Rocky Mountain Power
Docket No. 09-035-15
Witness: Gregory N. Duvall

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF UTAH

ROCKY MOUNTAIN POWER

Direct Testimony of Gregory N. Duvall

March 2009

Q. Please state your name, business address and present position with Rocky Mountain Power (the "Company"), a division of PacifiCorp.

A. My name is Gregory N. Duvall, my business address is 825 NE Multnomah St., Suite 600, Portland, Oregon 97232, and my present title is Director, Long Range Planning and Net Power Costs.

Qualifications

Q. Briefly describe your educational and professional background.

A. I received a degree in Mathematics from University of Washington in 1976 and a Master of Business Administration degree from University of Portland in 1979. I was first employed by Pacific Power in 1976 and have held various positions in resource and transmission planning, regulation, resource acquisitions and trading. From 1997 through 2000 I lived in Australia where I managed the Energy Trading Department for Powercor, a PacifiCorp subsidiary at that time. After returning to Portland, I was involved in direct access issues in Oregon, was responsible for directing the analytical effort for the Multi-State Process ("MSP"), and currently direct the work of the integrated resource planning group, the load forecasting group, the market assessment group, and the net power cost group in the Company.

Purpose of Testimony

Q. What is the purpose of your testimony?

A. My testimony describes the Company's proposed Energy Cost Adjustment Mechanism ("ECAM"), including the need for this kind of a mechanism, costs that would be recovered by the mechanism, and how the proposed mechanism

would be administered.

Energy Cost Adjustment Mechanism

Q. Please briefly describe the proposed Energy Cost Adjustment Mechanism.

A. The proposed ECAM is a rate mechanism designed to allow the Company to collect or credit the differences between the actual net power costs ("NPC") incurred to serve customers in Utah and the amount collected from customers in Utah through rates set in general rate cases. On a monthly basis, the Company will compare the actual system net power costs ("Actual NPC") to the net power costs embedded in rates from the most recent general rate case ("Base NPC"), and defer the differences in a balancing account. An ECAM rate will be calculated annually to collect from or credit to customers the accumulated balance over the subsequent year.

Q. Why is the Company proposing an ECAM at this time?

A. The Company's NPC represent a large proportion of the Company's total revenue requirement. They are subject to a high degree of volatility largely outside of the Company's control. Some of the factors causing this volatility include changes in retail load, hydro conditions, wind generation, market prices, third party wheeling expenses, natural gas and coal fuel expenses. Because the Company depends on both the electricity and natural gas markets to balance its system and meet the load requirement, fluctuations in the markets invariably impact the Company's NPC. Coal expenses, which were previously relatively stable, are affected by changes in commodity costs due to contract re-openers, and even the captive mine costs may change significantly in today's environment due to the rapid changes in

the costs of mining equipment and supplies. An ECAM would provide safeguards to customers and give the Company an opportunity to recover the NPC that are prudently incurred to serve those customers.

Q. Please describe the volatility of the wholesale power and natural gas markets?

A. RMP Exhibit___(GND-1) shows the historic natural gas prices at Henry Hub and Opal, along with the wholesale electricity prices for Mid-Columbia and Palo Verde separated by heavy and light load hours from January 1, 2005 through February 10, 2009. Over this period, gas prices have ranged from below $1/mmbtu to over $15/mmbtu. Over the last 12 months, gas prices at Henry Hub have gone from about $5/mmbtu to $13/mmbtu and back to less than $5/mmbtu, while Opal has gone from less than $1/mmbtu to over $10/mmbtu and back to about $3/mmbtu. Over the same time, electricity has varied widely from less than zero during light load hours to about $150/MWh and back down.

Q. Does the Company expect the volatility of NPC will continue?

A. Yes, it certainly could, given the current economic conditions and uncertainties regarding environmental legislation. The volatility in fuel and wholesale electric prices is compounded by the variability in the Company's load – also caused by economic conditions. Small fluctuations in load, combined with fuel and wholesale power volatility, can lead to significant changes in NPC. In addition, the composition of the Company's resource portfolio is shifting to wind and natural gas fired generation, both of which increase the volatility of the NPC because of the high volatility of wholesale natural gas and power market prices

and the intermittent nature of wind resources.

Q. Why are general rate cases no longer adequate to capture NPC?

A. Although the Company's general rate cases in Utah utilize forecast test period under the Commission's rules and requirements, static test period data cannot accurately reflect the volatility in NPC that we are currently experiencing.

For example, in Docket 08-035-38, I explained in my direct testimony that the Company's system NPC at that time were increasing sharply at a rate of $40 to $50 million every six months. The Company had not experienced rising NPC of the magnitude since the Western energy crisis. And since then, the market prices have plummeted due to significant changes in the world-wide economies. The reduction in NPC is equally unexpected. Referring to RMP Exhibit____(GND-1), it can be seen that the rising trend continued through July 2008. Then, in August 2008, natural gas and wholesale power prices began a precipitous drop. If the Company had a rate case with a test period ending June 30, 2008, the wholesale power and natural gas costs in that period would not at all be representative of current costs – to the detriment of customers.

During a period of NPC volatility, establishing a fixed level of NPC in a rate case virtually ensures that customers will either over pay or under pay the cost of the energy they are using.

Q. Is the Company proposing a symmetrical mechanism for NPC recovery?

A. Yes. The Company wants to recover its prudent and reasonable NPC – nothing more or less. Thus, we are proposing an ECAM mechanism that is applied symmetrically to safeguard customers when the NPC that the Company actually

incurs are lower.

Q. Does the ECAM shift the risk of NPC increases away from the Company and onto the customer?

A. No. Based on the historic data presented in RMP Exhibit___(GND-1), a symmetrical tracker is as much a safeguard for customers as it is for the Company. For example, a rate case where NPC are based on $100-150/MWh prices for electricity would not serve customers well if actual prices turned out to be less than $80/MWh. Or, if actual hydro generation were 500,000 megawatt-hours greater than the normalized amount included in rates and market prices were $100/MWh, NPCs would be overstated by $50 million total Company.

The proposed ECAM will recover from customers only actual NPC and will pass through to customers any Actual NPC reductions. While this creates symmetry, a desirable feature of an adjustment mechanism, it does not shift from the Company to customers the risks of prudent acquisition and reasonable pricing. The Company retains that risk. The Commission, Commission staff and parties will have the opportunity to assess the prudence and reasonableness of the NPC in the annual reconciliation filing on December 15 of each year and importantly as part of any general rate cases.

The critical focus here, however, is not about risk assignment, but one of fairness and balanced outcomes. The proposed ECAM will facilitate the long held regulatory principle of customers paying the prudently incurred cost of the service they receive.

Q. Does the Company have less of an incentive to make prudent resource acquisitions if an ECAM is in place?

A. No. The Company has expressed in numerous settings its goal to minimize resource costs by acquiring existing resources such as the Chehalis plant, building new plants or making purchases in the open market. We believe that properly priced plant additions over time will be less volatile for customers than open market power purchases regardless of whether they are recovered through an ECAM or other mechanism. Customers obtain immediate benefit through an ECAM because net power cost savings will flow through immediately. In addition, Senate Bill 75, which just passed in the 2009 General Session of the Utah legislature (the "2009 Session"), will allow the Company to recover the capital costs of a major plant addition through a single item rate case. The approval of both of these mechanisms will provide the proper matching of both the fixed and variable cost and benefits of any new generation resource with the prices customers pay.

Q. What types of costs would be included in the ECAM?

A. The ECAM rate will be calculated using all components of NPC as traditionally defined in the Company's general rate cases and modeled by the Company's production dispatch model GRID. Specifically, Base NPC and Actual NPC will include amounts typically booked to the following FERC accounts:

Account 447 – Sales for resale, excluding on-system wholesale sales and other revenues that are not modeled in GRID

Account 501 – Fuel, steam generation; excluding fuel handling, start up fuel/gas[1], diesel fuel, residual disposal and other costs that

[1] Start up fuel is accounted for separate from the primary fuel for steam power generation plants. Start up

are not modeled in GRID
Account 503 – Steam from other sources
Account 547 – Fuel, other generation
Account 555 – Purchased power, excluding BPA residential exchange credit pass-through if applicable
Account 565 – Transmission of electricity by others

The mechanism addresses power cost expenses and does not include any costs associated with fixed cost recovery (i.e., capital investment in rate base). However, as previously noted, Senate Bill 75 allows utilities to include in rates the revenue requirement of individual major plant additions. This will assure a better match between new resource fixed costs and net variable power costs. If NPC recovery is updated regularly but other fixed costs are not, a mismatch will be created between the variable and fixed costs associated with new resources. This mismatch is particularly significant for renewable resources since they have near-zero variable costs, are added with greater frequency than traditional generation investments, and are depreciated more rapidly than traditional generation investments.

Q. How would Base NPC be calculated?

A. Base NPC are computed using total company NPC from the most recent general rate case. Initially, Base NPC would be set based on the Company's next general rate case, anticipated to be filed later this year, including any adjustments ultimately approved by the Commission in that case. The total Company monthly NPC are divided by the monthly normalized MWh load used to determine the NPC to express the costs on a per unit basis.

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costs are not accounted for separately for natural gas plants, and therefore all fuel for natural gas plants is included in the determination of both Base NPC and Actual NPC.

Q. Do Actual NPC include adjustments prior to the comparison with Base NPC?

A. Yes. Adjustments will be made to NPC as booked to be consistent with the Company's production dispatch model, to remove prior period accounting entries, and to include applicable Commission-adopted adjustments reflected in the most recent general rate case. Actual NPC will not be adjusted for hydro conditions and forced outages because they give rise to the fluctuations in NPC that this mechanism is designed to capture. Actual NPC will be subject to review by the Commission and other parties annually when the Company files its applications for recovery of the deferred NPC.

Q. Please explain the balancing account and the calculation of the ECAM rate.

A. The balancing account and ECAM rate serve as a true-up mechanism to recover or credit the differences between Base NPC and Actual NPC. On a monthly basis, the Company will compare Actual NPC to Base NPC. Any differences in the system per-unit cost will be multiplied by actual Utah MWh load in that month and the product will be deferred in the balancing account. The monthly under- or -over-recovery will accumulate in the balancing account and earn interest at the Company's most recently approved rate of return on rate base in Utah.

On an annual basis the cumulative deferred balance in the balancing account will be converted to the Schedule 94 ECAM rate expressed on a cents per kilowatt-hour basis for projected Utah sales for the twelve months of the ECAM recovery period. An example of the monthly deferral calculation is provided as

RMP Exhibit____(GND-2).

Q. When will the Company reconcile the ECAM costs and recoveries and update the ECAM factors?

A. The Company proposes to file annual ECAM reconciliations and updated factors on December 15 each year with a new ECAM rate effective February 15. The first application addressing a deferred amount in the balancing account would be made December 15, 2010.

Q. Does this conclude your testimony?

A. Yes.