions where they'll sell power on the market, yes.

CHAIRMAN BOYER: Couple of questions. And following up on Commissioner Campbell's question right there, is the other part the fact that the Company is locking in sale prices that may, in fact, be higher than market later?

THE WITNESS: Say that again.

CHAIRMAN BOYER: Is one of the benefits of the power hedging the fact that the Company is locking in sales at --

THE WITNESS: At higher prices.

CHAIRMAN BOYER: -- prices that may be higher?

THE WITNESS: Yes.

CHAIRMAN BOYER: That's it.

THE WITNESS: Yes.

CHAIRMAN BOYER: Now getting back to these calculations. The benefit calculations, cost/benefit calculations.

THE WITNESS: Okay.

CHAIRMAN BOYER: Where natural gas hedging seems to be underwater most years -- and I'll use that, most years -- and power hedging positive side.

Is it your position that if, if the Company's hedging practices included some kind of a mechanism to take advantage of a decline in fuel prices, gas -- natural gas prices, for example, that that net benefit might even be higher than it is today?

THE WITNESS: Sure. Yes, it could be.

CHAIRMAN BOYER: That cost of hedging would be down -- say if they're only hedging 60 percent, or 70 percent, or 80 percent, something like that.

THE WITNESS: And that, that was one of the reasons why I want to -- why my recommendation is to separate the gas and the electric hedges. Because if we can reduce -- well, if -- for example, in 2009 they show a $221 million loss.

If you could reduce the amount of the loss on the gas hedging, the net benefit to the Company is greater.

CHAIRMAN BOYER: So if an ECAM were -- hypothetically, if an ECAM were approved, and if hedging were included in that ECAM, would that be a way to increase the benefit to customers, who now bear the risk of fuel costs in an ECAM?

THE WITNESS: I think it would, yes.

CHAIRMAN BOYER: Because they could take advantage of the ups and the downs?

THE WITNESS: They could take advantage of, of a drop in the price.

CHAIRMAN BOYER: Okay. Thank you Mr. Wheelwright.

Redirect, Ms. Schmid?

MS. SCHMID: Just a few.

REDIRECT EXAMINATION

BY MS. SCHMID:

Q. Mr. Monson asked you some questions about beating the market.

A. Yes.

Q. Is it true that in economic theory the long-term lowest price for a product is the market price?

A. The market price or the spot price, is that what you're saying?

Q. That the market price is the long-term lowest price for the product. So yeah, the spot price.

A. I believe, yes, that is.

Q. Okay. Is it then fair to say that if one wanted to achieve the lowest average price for a commodity then one would rely upon market purchases and not hedge; is that correct?

A. If you were looking strictly at price and you were buying -- on the spot market, yes. But you would have much more volatility.

Q. If I wanted to lower average costs I wouldn't try to beat the market, I would go with the market. Isn't that another way of saying what you just said?

A. Say that again.

Q. If -- let me rephrase the question. If you wanted to lower average costs you would go with the market rather than try and beat the market; isn't that true?

A. Yes.

Q. You have made some -- on behalf of the Division you have made some recommendations about studying the Company hedging program and having the Company provide some more information; is that correct?

A. Yes, it is.

Q. So is it the Division's goal through implementing the proposals that you make, such as studying and Commission approval, that the Division is seeking to balance the relationship between cost and stability?

A. Yes, it is.

Q. I have just a few more. Mr. Monson asked you about "the" objective of hedging. Is there more than one objective for hedging?

A. I think there can be many objectives for hedging, yes.

Q. So there's just not one?

A. No.

Q. And finally, you were asked questions about why a utility may engage in a hedging process, and you answered that. But one question that was left unasked is, why would the counterparty participate in the hedging process?

A. The counterparty believe -- the counterparty wouldn't enter into the transaction if they didn't think they could make money. They're not gonna enter into a transaction if they're -- if the intent is to lose money. So the counterparty intends to benefit from the transaction.

Q. Are you generally familiar with the Division's comments and testimony on ECAM design?

A. Somewhat.

Q. Is it your -- is your recollection that the Division's ECAM design proposes sort of a sharing band?

A. Yes.

Q. That -- and does this sharing band tie to meeting hedging targets and participating in a hedging analysis program?

A. I believe it does. It increases the, the sharing percentage as some specific targets are met. Is my understanding.

MS. SCHMID: Thank you. Those are all my redirect questions.

CHAIRMAN BOYER: Okay. Thank you, Mr. Wheelwright. You are excused.

We'll turn now to the Committee, but before we do so let me check with our reporter.

Kelly, are you doing okay?

THE REPORTER: (Answers in the affirmative.)

CHAIRMAN BOYER: Our intention would be to go till about five minutes to three. Would that be okay?

THE REPORTER: (Answers in the affirmative.)

CHAIRMAN BOYER: We do have to participate in a telephone conference at 3:00 for a few minutes.

MS. HOGLE: Excuse me, Mr. Chairman. Considering the importance of Commissioner Campbell's question that I hear him asking, and he's been asking for a little while and has not found an answer to his satisfaction, the Company would be happy to provide that answer.

And we think it would satisfy him. If, if it would be helpful Commissioner Campbell. And we would have somebody to answer that question for him.

CHAIRMAN BOYER: You're talking about the customer benefit of hedging, is that the question?

MS. HOGLE: Yes.

MR. PROCTOR: Well, since I'm already standing up should I just speak my objection at this point?

CHAIRMAN BOYER: Sure. Go ahead, Mr. Proctor. You're already up.

MR. PROCTOR: I probably need a microphone -- I'm not gonna need a microphone for this one. The whole premise of this proceeding was to deal with -- in prefiled written testimony.

And then to wait until well, there's a question asked, and conclude that the Commissioner hasn't received an answer that he wants -- I don't know how you figured that out. And then say, Oh, we'll bring somebody else in.

Who? When? Will we have an opportunity to depose them? So all those reasons, inappropriate. With all due respect. I mean, the Commission needs the information, that's why it's asking questions. But this is not the way to go about doing it.

It -- this is pretty close to violating the due process protections that exist within the Commission's hearing rules.

MS. SCHMID: I would also like to add an objection stating that I believe that it would be an improper use of the process for the Company to call a witness in such a manner as it proposed.

CHAIRMAN BOYER: Well, we share your concerns and the due process issues. We'll talk about it during the next recess and let you know. But we appreciate the offer, Ms. Hogle.

MS. HOGLE: Thank you.

CHAIRMAN BOYER: And we'll be back to you. Don't call us, we'll call you.

MS. HOGLE: Thank you.

CHAIRMAN BOYER: Okay.

MR. PROCTOR: I don't -- have you been sworn? No. Mr., Mr. Gimble needs to be sworn.

CHAIRMAN BOYER: Mr. Gimble has not been sworn in this proceeding.

(Mr. Gimble was sworn.)

CHAIRMAN BOYER: Thank you. Please be seated.

Mr. Proctor?

***

DANIEL E. GIMBLE,
called as a witness, having been duly sworn,
was examined and testified as follows:

DIRECT EXAMINATION

BY MR. PROCTOR:

Q. Mr. Gimble, you are employed by the Utah Office of Consumer Services; is that correct?

A. That's correct.

Q. What is your title there?

A. Special project manager.

Q. And in a sentence could you describe what duties you have as special project manager?

A. Yes. Primarily analyzing filings by the Utility. And working with Office staff and consultants retained by the Office to address issues contained in those filings.

Q. And in that capacity and with those duties, Mr. Gimble, did you prepare the prefiled testimony that is listed on the exhibit list for the Office and your testimony that's been distributed?

A. I did.

Q. Do you have any corrections or changes that need be made to any of those versions of the testimony?

A. I have a few.

Q. Would you start with the first one and go through them, please?

A. I have a couple changes -- corrections to make to my direct. Page -- or line 424 on page 16. "Forward" should be for -- or "forwards" should be "forward." And line 681 on page 24, "complete" should be "completed."

Couple more in the surrebuttal. Line 10, page 1, should be June 16th. Line 142 there's two periods after "study," should be one. Line 233, page 8, it says "both of these issues." "It" should replace "both of these issues."

And my final correction is on page on 14 in Footnote 9. It should say "direct testimony." I say "my testimony," I should say "my direct testimony."

Q. With those corrections, Mr. Gimble, if I were to ask you the questions that were asked in your direct or in your prefiled written testimony would your answers remain the same?

A. Yes.

MR. PROCTOR: With that, Mr. Chairman, the Office would move for admission of the testimony that is listed on Mr. Gimble's exist -- exhibit list.

CHAIRMAN BOYER: Any objection to the admission of Mr. Gimble's direct and surrebuttal testimony?

They are admitted.

(Exhibit Nos. OCS-5D Gimble, OCS-5D Gimble (errata), and OCSW-5SR Gimble were admitted.)

Q. (By Mr. Proctor) Mr. Gimble, have you a brief summary of your testimony?

A. I do.

Q. Would you provide it, please?

A. Sure. Market reliance and hedging are two threshold issues that must be resolved prior to the consideration of an ECAM, otherwise the public interest will not be served. Accordingly, the Office recommends that the Commission take the following actions:

Initiate at first take a -- initiate a thorough review of the Company's hedging practices before any natural gas fuel or hedging costs are included in an ECAM. The Office's hedging experts have submitted specific recommendations that should be included as part of this review.

Initiate -- secondly, initiate a comprehensive market analysis to determine an appropriate baseline level of market reliance. This analysis should include the supply and price risk associated with the Company's market reliance strategy.

Further, the market analysis should be presented as part of a focus proceeding before any costs associated with market purchases are allowed in any ECAM design.

Third, based on information acquired from the market analysis, consider setting limits on the volume of FOTs included in an ECAM. And establish a higher evidentiary threshold for market purchases above the limits until the Company's market reliance strategy is consistent with least-cost-least-risk outcomes in future IRPs.

In terms of our analysis presented in my test -- the Office's analysis presented in my testimony, I believe we demonstrate the following: The Company's current resource strategy includes significant reliance on market purchases, sometimes referred to as FOTs, front office transactions.

Secondly, the Company has not supported its market strategy with substantial evidence. And this comes out in my third point, is that the Company's market strategy -- or reliance strategy has not been endorsed by the Commission in recent IRP orders.

Further, if costs associated with these resource decisions were recovered in ECAM we believe it would result in an assignment of risk directly contrary to the Commission's 2007 IRP order, as Mr. Duvall discussed a bit this morning.

Fourth, prior to the inclusion of the costs associated with market purchases in any ECAM design a focus proceeding is required to determine what limits are reasonable and to avoid setting any arbitrary restrictions.

Turning to some issues we responded to in terms of the Company's rebuttal testimony. I won't spend a lot of time but just hit a couple of them. The Office assessed the Company's cost/benefit analysis of deferring the Lakeside II resources. This was the highly-confidential piece in Mr. Duvall's testimony.

We believe the issue isn't whether that single-resource decision turns out to be cost effective. We think the issue is, if the Company pursues resource, resource acquisition strategies that are inconsistent with its IRP results then the Company should bear those risks.

Secondly, the Office disputes the Company's claim that the Commission acknowledged the higher level of FOTs in all years but 2014 in comparing the 2008 IRP, per se, to the 2008 IRP update. I think your order is pretty plain on this -- or plain speaking on this.

You simply acknowledge that the Company's resource plan generally complies with the IRP guidelines. In fact, you explicitly stated that you weren't convinced that the preferred portfolio was optimal.

And you expressed concerns as to whether the level of market purchases in that portfolio were indeed in the public interest. That led you to direct the Company to conduct further market analysis in the four areas described in my direct testimony.

Third, the Office disagrees with the Company's position that the IRP is the best venue, at least at this time, for analyzing market reliance in hedging issues.

Moving forward with an ECAM pilot without first establishing appropriate baselines for market purchases and hedging would not be in the public interest because we believe it would shift certain risks and cost responsibility to the customers without adequate protections.

These issues cannot be designed around, nor can they be appropriately remedied during a pilot program. A baseline that maintains appropriate consumer protections we believe must be in place before considering an implementation of an ECAM.

We do agree with the Company that both hedging and market reliance are dynamic issues. They'll need ongoing review. It may be possible for that review to occur within the IRP process. But we think some changes to that process would also need to be put in place since a review does not currently take place.

Lastly, public interest? We continue to recommend that the ECAM not be adopted, as the Company hasn't met its evidentiary burden to show that an ECAM would be in the public interest.

The Office -- we would further submit that these threshold issues of market reliance and hedging that you're considering right now must be resolved by the Commission before any ECAM design can be in the public interest.

And that concludes my summary, and thank you.

MR. PROCTOR: Mr. Gimble's available for cross.

CHAIRMAN BOYER: Thank you.

Mr. Monson, will you be conducting the cross examination?

MR. MONSON: I will, thank you.

CROSS EXAMINATION

BY MR. MONSON:

Q. Mr. Gimble, in your testimony you expressed a concern about the Company's level of reliance on the short-term power market to meet its needs; is that right?

A. That's correct.

Q. And you state that this market reliance exposes the customers to excessive risk?

A. It could potentially expose customers to, to risk, yes.

Q. Are you aware of any time that the Office has suggested in a general rate case to the Company that its net power costs should not be approved because the Company was relying too heavily on market purchases?

A. In the area of net power costs?

Q. Right.

A. I haven't been intimately involved in that area in the last two cases. I can't speak to those cases. Going back to prior cases, I know we had some concerns with the level of short-term purchases. And I can't give you the specific case.

Our witness in the -- in those cases proposed some specific adjustments on short-term firm.

Q. Your testimony says you joined the PSC staff

in 1987 and the Office in 1990; is that right?
A. That's correct.
Q. So you're familiar with Questar Gas's gas balancing account, right?
A. Generally familiar.
Q. Do you recall in 1991 that the Office sought a refund of approximately 97 -- $77 million in connection with gas acquisition costs in a gas balancing account case for Questar Gas?
MR. PROCTOR: Objection, it's irrelevant to the issue that's particularly before the Commission in this particular case.
CHAIRMAN BOYER: Well, I, I don't remember him testifying about this in his direct testimony or surrebuttal.
MR. MONSON: No, he didn't testify about this case. But I want to find out if he remembers the Office taking the position that the Company ought to refund $77 million in a gas, in a gas balancing account case.
MR. PROCTOR: There's foundational questions -- problems as well with the question with respect to -- because we don't know the circumstances of that case, what was being asked, what was the response.

We don't have the testimony. We don't even have clear definition of what the issue was, other than Mr. Monson's summary. It's -- in any event, it's irrelevant.

MR. MONSON: I just asked him if he knew about it.

CHAIRMAN BOYER: Well, let's see if he knows.

THE WITNESS: I didn't expressly work on that case. I recall that the Committee, at the time, challenged. I think it had to do with take or pay contracts, if I recall.

Q. (By Mr. Monson) That's right.

A. And I don't remember if the 77 million was --

Q. Okay. That's what was throwing you?

A. It may be ball park, but I don't recall what the amount was.

Q. But you are aware of the case?

A. I really didn't work on that case.

Q. And you were working for the Office at that time, having just joined the Office from the Commission staff, right?

A. Yes.

Q. Okay. Would you like to see a copy of the Commission's order in the case? Would that help you?

MR. PROCTOR: I have to renew the objection with respect to any further --

CHAIRMAN BOYER: Yeah, I don't see the relevance of this line of questioning.

MR. MONSON: Can I proffer something?

CHAIRMAN BOYER: You may.

MR. MONSON: All right. I would, first of all, ask the Commission to take notice of the order in Docket No. 91-057-11 and Docket No. 91-057-17. It's in the order issued September 10, 1993.

And in this order the Commission states that the Committee of Consumer Services claimed that the decreases were insufficient -- these are decreases in the gas balancing account -- by $76,617,835 because Mountain Fuel should have purchased natural gas on the spot market.

MR. PROCTOR: May I respond to the proffer?

CHAIRMAN BOYER: Sure.

MR. PROCTOR: The manner in which Questar Gas purchases a commodity which is delivered directly to the consumer is so far apart from the particular issue that you have here before you, which is an interdependent relationship between an ECAM and a gas hedging program that's been in existence for four years, that any questions pertaining to this at this point forward are absolutely irrelevant.

CHAIRMAN BOYER: Well, I tend to agree with Mr. Proctor. I'm not sure where this is going. Are you trying to show some sort of inconsistency in the positions taken by the Committee and the Office over time?

MR. MONSON: Yes.

CHAIRMAN BOYER: Okay. Well, I don't -- let's not take the time to go there.

MR. MONSON: Okay.

CHAIRMAN BOYER: I don't think it's relevant.

Q. (By Mr. Monson) You're recommen -- excuse me. You're recommending that the Commission not allow front office transactions in the ECAM until it's studied the issue and determined the appropriate level of reliance on market purchases, including a demonstration that the Western market is robust enough to support that strategy; is that right?

A. That's correct. We're interested in getting more information in terms of the depth and liquidity of the various hubs that the -- where the Company does business.

Q. You also recommend that the Commission not allow any natural gas, fuel, or hedging costs in the ECAM until it has comprehensively evaluated that issue; is that right?

A. The hedging?

Q. Yes.

A. Yes.

Q. And you state, you state that both market reliance and hedging issues require more near-term analysis and specific guidance from the Commission on market reliance, and specific changes in endorsements from the Commission on hedging strategies and practices; is that right?

A. That's correct.

Q. What do you mean by "specific changes in endorsements"?

A. I, I think you've heard quite a bit of testimony today that, that right now the Commission doesn't have, effectively, a policy, for example on hedging, in terms of establishing baseline levels/ranges on hedging. That's what I mean. Same thing with FOTs.

Q. Do you believe the Commission would be willing to assume the responsibility of providing specific changes in endorsements on hedge -- hedging strategies and practices?

A. We think it's imperative that they take additional information on this and make an informed decision.

Q. So you think the Commission would, at the conclusion of this proceeding, you envision start to give specific guidance on the hedging practices of the Company?

A. That, that's our recommendation.

Q. And you talk in your testimony about baseline protections. Are they -- is that the same thing? Are you talking about the same thing there? These -- this guidance, these specific changes in endorsements?

A. I am.

Q. Didn't the Commission establish baselines in the 2009 general rate case, with regard to net power costs, based on a level of market reliance and hedging costs in that case?

A. Well, it set base rates. But we're dealing with an ECAM proposal, where variations in cost-related FOTs or hedging could potentially be passed through the ECAM. We think there needs to be some baseline protections set forth by the, by the Commission related to those two areas.

Q. The Office has been okay with the level of hedging and market reliance that was included in the last rate case, wasn't it?

A. In terms of the last rate case, I don't think we set -- I don't know if I can fully answer that, because I was working on the other side of the case. In terms of the cost of service part of the case. I wasn't involved in the net power cost portion of the case.

I know Mr. Falkenberg had various adjustments to the Company's net power cost level.

Q. Do you know if any of his adjustments were to either hedging costs or level of market reliance?

A. I don't know the answer to that.

Q. Okay. But the Company -- the Office does object to inclusion of these amounts in an ECAM; is that right?

A. We, we've, we think that there needs to be a first step, in terms of additional information needs to be presented and considered, analyzed by the Commission, before -- in the process of setting some, some -- making a baseline determination in the area of hedging and FOTs before they move forward with an ECAM.

Q. Well, assuming for a minute that the Committee -- the Office did not object, or didn't raise an issue with the level of hedging, or the cost of hedging, or the level of market reliance in the last rate case. What's different about not raising it there but raising it here?

A. Well, I think in an ECAM what you have here is the potential variability associated with what was set, you know, in base rates versus what might get passed through an ECAM. The risk gets shifted.

The Company -- the base rates get set. You manage the risk associated, you know, with your -- with, you know, your market purchases, et cetera, going forward. But with -- in an ECAM that, that potentially changes.

Q. (By Mr. Monson) But let's suppose for a minute the Company didn't -- let's suppose the Company decided not to hedge, and prices went up. Especially price of gas went up. Between, between now and the next general rate case. Can you accept that assumption for a minute?

A. I'll accept it.

Q. Okay. And then the Company came in in the next rate case and they said, Price of gas went up, we need higher rates, we need higher net power costs. What would the Committee's position be? Or the Office's position, I'm sorry.

A. So you're not doing any hedging, and then basically prices go up?

Q. (Moves head up and down.)

A. I mean, if we didn't challenge the -- run your scenario again. I want to make sure I've.

Q. Okay. We've got, we've got a general rate case with rates set.

A. Right.

Q. Including hedging.

A. Right.

Q. And a level of market reliance. And then the Company decides to stop hedging.

A. Okay.

Q. And then the price of gas and the price of fuel goes up. So in the next general rate case filed maybe a year later the Company comes in and asks for a large rate increase. What would the Office's position be?

A. I think we'd have a -- we'd want to analyze, you know, your decision to stop hedging.

Q. Okay. And wouldn't the -- if we continued to --

A. In terms of, you know, the reasonableness and, you know, the information, the criteria you used.

Q. Okay. And if we continued hedging, would that be a protection to the ratepayers from that increase in price in the next rate case?

A. Re -- or state it again, please.

Q. Okay. We've got a hedging program. We've got our rates set -- level of hedging costs, and then we continue that program.

A. Okay.

Q. Doesn't that provide some protection to customers that we're not gonna come in and ask for a huge increase because the price of gas went up?

A. I think it, you know, it does afford protections. What we're saying is that there needs to be a closer, closer scrutiny of the hedging program. Especially in the context of the ECAM.

Q. Okay. You state that customers need to have input into the hedging strategy, right? In your testimony?

A. I do. Or the Office does, yeah.

Q. And do you know how that was provided in the case of Questar Gas's gas balancing account before the Commission approved that account?

A. In terms of Questar Gas's risk management program?

Q. Right.

A. There was a series of meetings over, I want to say the better part of a year. Maybe around eight months. A stipulation was -- a stipulation came out of that that was presented to the Commission. Related to Questar Gas's hedging program.

Q. Okay. And when did that take --

A. But that was 2002, roughly.

Q. Okay, so there was a proceeding. Was the gas balancing account already in effect before that took place?

A. It was.

Q. Been in effect for many years, hadn't it?

A. Well, it had been -- I know it had been in effect since the '80s.

Q. Okay. You've also talked in your summary about the Commission's order in the 2007 IRP, right?

A. Yes.

Q. And you quoted that piece that's found on page -- lines 89 to 92 in your surrebuttal testimony?

A. Eighty-nine to 92?

Q. I think so. Yeah, page 4.

A. Yes.

Q. Okay. Now, doesn't this quote say that the Company should bear the risk of unreasonable costs?

A. That's what it says.

Q. So doesn't this imply that the Company should be able to include reasonable costs in the ECAM?

A. If -- with your assumption that if an ECAM was in place and it was able to demonstrate to the Commission, to its satisfaction, that the costs associated with deviations from its optimal portfolio were in the public interest, they could convince the Commission of that.

Q. So the issue is whether the costs are reasonable or not, right?

A. I'm just re -- I just put in what the Commission, you know, specified in their order.

Q. Okay.

A. In terms of, you know, a concern that the, that the selected portfolio might not be, you know, the least-cost-least-risk portfolio. And any -- or any changes from the portfolio identified as coming out of the 2007 IRP, the Company bore the risk.

Q. So if -- whether or not costs are reasonable can be examined in a general rate case, right?

A. That's typically where it occurs, yes.

Q. And in the last general rate case nobody raised any question about the reasonableness of the hedging costs or the market reliance; is that right?

A. I think I earlier said I couldn't speak to that.

Q. Okay. And, and can't the reasonable -- reasonableness of those costs also be examined in a pass through proceeding?

A. I think, I think they could if you met the threshold issues in terms of what we're raising here, is we need some Commission guidance in terms of establishing baselines in the area of hedging and also FOTs.

MR. MONSON: That's all.

CHAIRMAN BOYER: Okay, thank you Mr. Monson.

Ms. Schmid, are you going to have questions of Mr. Gimble?

MS. SCHMID: No questions.

CHAIRMAN BOYER: Okay. Ms. Hayes?

MS. HAYES: No questions.

CHAIRMAN BOYER: Mr. Evans? We're gonna break here in about two minutes. I don't want to --

MR. EVANS: I can do it in two.

CHAIRMAN BOYER: Let's see you do that. Proceed, Mr. Evans.

CROSS EXAMINATION

BY MR. EVANS:

Q. Good afternoon Mr. Gimble.

A. Good afternoon.

Q. Referring to Mr. Monson's hypothetical where he asked you if the Company quit hedging and gas prices went up, what would you say? Do you recall that hypothetical?

A. I do.

Q. Is it the Commission's proposal that no hedging of natural gas should occur?

A. That's not our proposal. We think it needs to be closely examined.

Q. Somewhat less than the Company is doing right now but not nothing, right?

A. Yeah, not nothing.

Q. Okay. Question for you on cross as well. How long do you con -- do you believe it might take for the Commission to get -- well, let me ask you this first.

Do you contend that this process ought to be outside the IRP or within the IRP?

A. We -- our position is it should be outside the IRP initially.

Q. And --

A. But possibly within the IRP going forward after that.

Q. And does the Office contemplate that that review could be done by the conclu -- let me back up.

If the Company were to file a general rate case in January, is it the Office's view that this Commission review of hedging practices could be done by the completion of the general rate case?

A. By the completion of the general rate case?

Q. Yes.
A. Yeah, I think that's a fair assessment. I think it could be.
Q. So that, so that maybe a January rate case -- a rate case filed in January might be an appropriate time to reset hedging costs for the purposes of an ECAM?
A. That, that time frame might work.
MR. EVANS: No further questions. Thank you.
CHAIRMAN BOYER: Actually, Commissioner Allen has no questions. Commissioner Campbell?
COMMISSIONER CAMPBELL: Are you aware if the Commission has provided guidelines to Questar as it relates to their hedging program? I mean, has the Commission dictated specifics about that program before?
THE WITNESS: I think there are some general guidelines.
COMMISSIONER CAMPBELL: So if we don't have specific -- or I, I think some of the things that you want the Commission to share with the Company, wouldn't that kind of get over into that territory of micromanaging?
I mean, how -- certainly generalities are somewhat okay, but some of the issues that you've been

talking about seem quite specific to me. And I don't know if we feel like we have the expertise to make some of those decisions. And certainly not the record before us right now.

THE WITNESS: And that's why we're -- you know, our recommendation is to get, get the information and create that record so you can make, you know, an informed decision. And, you know. And maybe we are just going to, you know, end up with general guidelines.

But, you know, we, we do think there needs to be baseline protections for customers in these areas of, you know, market reliance and hedging. And so we are looking for the Commission to give some...

COMMISSIONER CAMPBELL: I will confess, I've done a sneak peak of your other testimony. And the question is, is are there protections in the design of the ECAM that can be put into place that address these issues before we actually get into the weeds on these issues?

THE WITNESS: And I'm not -- our testimony in this phase, phase is you can't deal with these threshold issues in market reliance and hedging through design. We think there needs to be a separate process. A separate, you know, focus proceeding to deal with it.

CHAIRMAN BOYER: Well, Commissioner Campbell asked my questions, so I have none.

Mr. Proctor, are you gonna have any redirect?

MR. PROCTOR: Nope.

CHAIRMAN BOYER: Okay, very well. You are excused, Mr. Gimble.

THE WITNESS: Thank you.

CHAIRMAN BOYER: Thank you. We're hopeful that we can conclude this telephone conference in 15 minutes or so, so we'll take a recess until then.

We're also hopeful that we can conclude this hearing today. I know we have at least a couple of witnesses from out of town. I don't know where Ms. Kelly lives these days.

MS. KELLY: I live in Pocatello.

CHAIRMAN BOYER: Okay.

MS. KELLY: My daughter's birthday is tomorrow. So if I could get home tonight, that would really be wonderful.

CHAIRMAN BOYER: We will not be having hearings tomorrow. We are 110 percent committed tomorrow ourselves.

MS. KELLY: Okay.

COMMISSIONER BOYER: Okay, very well. We'll see you back here within 15 minutes or so.

(A recess was taken from 2:57 to 3:18 p.m.)

CHAIRMAN BOYER: We're back on the record. Thanks for your patience. We were able to -- we're not very smart but we are fast, as I told Mr. Evans in the hallway.

All right. Mr. Wielgus?

MR. WIELGUS: Yes.

CHAIRMAN BOYER: You have not been sworn in this matter.

MR. WIELGUS: Not yet.

(Mr. Wielgus was sworn.)

CHAIRMAN BOYER: Thank you. Please be seated.

PAUL WIELGUS,

called as a witness, having been duly sworn,

was examined and testified as follows:

DIRECT EXAMINATION

BY MR. PROCTOR:

Q. Mr. Wielgus, would you state your name, spell it for the reporter please, and describe the nature of your business, your occupation?

A. Sure. My name is Paul Wielgus, W-i-e-l-g-u-s. I'm the managing director with GDS Associates, which is an energy consulting firm with --

headquartered in Marietta, Georgia.
Q. And how long have you been engaged in the consulting business?
A. Off and on for about six years.
Q. Are utilities a general focus of your particular consulting work?
A. Utilities, municipal, some industrials, and some other private clients.
Q. And in this particular matter you were retained by the Utah Office of Consumer Services; is that correct?
A. Yes.
Q. And generally what was the description of your duties?
A. To generally discuss natural gas hedging costs and related matters.
Q. And in -- and you prepared testimony in this matter that's been prefiled with the Commission, correct?
A. Yes.
Q. And did you have an opportunity and did you take the opportunity to review the filing that had been made by Rocky Mountain Power?
A. Yes.
Q. And the testimony that had been supplied --

or submitted in connection with that application?

A. Yes.

Q. Did that include also Phase I of the -- this proceeding, that was resolved by an order in February?

A. Yes. From what I recall, yes.

Q. There is an exhibit list that has been circulated that contains the exhibits of your testimony. Did you prepare or cause to be prepared that prefiled written testimony?

A. Yes.

Q. Do you have any corrections to the testimony?

A. Yes, I do. On Page 7 of the direct testimony, line 143, "uncertainties" is misspelled. It should be spelled as in line 144.

Q. If I were to ask you, then, the questions that were put to you in the written question -- written testimony would your answers today remain the same?

A. Yes.

MR. PROCTOR: The Office would offer the admission -- or ask that you admit the testimony as listed on the exhibit list pertaining to Mr. Wielgus's testimony.

CHAIRMAN BOYER: Are there objections to the admission of Mr. Wielgus's direct and surrebuttal testimony, together with exhibits?

They are admitted.

(Exhibit Nos. OCS-4D Wielgus, OCS-4.1, Appendix, OCS-4SR Wielgus, and OCS-4.1SR were admitted.)

Q. (By Mr. Proctor) Mr. Wielgus, have you prepared a brief summary of that testimony?

A. Yes, I have.

Q. Would you provide it, please, to the Commission and the parties?

A. Yes. The purpose of my testimony was to generally discuss natural gas hedging costs and related matters. My conclusions, based on my review and experiences, are:

One, to sufficiently evaluate the result of natural gas hedging there needs to be a thorough analysis of the associated transaction costs.

Two, the benefits of partial levelling of rates based on natural gas hedging should be valued and compared to other rate stability options and the cost of stability.

Three, the use of natural gas price options by the Company should be evaluated for implementation.

Four, the purpose of the Company's hedging activities should be decided.

And five, the policy formulation regarding hedging and the ECAM should be made after the necessary input on these issues and others is received and the analysis is complete.

Until the above is accomplished, a decision on whether the Company's natural gas hedging and ECAM are consistent with the public interest is precluded.

A statement by one of the Company's witnesses, Mr. Graves, supports this when he states that one of the practical consequences of the proposed ECAM is that the right amount of risk management should become a policy that is decided with input and guidance from the Commissioners and the customers.

Q. Does that conclude your summary?

A. Yes.

MR. PROCTOR: Mr. Wielgus is available for cross.

CHAIRMAN BOYER: Thank you Mr. Proctor.

Mr. Monson?

MR. MONSON: Thank you.

CROSS EXAMINATION

BY MR. MONSON:

Q. Mr. Wielgus, just to pick up on what you just said in your summary, you quoted something from Mr. Graves' testimony?

A. Yes.
Q. Mr. Graves acknowledged that with an ECAM in place it was important to find out what level of risk tolerance the customers would have, right?
A. I don't recall, but I'll take your word for it.
Q. And -- but he did not recommend that that needed to be done before inclusion of hedging costs and market reliance in the ECAM, did he?
A. I don't recall, but I think that's the case that he did not recommend that.
Q. Okay, thank you. Rocky Mountain Power sent a data request to the Office asking for prior testimony -- testimony by you on hedging. Did you -- did the Office consult with you on a response to that request?
A. Yes.
Q. And the response was that prior to this docket you hadn't submitted any testimony on hedging; is that right?
A. I hadn't submitted any testimony I think on point was the question that was asked.
Q. Okay. And so I was looking for what experience you would have with the issues related to hedging. And I noticed that you, from 1991 to 1997,

were a director at Enron Capital and Trade. Is that with -- in that job did you have experience with hedging?

A. Yes.

Q. And could you tell us a little bit about what you did?

A. A number of different responsibilities, from origination to short-term marketing of various energy projects and energy supply. Also some capital projects as it related to power project gas pipelines and electric-drive gas compression services.

Q. Okay. But with regard to trading in the gas market?

A. No, I was not a trader, but worked very closely with traders and with the pricing lists to price the products -- both short and long-term origination products -- on the supply -- on the power supply and on the gas supply.

Q. So both gas and electric?

A. Yes.

Q. And did you have any responsibility for developing the strategy followed by Enron in its trading strategies?

A. No.

Q. Okay. In, in your testimony you say that there's some indication, based on Mr. Duvall's rebuttal testimony, that the Company's changing its position with regard to the objective of the hedging program; is that right?

A. Yes.

Q. You attach -- as one of the bases for that you attached, as an exhibit to your surrebuttal testimony, a data request; is that right?

A. Yes.

Q. Can you please explain to me how this response to this data request indicates that the Company is not still hedging to reduce the risk of -- the adverse risk of market prices changing?

A. Up until this point it was clear to me that the Company's position was that it was minimizing the volatility associated with those prices.

Q. Okay. And isn't that what this answer says: Hedges, whether fixed price for -- physical or fixed-for-floating financial swap transactions, are executed to reduce the risk of adverse market prices sometime in the future?

A. An adverse market price is different than fixing the volatility of a price.

Q. In your mind, it's different?

A. In my mind it's different, yes.

Q. How?

A. In my mind it's different in that if you, if you are taking on and managing the volatility of that price you've accepted that market -- risk of that particular market. And here you're talking about the adverse market positions or prices in that market versus just fixing the volatility of that, that market.

Q. Okay.

BEGIN STRICKEN PORTION

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END STRICKEN PORTION

Q. (By Mr. Monson) You also discuss enterprise risk management in your testimony, right?

A. Yes.

Q. And you discuss the various risks the Company is attempting to manage. And suggest that if the risks were applied at the enterprise level, from the ratepayer perspective, in addition to being applied at the policy level, the process could produce the best results; is that right?

A. I don't recall if I say the best results, but it could result in better, better results.

Q. If you'd turn to line 81 of your surrebuttal?

A. Oh, "the best results."

Q. Okay. What do you mean by "the best results"?

A. The best results would be results that not only took into consideration how that resource might be spent to whether it's fixing the volatility of the price, managing the market risk of that market.

Or perhaps there's better ways to spend that -- those additional resources in other areas, from the ratepayers' perspective, as it relates to the limited amount of resources, just like the Company has, that the ratepayer may have.

That -- other options in -- perhaps labelled as investing those dollars, perhaps there may be a better or best place for that, other than the current managing the volatility. After that analysis it may come back, but that is the answer.

Q. And so is there any way the Commission could measure, quantitatively, whether the Company had achieved the best result?

A. I think there can be an opinion as far as one result is better than the other. And the options that are available, one isn't the best result.

Q. Are you suggesting by this testimony that the measure would be the lowest cost for NPC? For net, for net power costs?

A. No.

Q. Okay. Would you agree with me that natural gas and electricity are now commodities?

A. Yes.

Q. And any company that trades in commodities should have a front office, a mid office, and a back office?

A. Yes.

Q. And you agree that even if the Company did not do physical or financial hedges, it would still be required to have these front office, mid office, and back office, right?

A. To some degree.

Q. But you disagree with Mr. Duvall's testimony that the costs associated with these offices would largely be incurred even if the Company did not have a hedging program?

A. Yes.

Q. Okay. And you said there was -- you said there would be a measurable reduction in IT systems, reporting, accounting, legal, and risk management compliance resources if the Company didn't have a hedging program?

A. Yes.

Q. When you say "measurable," what do you mean?

A. That it would be something that would be noticed as far as the expenses from the Company's perspective, and ultimately the ratepayers' perspective, of what those costs would be to not only manage the physical transactions, but on top of that the financial transactions.

Q. Did you, did you do any kind of analysis or study of the Company's risk management personnel, or office, or the hedging group in the Company?

A. We asked a data request, I think. But I honestly don't recall whether we divided -- or looked at allocating or estimating costs of hedging versus physical.

Q. Do you have any idea what percentage of the trades that the front office does at PacifiCorp are for hedging, versus simply cash purchases to meet daily needs?

A. No, I don't.

Q. Would you accept, subject to check, that it's less than 5 percent?

A. Could you re-ask that question?

Q. Would you accept that the amount of trades for hedging is less than 5 percent of the total number of trades?

A. I guess it would depend on how you, how you valued that percentage. It's 5 percent of?

Q. Number of trades.

A. If -- subject to check, sure. That's fine.

Q. I mean, does it seem reasonable, based on your experience?

A. That could be reasonable, sure.

Q. Okay. So -- and I -- and did you read Ms. Schell's testimony?

A. Yes.

Q. She says in there there's one gas trader, right?

A. Yes.

Q. Now, at the time she checked there was an opening, so there's really two gas traders. But if the Company were to reduce its number of trades by 5 percent could it eliminate either of those two positions, do you think?

A. I don't know the answer to that. But there's a lot of spun-off activities as a result of that hedging. One of the reasons we're here today.

Q. If -- do you -- you don't know how many traders the Company has for electricity?

A. No, I don't know.

Q. Let me ask you to assume that there's six traders on, on the job at any given time. Two of whom are buying and selling electricity realtime. One is a forward trader and also engages in cash trades. And the other three are cash traders who deal with near-term trades in the balance of the current month and the next month. Does that sound reasonable?

A. I don't, I don't know the answer if that's reasonable or not based on, based on your description. But I assume it is.

Q. Do you know how many of those individuals could be let go if the Company were to reduce its number of trades by 5 percent?

A. No, I don't. And, you know, you make some descriptive terms there, whether it's cash traders, when we talk about front office transactions. I think that's one of the issues that we have, is what -- for all of us to properly and appropriately understand, when we say these different terms, exactly what they mean.

And I'm not sure that's the case. So that's part of the issue in trying to answer your questions.

Q. Do you know what IT systems the Company could eliminate if it reduced its number of trades by 5 percent?

A. No. But they, they recently I, guess, either have implemented, or proposed, or have approved a new system to track some of their trades. Or to track their trading.

Q. Do you know whether or not that was caused by hedging, or was it caused by the number of trades?

A. I would assume that hedging drives a considerable amount of that.

Q. Even is hedging is only five percent of the number of trades?

A. Sure, yes. Yes.

Q. Why would that be?

A. Because of the complexity and the, and the financial exposure associated with putting on expositions.

Q. Are you aware that none of the costs of the traders, the IT systems, the reporting, accounting, or legal are included in net power costs?

A. I'm not aware of that.

Q. And if they aren't included in net power costs they wouldn't be recovered through an ECAM either; is that right?

A. But they would be paid by the ratepayer in some form or fashion, I assume.

Q. Would they be included in a general rate case under O&M expenses?

A. I don't know the answer to that, but perhaps.

Q. Okay. And if they were, then they'd be examined whether they were reasonable or not in a general rate case?

A. I would assume so.

Q. So they wouldn't impact the ECAM?

A. They would impact the cost to the ratepayers.

Q. Okay. And -- but you say the more important issue with regard to hedging is the, is the transaction cost relating to credit and -- which can be very material, right?

A. Yes.

Q. Okay. Do you understand how the costs relating to credit are incurred in hedging transactions?

A. Yes.

Q. Can you explain that?

A. It could be a number of different ways. One could be -- it's dependant upon the transaction that the Company has entered into and what the counterparty on the other side of that transaction requires. It can be in a form of a letter of credit. It can be form of posting cash. It can be in the form of actually making payments to that, to that counterparty.

There's a number of different structures that can be put together. And that's negotiable between the two counterparties, the Company and the other counterparty.

Q. Okay. So let's suppose the Company is on the wrong side of the hedge and it has to post cash collateral, say, to the counterparty. Is that a -- is that something that can happen?

A. Could happen.

Q. Do you understand what accounting takes place if the Company is required to post, post cash collateral?

A. No, I'm not familiar with the exact accounting of that.

Q. Would you accept that it reduces the working capital available to the Company?

A. Probably.

Q. Is working capital included in net power costs?

A. I don't know the answer to that.

Q. Do you know how working capital is determined in a rate case?

A. I don't know the answer to that.
Q. Assuming that working capital is determined in a rate case based upon a lead/lag study -- are you familiar with lead/lag studies?
A. No.
Q. Okay.
MR. MONSON: That's all my questions.
CHAIRMAN BOYER: Thank you Mr. Monson.
Ms. Schmid, have you questions of Mr. Wielgus?
MS. SCHMID: No questions.
CHAIRMAN BOYER: Okay.
Okay, turning now to Ms. Hayes. Questions for Mr. Wielgus?
MS. HAYES: No questions.
CHAIRMAN BOYER: Mr. Evans?
MR. EVANS: Just, just a very short one, Mr. Chairman.

CROSS EXAMINATION

BY MR. EVANS:
Q. Mr. Wielgus, I have a, I have a question about your testimony online 107 of your direct, beginning there?
THE REPORTER: Can you speak up, Counsel, please?

MR. EVANS: Yeah. The light's on, that's usually the problem.

Q. (By Mr. Evans) Beginning with line 107 on your direct testimony you discuss -- and there's some confidential text in here as well. But the discussion is how one might estimate the value that ratepayers receive from the Company's incurred hedging costs.

Is that -- have I got that right?

A. Repeat that again, please?

Q. Well, how you might value the benefit that ratepayers receive from the Company's incurred costs of hedging.

I'm looking at line 113 specifically in that paragraph. The value of the Company's energy hedging program can be looked at by comparing?

A. Yes.

Q. And, and to rephrase, maybe. What I think you're saying is that you can somehow value the benefit of the partial levelling of rates.

How would, how would one go about doing that? I'm just -- I'm curious.

A. There would have to be some exercise to, to try to calculate how valuable -- what is the value that the ratepayer would be willing to pay for the, for the level of price stability that the natural gas hedges provide.

Q. This is Commissioner Campbell's question, essentially, isn't it?

A. Yes.

Q. And are you saying that there's a way to monetize that value?

A. There may not be a way to monetize it, but there's a way to calc -- try to calculate that. To -- it would be an estimate, but it would be, it would be an estimate of that value to the customer.

Q. Would that estimate be in dollars?

A. Yes.

Q. Okay. So, so you believe that's an estimate that ought to occur before these costs go into ECAM; am I correct in assuming that?

A. Yes.

Q. And that could occur in some other proceeding, not this one, is how I understand the Office's position?

A. It should, it should occur in the proceeding as it relates to the hedging practices and, and the ECAM.

Q. Thank you.

MR. EVANS: No more questions.

CHAIRMAN BOYER: Thank you Mr. Evans.

Commissioner Allen?

COMMISSIONER ALLEN: No.

CHAIRMAN BOYER: Commissioner Campbell?

COMMISSIONER CAMPBELL: On page 10 of your direct testimony you list five recommendations. And I guess my question to you is, are those recommendations related to hedging as, as they would be used in an ECAM, or are they related to hedging as it is used today?

THE WITNESS: As it would be in ECAM.

COMMISSIONER CAMPBELL: And I think I heard -- when you talked about the partial levelling of rates I think I heard, in Mr. Gimble's cross examination, a hypothetical where, where there would be some customer rate stability if you had a second rate case involved.

And I think the hypothetical went that if you, you hedge natural gas costs in Rate Case 1, and then in Rate Case 2 you continue to hedge, there might be some, some degree of levelling of rates there.

In that situation, I mean, what -- once again, I'm not sure how you value that. Maybe it's back to Mr. Evans' question. Is that worth $200 million to ratepayers? Or how, how do you assign -- I still -- for Mr. Evans' question I didn't hear how you assign dollar numbers to benefit of stability.

THE WITNESS: I think that's two different questions if you're asking it from the way the net power costs are recovered today, versus the way perhaps they would be under an ECAM. Today I agree with your comment that the protection is for the Company.

And the Company is making those decisions for its protection. And the Company has designed its program, and its risk management policy, and its risk tolerance is all designed to address the risks that it has under the current design.

They've basically constructed their book -- they've constructed their policies to manage their book. And if an ECAM were implemented today, basically what the Company would be doing would be transferring that book to the ratepayers.

Which the ratepayers don't have a clear understanding -- as was, I think, exemplified today in, in the testimony -- don't have a clear understanding of exactly what's in that book. They didn't design the program. And they have no idea what the value of that book is.

And I think until the parties have, have done the necessary work to value what's in that book so that when that book is basically transferred from the Company's side to the ratepayers' side they fully understand the value of that book, I, I can't think of a situation where any trader, any originator, anybody who is looking at a trading book would, would agree with the Company and transfer that book, say overnight, to the other side of the business, to the ratepayers.

And as Mr. Duvall recommended, not to change anything that's in there as a result of that transfer, that just -- I just can't envision where someone would recommend to the Company, without having the necessary -- having done the necessary due diligence, that they would accept that book, as is, with no changes, and to continue to do the same activity.

COMMISSIONER CAMPBELL: So it's a fair assumption that, that Company incentives and motives as it relates to hedging might be different than what customers would expect or want?

THE WITNESS: Under its current design and proposed design, very much so. Yes.

CHAIRMAN BOYER: Mr. Evans asked my question, and Commissioner Campbell followed up with my second question. But I, I mean, I -- based on my own experience I know that ratepayers do not like volatile prices.

They don't like increasing prices, but they dislike even more volatile prices, I think. Prices that go up and down. But I'm still not clear as to how one monetizes the benefit of rate stability between case, to case, to case.

THE WITNESS: No, no system will be perfect. No -- at some point the ratepayers will accept some of that risk, some of that price change risk, regardless of whatever type of program design. At the very -- at the, at the very forward years there is that -- the ultimate risk to the ratepayers.

One way to, to put a value on that stability is one of the things has been mentioned, one of the options that the Company hasn't taken on yet, is the implementation of price options. They're very definable. They have a, they have a very defined time.

You can either do them on the exchange or you can do them readily over the count -- over the counter. They're very liquid. And they have a very set price.

So the customer could see, If I want this stability -- basically a cap -- and if the price falls below that cap I get the benefits, they can then measure for this stability it's this price, for this stability it's that price.

So the customers can then make a decision, the ratepayers can then make a decision, based on the price of that certainty that they want, is it worth that premium? Or is a lesser premium more -- so that is one way to be able to -- the term earlier was "monetize." That is one way to be able to monetize the value of that stability. Especially the downward stability.

There's no better price protection from a buyer perspective -- which the ratepayer is -- there's no better buyer protection than a price option. Because they get the, the benefit of the price protection, but they also share in the downside of the market, which is important to them. Or should be important to them.

CHAIRMAN BOYER: Is it fair to say that the Office believes that ratepayers should have some involvement in at least defining hedging practices? Some kind of input into that process?

THE WITNESS: Absolutely.

CHAIRMAN BOYER: And there's a concept in the law dealing with risk allocations, especially among tort lawyers. And the general rule of thumb is that risk should be placed on those best able to mitigate that risk. Or those who caused the risk.

How, how would you envision ratepayers actually weighing in on hedging practices with, you know, the level of hedging? The, you know, whether you hedge one year out or two years out, or whether you hedge 50 percent, or 80 percent, or 100 percent. How, how do customers weigh in on that?

THE WITNESS: I think they weigh in through a process like this. I think, unlike the IRP -- I'm not an expert in the, in the, in the legal weight of the IRP, but it seems to be more of, of a process that it is actually something that is more binding.

And the purpose of an IRP is least cost objective. Hedging isn't necessarily least cost. So there should be a separate proceeding where it is litigated in a setting like this. The evidence is presented. Each gets -- each ratepayer interest gets to, to weigh in on that, and the Commission decides.

CHAIRMAN BOYER: Okay, thank you Mr. Wielgus.

Redirect, Mr. Proctor?

MR. PROCTOR: No, thank you.

CHAIRMAN BOYER: You are excused. Thank you very much.

THE WITNESS: Thank you.

CHAIRMAN BOYER: We'll hear now from Dr. Schell.

(Dr. Lori Smith Schell was sworn.)

CHAIRMAN BOYER: Thank you. Please be seated.

DR. LORI SMITH SCHELL,

called as a witness, having been duly sworn,

was examined and testified as follows:

DIRECT EXAMINATION

BY MR. PROCTOR:

Q. Dr. Schell, would you state your name, spell it for the reporter of course, and describe in general your occupation and your interest?

A. Okay. My name is Lori Schell, S-c-h-e-l-l. I am the founder and owner of Empowered Energy, a small independent consulting company in Colorado.

Q. How long have you been engaged in consulting?

A. On my own, for eight years. And much earlier in my career for another five years.

Q. Was there a CV attached to your testimony?

A. Yes, there was.

Q. You are here testifying on behalf of the Utah Office of Consumer Services. Could you describe what the Office's direction to you was?

A. Was to look at the hedging policies of the Company. And to determine whether they were reasonable and represented the interests of the ratepayers.

Q. You are a Ph -- hold a Ph.D.?

A. Yes.

Q. And what -- in what field?

A. In mineral economics and operations research.

Q. And have you been engaged in consulting in connection with utility programs and utility policies?

A. I have done some consulting for utilities.

Q. Have you ever been involved in a subject matter such as the one that's in this particular case, and that's hedging?

A. In -- with respect to utilities?

Q. In any hedging.

A. In any hedging? I've been very actively involved in hedging as a professional in one of my corporate positions.

Q. And which one was that?

A. That was at Trigen Energy Corporation, where I was the director of energy risk management.

Q. And is Trigen a public utility?

A. It is not. It is a combined heat and power company, so has both the electric and the natural gas interests.

Q. As part of your -- the request from the Office you have prepared testimony that is listed on the exhibit list; is that correct?

A. Yes.

Q. And this was prepared under your direction or by you?

A. Yes.

Q. Do you have any corrections to make to any portion of that testimony?

A. Yes, I do. On the Exhibit OCS-2.2, on page 1, I incorrectly referred to the docket number in the first column of numbers. The correct docket number should be "03-2035-02." And the same correction applies for Exhibit OCS-2.3 Schell, where the first column should have that same label, "03-2035-02."

Q. And with those corrections, if I were to ask you the questions that you answered in your prefiled written testimony would your answers today be the same?

A. Yes, they would.

MR. PROCTOR: The Office would move for admission of the testimony of Dr. Schell, as listed and as numbered on the exhibit list which you have before you.

CHAIRMAN BOYER: Is there any objection to the admission of Dr. Schell's direct and surrebuttal testimony, together with exhibits?

They are admitted.

(Exhibit Nos. OCS-2D Schell, OCS-2.1, OCS-2.2, OCS-2.3, OCS-2SR Schell, and OCS-2.1SR were admitted.)

Q. (By Mr. Proctor) Dr. Schell, do you have a summary of your testimony that you could provide?

A. Yes, I do. So in Phase I of this docket I testified that PacifiCorp Energy was generally in compliance with its volume-based hedge targets with respect to natural gas.

With respect to its year one hedge targets this meant that PacifiCorp Energy had hedged up to and in excess of 100 percent of its forecast natural gas requirements, effectively reducing the volatility of the natural gas price component of PacifiCorp's net power costs.

In Phase II of this docket I testified that PacifiCorp Energy's volume-based hedge targets should be reduced across the board. And that its year one maximum hedge target should be reduced by up to 15 percent of PacifiCorp's total megawatt hour requirements.

This conclusion was based on an analysis of PacifiCorp's total system balancing sales and purchases. System balancing requirements occur due to the short-term interim month changes in load and generation, which reduce the ability to effectively hedge the associated volumes.

Transaction costs could be avoided by not hedging volumes associated with this inherent frothiness in PacifiCorp's operation.

Based on my recommendation to reduce the volume based hedge targets I also recommended that the range associated with the new To-Expiry Value-at-Risk, or TEVaR Metric, should be reexamined. This was based on the fact that the TEVaR metric was designed to provide "reasonable continuity" with the volume based hedge targets that it has now replaced.

Reducing the volume based hedge targets could increase the target range of those TEVaR values, providing increased hedging latitude to PacifiCorp Energy.

Q. Does that conclude your summary?

A. Yes, it does.

MR. PROCTOR: Dr. Schell is available for cross.

CHAIRMAN BOYER: Okay, thank you.

Mr. Monson?

MR. MONSON: Thank you.

CROSS EXAMINATION

BY MR. MONSON:

Q. Dr. Schell, Rocky Mountain Power sent a data request to the Office requesting information about prior testimony you had filed on hedging. Were you consulted about the answer to that question?

A. Yes, I was.

Q. And isn't it correct that the response said that prior to this case you hadn't filed testimony on hedging?

A. That is correct.

Q. Okay. But you're -- you mentioned you had experience at Trigen Energy?

A. Yes.

Q. And I think I maybe didn't hear correctly, but what kind of company is Trigen Energy?

A. It's a combined heat and power company. A cogeneration, or in their case tri-generation company.

Q. Okay.

A. That --

Q. Is it a regulated public utility?

A. In certain jurisdictions it was.

Q. Okay. And what jurisdictions did it operate in?

A. The main electric power RTOs that it got rated in were the PJM, the New York ISO, focus in synergy and (the witness is speaking too softly.)

THE REPORTER: I'm sorry, I didn't hear the end of the answer.

THE WITNESS: Synergy and Entergy.

Q. (By Ms. Schmid) So it was a generator that would sell power to other -- to utilities; is that right?

A. It was a generator of electricity as well as co-generated steam, hot water. But yes, the main product it sold was electricity.

Q. Okay, thank you. Your -- as you said in your summary, one of your, one of your two recommendations is that the company should lower its volume based hedge targets based on system balancing; is that right?

A. That's correct.

Q. And you acknowledge there will always be a need for system balancing, but that the magnitude and duration of that activity cannot be determined until realtime load and generation conditions make themselves manifest?

A. Yes.

Q. So you, you state that Exhibit 2.2 of your testimony contains summary data related to PacifiCorp's reported net power costs over time; is that right?

A. Yes.

Q. And in your exhibit you've compared the level of system balancing activity with the total energy requirements, based on net power cost studies used in six rate cases?

A. That's correct.

Q. And on the basis of these studies you conclude that the average volume weighted level of historical total system balancing activity as a percentage of total energy requirements is 14 percent?

A. Yes.

Q. On that basis you recommend that the Company should lower its first-year volume based hedge targets to no more than 85 percent of its forecast total energy requirements?

A. That's correct.

Q. You acknowledge an implementation of your proposal would increase the Company's rate volatility; is that right?

A. Yes.

Q. Have you obtained any input from customers as to whether or not they would mind that increase in rate volatility?

A. I think that's one of the main issues of this proceeding, is that to my knowledge there has been no input from the ratepayers. And so we don't know how much they value the rate stability.

Q. Okay. Now, are you aware that the net power cost studies that were used in the six rate cases are the result of grid model runs?

A. Yes.

Q. So they're not actual historical results?

A. That's correct.

Q. And in fact when actual historical results are reported they don't show purchases or sales for system balancing, they just show short-term, firm, and non-firm purchases and sales; is that right?

A. That is correct. So I was unable to confirm whether, in reality, the same results would occur.

Q. And a short-term purchase or sale can actually be a sale that's made months or even years in advance, it just happens to be short-term in that it's only 30 days or less, right?

A. I didn't focus on the short-term sales, I just focussed on the system balancing category.

Q. Okay. But, I mean, my point is that your focus then was on model runs, not on actual results?

A. Yes.

Q. So we don't really know at the end of the day, because -- because we can't predict in advance, as you said, the magnitude and duration of the balancing until realtime load and generation conditions make themselves manifest, we don't actually know the actual purchase and sales that work for system balancing, do we?

A. We do not. And apparently that data is not available from the Company.

MR. MONSON: That's all I have. Thank you.

CHAIRMAN BOYER: Thank you Mr. Monson.

Ms. Schmid?

MS. SCHMID: No questions.

CHAIRMAN BOYER: Ms. Hayes.

MS. HAYES: No questions.

CHAIRMAN BOYER: Mr. Evans?

MR. EVANS: None here, thank you.

CHAIRMAN BOYER: Commissioner Allen?

COMMISSIONER CAMPBELL: No.

CHAIRMAN BOYER: Nor do I. You may be excused. Thank you, Dr. Schell, for participating.

Okay. Now we will hear from Ms. Kelly in time to get her home for her birthday festivities tomorrow, it looks like.

Ms. Kelly, have you been sworn in this proceeding?

MS. KELLY: Yes, I was.

CHAIRMAN BOYER: In Phase I? Okay. The floor is yours, Ms. Hayes.

MS. HAYES: Thank you.

NANCY L. KELLY,
called as a witness,
having previously been duly sworn,
was examined and testified as follows:

DIRECT EXAMINATION

BY MS. HAYES:

Q. Ms. Kelly, please state your name for the record?

A. Nancy L. Kelly. Oops, sorry. Nancy L. Kelly.

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

A. Western Resource Advocates. I'm a senior policy adviser.

Q. On whose behalf are you testifying today?

A. Today I'm testifying on behalf of Western Resource Advocates and Utah Clean Energy.

Q. Have you participated in this docket for Western Resource Advocates and Utah Clean Energy?

A. Yes, I have.

Q. Did you file direct testimony marked for identification on the exhibit list as WRA & UCE Exhibit II.1-1.OD, along with accompanying exhibits marked for identification as WRA & UCE Exhibits II.1-1.1D and II.1-1.2D?

A. I did.

Q. Do you have any changes or corrections to that testimony?

A. Yes.

Q. Would you walk us through those?

A. Yes.

Q. Thanks.

A. Beginning with my direct. On page 3, line 51, that should say "IRP 2007."

And then surrebuttal. On page 2 I have two corrections. At very end of line 29, the word "is" should be struck. And be replaced with the word "as." On line 40, the last sentence, "it also" should be struck and replaced with "the order further."

MR. MONSON: I didn't understand. Excuse me, I didn't understand that change. Could you -- what should be stricken?

THE WITNESS: Instead of, instead of saying "It also states," it should say "The order further states."

MR. MONSON: Thank you.

THE WITNESS: Certainly.

On page 13, row 272, there should be the word "and" inserted after "in," so that it says "the IRP process has not resulted in an optimal mix of resources...."

On page 18. On -- this one's a little bit longer. At row 364, the sen -- there's a sentence that begins "The purpose of integrated resource planning is not to identify...." Strike the word "the." Replace the word "the" with "a portfolio that will be."

Then it would say "least cost." Strike the word "portfolio." Insert "if the set of assumptions underlying the construction of the portfolio comes about."

And I will read that sentence the way it should, should look. And if anyone would like, I -- we have copies of what I did, so. So it should now read:

"The purpose of integrated resource planning is not to identify a portfolio

that will be least cost if the set of
assumptions underlying the construction
of the portfolio comes about, but to
identify a portfolio that balances cost
and risk over a range of possible
futures."

On same page, line 382. In the middle of the line is the word "no." That should be capitalized and a period should be put after it so that it references number.

Page 19, row 400. There are two words there that need to be combined. Instead of saying "to ward" the market it should say "toward" the market.

And finally on page 20, footnote 42 needs to be moved from line 417 to line 427. Thank you.

Q. Thank you.

A. That completes my corrections.

Q. And I just want to mention that your surrebuttal testimony is marked as Exhibit 2.1-1.OSR.

So given these corrections, if you were asked the same questions today as set forth in your prefiled testimony would your answers be the same today?

A. They would.

MS. HAYES: Western resource advocates and Utah Clean Energy then move to admit the testimony of

Nancy Kelly as marked.

CHAIRMAN BOYER: Are there any objections to the admission of Ms. Kelly's direct and surrebuttal testimony, as corrected, and together with exhibits? They are admitted.

(Exhibit Nos. WRA & UCE II.1-1.0D, WRA & UCE II.1-1.1D, WRA & UCE-II.1-1.2D, and WRA & UCE II.1-1.0SR were admitted.)

Q. (By Ms. Hayes) Ms. Kelly, do you have a summary of your testimony that you would like to present to the Commission?

A. Yes, I do have a summary.

Q. Please proceed.

A. In Part I of this proceeding I sponsored testimony on behalf of Western Resource Advocates. I recommended to the Commission that it deny PacifiCorp's application for an ECAM as not in the public interest.

I understood the burden of proof in establishing the need for an ECAM to lie with the Company, which I did not believe it had met. And I was concerned with the effect of an ECAM on manage -- management incentives to operate efficiently.

Further, I considered it unfair to shift the risk of past planning decisions to customers, who are least able to manage the risk. However, my fundamental objection to any ECAM design, then and now, is with its effect on long-run planning and acquisition.

By treating operating expenses differently from other costs, an ECAM biases resource acquisition to those resources whose costs are recovered through the ECAM. Primarily wholesale power and natural gas resources.

This bias is contrary to the public interest because the Company's planning studies have shown that portfolios heavy in market purchases and natural gas resources are risky. Meaning that the actual cost may far exceed the forecast cost at the time a decision is made.

Significantly, at the same time that an ECAM biases resource acquisition toward natural gas resources and market purchases, it create a bias against demand side management and renewable resources.

The very resources shown through the Company's planning studies to best protect customers from the multiple risks facing the industry today, including wholesale power and natural gas costs and the cost of complying with potential regulation of CO_2

emissions.

I therefore recommended that the Commission deny PacifiCorp's application as not in the public interest.

At the conclusion of Phase I, the Commission decided that it did not have enough information regarding alternative ECAM designs and how they might address issues that were raised in Phase I to reach a final conclusion regarding the public interest aspect of an ECAM.

The Commission determined to proceed to a second phase to further explore alternative ECAM designs, or other means or methods, to address the Company's claims of difficulty in recovering its net power cost.

It also requested that the two issues identified by the Office of Consumer Services as threshold issues be further explored with all relevant areas of inquiry.

As a result of compromise among the parties, a schedule was set to first address the Office's threshold issues and then all other design issues. As I understand it, the purpose of this part of the proceeding is to seek a ruling and direction from the Commission regarding these threshold issues.

It is the position of WRA and Utah Clean Energy, whose testimony I have sponsored in this phase of the proceeding, that not only must market reliance and natural gas hedging be addressed prior to, or in conjunction with, the adoption of an ECAM before an ECAM could be found in the public interest, integrated resource planning and resource acquisition generally must be addressed.

A primary reason for singling out the wholesale market purchases and natural gas fuel cost components of net power cost in this part of the proceeding is because meeting load requirements with short-term wholesale market purchases and natural gas resources is particularly risky, as identified in PacifiCorp's integrated resource planning processes, and the Company's resource plans have included more market and natural gas resources than planning studies indicate is optimal.

If an ECAM is implemented, the actual net power costs of these resources will be immediately assigned to customers instead of being shared by the Company and its shareholders between rate cases, as is currently done.

Because integrated resource planning has not resulted in the set of resources shown to best protect customers given the expected combination of costs, risk, and uncertainty, it is unfair to require that customers assume the risk of this planning strategy without a mechanism in place to correct this in the future.

Utah customers should not assume the net power cost risk of resources that are not supported through integrated resource planning.

Therefore, WRA and UCE, UCE recommend that if the Commission decides to move forward with an ECAM, the adoption of any ECAM design hinge on the implementation of an IRP compliance mechanism to be implemented in conjunction with the adoption of an ECAM.

In order to implement the ECAM the Company must demonstrate that it has adhered to the action plan of the portfolio that best manages risk and uncertainty, as demonstrated through the integrated resource planning process using the Commission's suggested three-step approach for evaluating risk and uncertainty.

And that three-step approach has been spelled out in both of the last two IRP orders. And also in the RFP order on modeling.

Assuring that customers receive the benefits of integrated resource planning is a longstanding objective of this regulatory community and this Commission, as evidenced by its many IRP orders, RFP orders, and its December 2004 MSP order.

Before moving forward with an ECAM, we request that the Commission carefully evaluate the effect of an ECAM on long-run planning and assure the public interest is met. Our recommendation is that you take the following actions in this part of the ECAM proceeding:

First, identify market reliance and natural gas hedging as threshold issues to be addressed prior to the implementation of any ECAM design.

Two, identify market reliance and natural gas hedging as fundamented -- fundamentally integrated resource planning issues.

Three, identify resource acquisition as a threshold issue.

Four, rule that customers should not assume the net power risk through an ECAM of resources that are not supported by integrated resource planning studies without providing an ER -- IRP compliance mechanism to assure that customers receive the benefit of integrated resource planning over the long run.

And five, rule that the long-run resource acquisition biases introduced by an ECAM must be mitigated through an IRP compliance mechanism in order for any ECAM design to be considered in the public interest.

WRA and UCE are indifferent as to whether the IRP compliance mechanism is developed in this docket or in another. However, without some type of IRP compliance mechanism in place, as well as strong sharing bands, WRA and UCE maintain that no ECAM design can be, can be demonstrated to be in the public interest.

That concludes my summary.

MS. HAYES: Ms. Kelly is now available for cross examination.

CHAIRMAN BOYER: Thank you Ms. Kelly.

Mr. Monson?

MR. MONSON: Thank you.

CROSS EXAMINATION

BY MR. MONSON:

Q. Ms. Kelly --

MR. PROCTOR: Mr. Monson -- I'm sorry, may I?

MR. MONSON: Oh.

MR. PROCTOR: I'm sorry, excuse me.

Mr. Chairman, for reasons that really are important, I need to be excused. If that would be acceptable to the parties and to the Commission.

CHAIRMAN BOYER: It is. And you don't have to explain why.

MR. PROCTOR: We have no questions of Ms. Kelly.

CHAIRMAN BOYER: And you don't have to explain why.

MR. PROCTOR: Thank you.

CHAIRMAN BOYER: Thank you for your participation up to this point.

MR. PROCTOR: Thank you.

CHAIRMAN BOYER: Mr. Monson?

MR. MONSON: Thank you.

Q. (By Mr. Monson) You state that your June 16th testimony attempts to bolster the record, as requested by the Commission, regarding the need for an IRP compliance mechanism to be in place before shifting the full risk of PacifiCorp's past and future resource acquisitions to customers; is that right?

A. Yes. That was in response to Mr. Duvall's stating the issue as the effect -- can you direct me to where it is, and I can tell you what I was responding to?

Q. Yeah. It's in your surrebuttal, lines 51 to 54.

A. Okay. So it was in response to Mr. Duvall's narrowing the issue to how -- to the effect of an ECAM. And so I was introducing further information to bolster the record regarding input bias. Because as I understand it, the effect of an in -- of an ECAM promotes input bias.

Q. Okay. And you also state, at lines 55 to 57, that your testimony proposes other measures or means that the Commission can use to mitigate your primary concern with adoption of an ECAM, right?

A. Yes.

Q. And then in your surrebuttal testimony you provide additional information, as you characterize it, to develop the record; is that right?

A. Yes.

Q. Okay. And this amounts to a discussion of four articles claiming that adoption of a fuel cost adjustment mechanism creates an input bias; is that right?

A. Yes.

Q. Now, are these the same articles that you mentioned in your direct testimony filed on ECAM design on August 4th?

A. No.

Q. Now, in that testimony you didn't identify the specific articles, did you? You just said academic literature, or something to that effect?

A. Right. I was referring at that time to the articles that Mr. Paul Chernick had introduced into the record. And then your witness, Mr. McDermott I believe, had responded. And they had an exchange on that.

Q. Okay. And then you summarize your June 16th testimony; is that right?

A. Where are you now?

Q. After you finish the discussion of those articles. You summarize your --

A. Can you direct me to the page and line, please?

Q. Yeah. Well, let's see. I can if I count them up. You spent seven pages discussing those articles. So we can go to the end of those. And then you go: "Response to Mr. Duvall's critique of testimony." That's on page 10.

A. Okay.

Q. And then you summarize your testimony, right? Your June 16th testimony?

A. Yes, okay.

Q. And then you again discuss your IRP compliance mechanism; is that right?

A. Yes.
Q. Is that the same mechanism that you proposed in your direct testimony filed on August 4, 2010?
A. Yes. I, I first introduced it in my June 16th testimony. And I modified it in my August 4th testimony. And I referenced the changes in my surrebuttal testimony on August 10th.
Q. And they all deal with this IRP compliance mechanism?
A. Correct.
Q. Okay.
MR. MONSON: Commissioners, I think that we could save some time and get Ms. Kelly on her way if we could reserve cross of those areas of her testimony dealing with the IRP compliance mechanism for Phase II, Part 2, which she's directly addressing in her testimony -- direct testimony in that.
CHAIRMAN BOYER: That would be totally acceptable to us.
THE WITNESS: Acceptable to me.
MR. MONSON: Okay. Then we're done. I'm done.
CHAIRMAN BOYER: Okay. Thank you Mr. Monson.
Ms. Schmid, any questions of Ms. Kelly?
MS. SCHMID: No questions.

CHAIRMAN BOYER: Ms. Hayes? Well, that's your witness. You probably do.

Mr. Evans?

MR. EVANS: No, I have none. Thank you.

CHAIRMAN BOYER: Okay. And nothing from you, Commissioner Allen?

Commissioner Campbell.

COMMISSIONER CAMPBELL: Maybe I should reserve my questions if they deal -- if I get into the compliance issues in your August 4th testimony, let me know, and maybe I'll reserve my questions till then as well.

But you state that, you state that they need to comply with the, with the portfolio in the last IRP. In your opinion did they choose the right portfolio in the last IRP?

THE WITNESS: No. I have an attachment to my surrebuttal from Phase I that shows -- compares Portfolio 5 with Portfolio 8. And Portfolio 8 would have been the portfolio that was -- that would have been identified as what I'm calling the, I think the step-three portfolio.

So I'm making a distinction. The Commission's orders in the past two IRP have recommended approach -- an approach for evaluating risk and uncertainty that starts with looking at the range of potential futures.

Finding an optimized portfolio for each of those futures. Subjecting them to stochastic risk analysis. Which means, in this case, running 100 -- doing 100 stochastic runs with each of the portfolios to get an number of performance metrics for those portfolios.

And on that surrebuttal testimony -- I, I could pull it up if you would like -- there, there are a number of performance metrics.

The third step is then to take the portfolios that performed well in the stochastic analysis and re-subject them to the same conditions that created the original portfolios to measure the scenario risk.

In that third step, Portfolio 8 was the portfolio that was identified. So in our, in our comments to the Commission on the IRP, and in my surrebuttal attachment, and then in my testimony here we're saying that, that Portfolio 8 was the portfolio that best balanced cost and risk.

And that the portfolio that the Company chose didn't perform as well, particularly on the risk metrics. It had -- it, it was riskier.

And so, so the answer to your -- the very long answer to your short question was -- is, is no. The, the portfolio that the Company has chosen is not the portfolio that balances cost and risk.

COMMISSIONER CAMPBELL: I think I'm gonna try one more question, then maybe we'll be done today.

THE WITNESS: Okay.

COMMISSIONER CAMPBELL: Why do you think the Commission acknowledges IRPs and does not approve them?

THE WITNESS: Because the Commission does not want to micromanage the Company. Has been one reason. And also because the Commission has not wanted to get into a fully-litigated proceeding over IRP. And so IRP has been an information-sharing procedure.

But the -- but always the -- but the determination of the resource acquisition plan is the Company's. They, they determine which resources they will acquire.

And I am not challenging that on its own. What I'm suggesting is that if an ECAM is going to be put into place, which shifts the full risk of past, past planning decisions to customers so that they -- so that shareholders are no longer sharing in that risk, then the resource acquisition should reflect the Company's planning studies.

And should, in fact, be the resource acquisition strategy that balances cost and risk for customers.

CHAIRMAN BOYER: Just a couple of questions, Ms. Kelly. You've heard -- we've all heard ample testimony this morning on -- for the proposition that hedging, and front office transactions, market reliance, and so on promotes rate stability, or reduces rate volatility, if you will.

Are you, are you suggesting that another -- an alternate way to achieve those same ends is by increasing the proportion of renewable energy in the portfolio? Inasmuch as fuel costs are free?

THE WITNESS: Indirectly, that was the results of the last planning studies. The last planning studies showed that the resources that had the additional capital expenses, and the wind, wind resource, and had the DSM, reduced upper-till risks. They were less risky.

And that it was a minimal expected cost at a zero carbon level. As the carbon level went up, that resource portfolio not only lowered the upper-till risk, the riskiness, but it also lowered the expected cost, the average, over the hundred stochastic runs.

And -- but no, I, I -- what I am saying is that the resource acquisition strategy should be in alignment with the action plan that would come from the portfolio that would be identified using the Commission's three-step approach.

CHAIRMAN BOYER: Do you agree that rate stability provides value to customers?

THE WITNESS: Yes.

CHAIRMAN BOYER: And would you have any idea on how to monetize that value? How to measure that value?

THE WITNESS: Well, in terms of -- I -- my focus is on long-run planning, not on the hedging part. In terms of long-run planning, if, if the Company's resource acquisition plan is in alignment with the portfolio that best manages upper-till risks, you're gonna get greater rate stability.

CHAIRMAN BOYER: Is -- and I don't want to get into, you know, jump the gun here and start talking about design issues. But is your objection to an ECAM an objection to an ECAM in any form, or in the present form without the sharing bands you've talked about?

THE WITNESS: My, my main concern with an ECAM is on long-run planning bias. That, that an ECAM biases resource acquisition to front -- towards front office transactions in natural gas resources.

Now, if those resources weren't risky, if those resources were stable -- stably priced, well, this incentive effect of an ECAM could be in the public interest. But it's just the opposite.

My concern with an ECAM is that it incents further acquisition of the very resources that are most risky, and it shifts the risk of those resources to customers. And I have not been able to figure out how to address that through design, and so that was why I initially objected.

And during, during the last hearing I -- in response to Commissioner Campbell's question regarding putting teeth in the IRP, I started thinking about that a lot. And determined that if, in fact, the resource acquisition strategy was in line with the Company's planning studies that balance cost and risk, I wouldn't have a problem -- I would have much less of a problem with that component of an ECAM.

The fundamental flaw, for me, would be removed, and other aspects could be addressed through design. But it was -- it is this fundamental flaw of the, of the bias towards risky resources that is my objection to an ECAM.

CHAIRMAN BOYER: So asked a different way, if the benefits and costs of hedging in front office transactions, if they were included in an ECAM, were shared, that would, at least in part, mitigate your concern about the resource procurement bias, would it not?

If the, if the shareholders were --

THE WITNESS: I think share -- sharing addresses operational inefficiency. I don't think it gets at this resource acquisition bias.

CHAIRMAN BOYER: Commissioner Campbell has a follow-up question.

COMMISSIONER CAMPBELL: Since my name was used in vain.

THE WITNESS: I'm sorry.

COMMISSIONER CAMPBELL: No, I mean, can you really put teeth into a plan? I mean, how many plans have you made that you have a hundred percent followed? I mean, isn't a plan kind of directional rather than specific?

THE WITNESS: I agree with that. But there is an action -- with each, with each portfolio, if one were gonna -- one were to proceed with that actual portfolio you would need to take particular actions to implement it. And so every portfolio would have an action plan if the Company specified it.

So all I'm suggesting -- the only change that I'm anticipating to IRP would be that when -- that the Company would identify the Step 3 portfolio and create an action plan for it. That's all it would have to do.

And then, if it had taken the actions in -- that were in that action plan in the two previous years, it would be considered in compliance. Now, I understand that -- we understand that things are dynamic, and fluid, and always changing.

And there would be every opportunity to, if there was a, you know, a substantial change in circumstances, to come in and make a filing to change things. Just like was done with -- in the recent situation.

So I, I'm not saying lock in no matter what. I'm, I'm, I think, wanting the strategic business plan to better align with the IRP modeling results. That's, that's what I'm recommending.

CHAIRMAN BOYER: Ms. Hayes, any redirect for Ms. Kelly?

MS. HAYES: No, thank you.

CHAIRMAN BOYER: Okay. Well, thank you Ms. Kelly, you may be excused --

THE WITNESS: Thank you.

CHAIRMAN BOYER: -- to attend your birthday festivities.

We very much appreciate everyone's participation. We especially appreciate the Committee for raising these issues earlier and giving us an opportunity to discuss these issues and how they interact with the further discussion of ECAM design.

We don't envision issuing an order on this -- Part 1 of this Phase II at this point in time. If, if after we sleep on it and think about it and need to get further guidance for the next proceeding in Part 2 of Phase II, we will certainly let the parties know by scheduling order or otherwise.

Is there anything further we need to discuss?

MR. MONSON: I just want to note on the record that we did pass out a complete copy of the -- of our cross exhibit --

CHAIRMAN BOYER: Yes. And let's make a note that the complete copy of the -- what was it? I can't remember we called that. The Pace report has been admitted into evidence then. There was an objection to it, but with the offer of the entire document I believe it's in.

And I guess I should mention, Ms. Hogle offered to provide additional testimony on

Commissioner Campbell's questions earlier, and we won't require that or accept that testimony at this time. But we appreciate the offer.

So thank you all for your participation. And safe travels. That will conclude this hearing.

(The hearing was concluded at 4:31 p.m.)

C E R T I F I C A T E

STATE OF UTAH)
) ss.
COUNTY OF SALT LAKE)

This is to certify that the foregoing proceedings were taken before me, KELLY L. WILBURN, a Certified Shorthand Reporter and Registered Professional Reporter in and for the State of Utah.

That the proceedings were reported by me in stenotype and thereafter caused by me to be transcribed into typewriting. And that a full, true, and correct transcription of said proceedings so taken and transcribed is set forth in the foregoing pages, numbered 1 through 266, inclusive.

I further certify that I am not of kin or otherwise associated with any of the parties to said cause of action, and that I am not interested in the event thereof.

SIGNED ON THIS **24th** DAY OF **August**, **2010**.

Kelly L. Wilburn, CSR, RPR
Utah CSR No. 109582-7801

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