BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

In the Matter of the Application of Rocky Mountain Power for Authority To Increase its Retail Electric Utility Service Rates in Utah and for Approval of Its Proposed Electric Service Schedules and Electric Service Regulations.	))))))))	**Docket No. 09-035-23** **DPU Exhibit No. 3.0SR**

Surrebuttal Testimony of

Michael J. McGarry, Sr.

REVENUE REQUIREMENT
AND
NET POWER COSTS RELATED TO HEDGING

For the Division of Public Utilities

Department of Commerce

State of Utah

November 30, 2009

Surrebuttal Testimony of Michael J. McGarry, Sr.

1. INTRODUCTION

Q. Please state your name and business address.

A. My name is Michael J. McGarry, Sr. My business address is 2131 Woodruff Road, Suite 2100, PMB 309 Greenville, SC 29607.

Q. Are you the same Michael J. McGarry Sr. who submitted direct testimony in this proceeding on October 8, 2009, and supplemental direct testimony on October 29, 2009?

A. I am.

Q. Are you once again appearing on behalf of the Utah Division of Public Utilities (Division) in these proceedings?

A. Yes.

2. PURPOSE

Q. What is the purpose of your testimony that you are now filing?

A. This surrebuttal testimony is to address the rebuttal testimonies of Rocky Mountain Power (RMP or Company) Witnesses Mr. Steven R. McDougal, Mr. Robert Lasich, and Mr. Erich Wilson.

3. ERRATA – CORRECTION TO EXHIBIT 3.5

Q. What errata are you submitting?

A. Company Witness Mr. McDougal correctly pointed out that I had double counted the inflationary escalation factor in the development of the Divisions' position for the Pension Administration adjustment in DPU Exhibit 3.5.2 Line 6. In addition, I noted that a formula had not carried over in the derivation of the Column's marked Utility Labor and Utah allocated. I have shown the correct calculations on the revised exhibit.

Q. What was the effect of this revision?

A. As shown on the Exhibit 3.5.2 (Revised), this change reduces my proposed adjustment slightly by $10,569 on a total Company basis before the combined effects of the jurisdictional and FERC allocations made as a result of including this adjustment in the Jurisdictional Allocation Model (JAM). Division Witnesses Dr. Brill and Mr. Croft provide the final effect of this change. I have revised the summary Exhibit 3.5.1 to reflect this change as well. I address Mr. McDougal's criticism of my proposed adjustment later in this surrebuttal testimony.

4. CHANGES IN DIVISION POSITION

Q. Are there any changes to the Division's position that you would like to make?

A. Yes.

Q. Please explain.

A. After reviewing Witness Mr. McDougal's rebuttal testimony at lines 692 to 700 concerning my adjustment to the 401k administration expenses in Exhibit 3.5.1, I am withdrawing that portion of my testimony at lines 453-455 which states, "The resulting adjustment would reduce 401(k) administration costs by $470,000 on a total Company basis and $135,858 in the Utah jurisdiction (DPU Exhibit 3.5)." As shown on Exhibit 3.5.2 (Revised) line 13, the Division's position is effectively the Company's budget position. Both of us had removed the effect of the $470,000 refund in 2007 in the test year.

Q. What is the next issue that you wish to discuss?

A. Property Insurance.

Q. Please explain.

A. At lines 783 to 789 of his rebuttal testimony, Witness Mr. McDougal rejects my proposed adjustment to set property insurance at $9,770,454. He states that the Company's proposed level already includes a normalized level of expense which reflects the low claim bonus the Company received during the base year.

Q. Do you agree with Mr. McDougal's characterization of your adjustment?

A. No. However, my adjustment as proposed in my direct testimony and shown in Exhibit DPU 3.6.1 and detailed in Exhibit 3.6.2 should be withdrawn.

Q. Please explain.

A. My adjustment was proposed based on information gathered in discovery and the expectation that the Company would propose a revision to its property insurance. The Company has not done that despite indicating the following:

Company's response to OCS 5.4

> "Actual estimated premium is now $10,629,385 because of new information received regarding low claims bonus:
>
> The insurance companies providing the continuity credits and low-claims bonuses have indicated to MidAmerican Energy Holdings Company that the distributions received in the past will not likely occur in the next couple of years. These are discretionary distributions by the insurance companies. Losses and reductions in liquidity of the insurance industry in recent months have resulted in these companies exercising due-diligence of any surplus capital by suspending the credit distributions for the near term."
>
> See Attachment OCS 5.4.

The attachment to OCS 5.4 shows the following:

TOTAL PROPERTY PREMIUM				**9,779,385**
July 2009 Update Low Claims Bonus 10-1-08 to 10-1-09	0 12/09	Correction	850,000	
			230,000	10,399,385
Revised estimate				**10,629,385**

As such, my proposed adjustment was in anticipation of the Company revising its costs in the rate case as Mr. McDougal has done in many other adjustments in his rebuttal (see page 3 of his rebuttal). I reflected this response to OCS 5.4 expecting an adjustment as clearly shown on my Exhibit 3.6.2. Since the Company has not proposed this adjustment, Mr. McDougal's criticisms of my adjustment, which I do not ascribe to, are moot. I am recommending the Commission adopt the Company's normalized level as originally filed in the case.

Q. Do you have any comments concerning Mr. McDougal's criticism of your adjustment associated with CWIP write-offs?

A. Yes. Based on the information contained in Mr. McDougal's rebuttal, I am modifying that adjustment included in my direct as Exhibit 3.8. Mr. McDougal has not challenged my premise that the Company, not the ratepayer should be responsible for the costs of projects written off that are entirely within the Company's span of control. However, the Company has provided sufficient explanation for several of the projects that were written off that they were not entirely within the span of Company control. Those that remain leave an adjustment of $174,389 (or $71,727 on a Utah allocated basis). Therefore, I have revised Exhibit DPU 3.8 to rename it to Exhibit 3.8.1SR and to show the change in my position. In addition, I have added a supporting schedule, Exhibit 3.8.2SR to show the derivation of the amount included in Exhibit 3.8.1SR,

5. RESPONSE TO COMPANY'S REBUTTAL

Q. Do you have any comments concerning the Company's criticisms of any of your other proposed adjustments?

A. Yes, I do.

Q. Please explain.

A. At lines 236 to 251, Company Witness Mr. McDougal rejects my proposed adjustment to the Company's pension administration expenses (Exhibit DPU 3.5.1). He argues that my proposed adjustment of $359,395 results in a pension administration expense that is less than any of the three previous years and less than what the Company had spent year to date in 2009. He states that his method of annualizing the 2009 YTD costs is more reflective of the expenses ($685,230)[1] the Company expects to incur in the test year.

Q. Do you agree?

A. No. The Company has offered no additional evidence that its costs are going to rise significantly over those that it incurred in the base year (2008) to refute my argument. As I stated in my direct testimony, the Company's argument that pension administration expense will increase due to collective bargaining negotiations requiring additional actuarial work is no longer relevant. The union agreements have been negotiated in 2008/2009 and there is no reason to expect significant increases in 2010. Absent other compelling factors, escalating base period costs with the appropriate inflation factor should be the acceptable method

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[1] Rebuttal Testimony of Steven R. McDougal, page 11, at lines 229-231.

for determining costs in the test year. In this case, I cannot find any reason to modify that method.

Q. Is there any other way to determine if the Company's proposed level is excessive?

A. Yes. While I would prefer to use 60 months of data for an average, the 48-month average of the data provided in Mr. McDougal's rebuttal at line 245 shows that the average cost for the four years is $554,209, which is $131,021, or 19.1%, less than what the Company is proposing in its revised adjustment 11.9. While I believe that escalating the base year is more appropriate, the Commission could consider using an average method as it has done with other costs that have widely varying year to year expenditures.

Q. What is the next issue you wish to address?

A. Injuries and Damages. Mr. McDougal challenges the way in which I developed my proposed adjustment in Exhibit DPU 3.7.1. He claims that I mistakenly recommend adjusting the Company's base year by adding back the base year insurance cash received in an attempt to convert the Company's base year accrual amount to a cash figure.[2] Mr. McDougal states that the Company's base year is developed using a three-year average of net cash outlays. He also criticizes my use of a 60-month average[3] to arrive at a normalized test year balance.

I will address each point in order. With respect to converting the Company's adjustment to cash, what is important to consider is the way that the JAM accumulates the adjustments. It is my understanding that the JAM takes the

[2] Rebuttal testimony of Steven R. McDougal at 37, lines 799-801.
[3] As corrected in my supplement testimony filed on October 29, 2009.

proposed adjustment, not the proposed level of expenses, and runs the adjustment through the "revised protocol" to arrive at the Company's Utah distribution revenue requirement. That being the case, the Company's adjustment of $1,064,820 (as I have depicted it) would run through account 925 in the JAM. This adjustment would have the effect of raising the Company's revenue requirement to reflect the 3-year average cash balance for injuries and damages. For ease of reference, Exhibit 3.6.2 is shown below.

Rocky Mountain Power
Utah General Rate Case
Injuries and Damages

Docket No. 09-035-23
DPU Exhibit 3.7.2 (revised)
Michael J. McGarry, Sr.
filed: 10/8/2009
Errata 10/29/2009

Line #	Description	Company Method	Response DPU 22.4	Division Adjustment	
	Period:				
1	1/04-12/04		$ 6,829,214	2,845,506	5 Month
2	1/05-12/05		4,338,081	4,338,081	
3	1/06-12/06	2,343,330	2,343,330	2,343,330	
4	1/07-12/07	7,360,133	7,360,133	7,360,133	
5	1/08-12/08	3,257,715	3,257,715	3,257,715	
6	1/09-7/09		393,167	393,167	7 Months
7		12,961,178	24,521,640	20,537,932	
8	3 Year Average	$ 4,320,393			
9	60 Month Average			[redacted]	Original formula had "67", s/b 60
10	Base Year Expense	$ 8,500,333		$ 8,500,333	
11	Less Insurance Receivable	(5,340,408)		(5,340,408)	
12		3,159,925		3,159,925	
13	Add Cash Received 2008		2,795,245	2,795,245	
14		$ 3,159,925		5,955,170	
15	Escalation %	3.03%		3.03%	
16	Escalation Applied	95,648		180,257	
17	June 2010 Escalated Balance	$ 3,255,573		$ 6,135,427	
18					
19	3 Year Average from Above	$ 4,320,393			
20	60 Month Average from Above			$ 4,107,586	
21	Regulatory Adjustment	$ 1,064,820	$ (3,092,661)	$ (2,027,841)	
	as filed		$ (3,521,812)		
	Change		$ 429,151		

Line 21 clearly shows the development of the Company proposal as included in Company's Exhibit SRM-2 page 4.17. The problem with the Company's proposed adjustment is that it is based on an amount that is NOT on a cash basis. Starting at line 10, the Company begins with the base year expense of $8,500,333 and then subtracts its receivables of $5,340,408, arriving at a base number of $3,159,925. However, the Company mistakenly excluded cash received during 2008 ($2,795,245) which, when added back, would more accurately reflect the true cash level for the base year. By not adding back the cash received in 2008 results, the Company's proposed adjustment in the JAM is overstated.

With respect to the use of a 60-month average, I stand by my argument presented in my direct testimony (and as corrected in my supplemental) for the Commission's consideration. I demonstrated that the Company's expenses have varied significantly over the last five years and that extending the use of the averaging for 60 months is appropriate in this case. For clarity, the Division's proposed adjustment to the Company's proposed level of injuries and damages is $212,807 on a total company basis or $87,921 on a Utah allocated basis. This total company amount is derived from the difference between the Company's position as shown on line 19 ($4,230,393) and the Division's proposed level on line 20 ($4,107,586) with the Utah allocated amount reflecting the approximately 41% allocation for Utah customers. The amounts reflected in my Exhibit 3.7.1 are the change in the proposed regulatory adjustments. Deciphering the intent of the exhibit is made more complicated by the fact that the Company and my starting base period positions are different. Simplistically, the Division's proposed adjustment can easily be arrived at as the difference between the Company's position, a 3 year average cash basis, and my proposed position of a 60 month cash basis average as shown at lines 8 and 9 of Exhibit 3.7.2 (errata), respectively or $212,807 ($4,320,393 minus $4,107,586).

Q. Do you have any comments concerning Mr. Lasich's criticisms of your coal inventory adjustment?

A. Yes.

Q. Please explain.

A. Company Witness Mr. Lasich places a significant amount of emphasis on what the Company purports to be its formal policy statement concerning its fuel stock. As I mentioned in my direct testimony, this document should be viewed very loosely as an official policy.[4] Witness Mr. Lasich claims in his rebuttal testimony that this policy was developed over 15 years ago and established long-range targets for the Company's coal plants. He further states that the policy is "reviewed and updated periodically to incorporate factors such as potential supply interruptions, coal quality, market conditions, etc. The last update was prepared earlier this summer…"[5] However, this "preliminary draft" shows no approving signature or even a date when it was first issued. Considering that the Company has owned coal generation for decades, as Witness Mr. Lasich acknowledges, one would expect this policy to have been a long-standing document with many versions and updates as the dynamics and fuel stock needs of the Company's coal generation fleet changed. The document contained in response to DPU 26.4 shows no record of that evolution. Further, the document simply states the broad target levels. There is no requirement, procedure, or protocol for updating and/or approving the Company's strategy; nor is there any analytical/economic benefit assessment of the cost of the strategy. Prudent management would require some

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[4] Direct Testimony of Michael J. McGarry, Sr. DPU Exhibit 3.0 at page 13, lines 240-244.

[5] Rebuttal testimony of A. Robert Lasich – Confidential at page 2, lines 35-39.

level of analytics to determine the dollar values and benefits associated with various levels of inventory especially when a significant change may take place, such as the one associated with Arch Electric Lake settlement. To further explore this issue of the reasonableness of the Company's overall strategy, I asked the Company to provide copies of the former policies and any analysis or studies that quantify the costs and benefits that the Company has pursued for its coal plant inventory.

Q. Did you receive any additional information from the Company?

A. Yes. The company provided responses to the Division's data request 65.1 and 65.2. The attachments to both responses are considered confidential.

Q. What is the impact of the Company's responses to these data requests DPU 65.1 and DPU 65.2 on your direct, supplemental or this rebuttal testimony?

A. The information provided essential re-affirms my position in this case. For example, in DPU 65.1, we requested that the company provide the coal inventory policies in effect during 2006, 2007 and 2008. The company provided a single 24 page confidential document which includes a cover memo and then a document titled: "Crisis Management Plan". My initial review of this document shows that it is certainly the foundation of coal stock pile strategy. However, it was first drafted in [begin confidential] [redacted] [end confidential].[6] For a policy that was in place for decades, it is troublesome that the 1st version of this document is so contemporary. In addition, the target stock pile levels identified in the plan are even lower than the levels that I have adjusted to in my direct testimony. On page

[6] See Surrebuttal Exhibit DPU 3.9SR – RMP response to DPU 65.1 Attachment (Confidential) page 9 of 24

7 of the attachment to DPU 65.1 (Surrebuttal Exhibit DPU (3.9SR)), it shows that the Company's target stock pile levels were [begin confidential] [redacted] [end confidential] which is substantially lower than the [begin confidential] [redacted] [end confidential] I proposed in my direct testimony.

Q. Do you have any comments regarding Mr. Lasich's discussion regarding the Arch Mine settlement?

A. I do. Mr. Lasich gives a description of the Arch Electric Lake settlement and the agreement that was reached for the Company to procure the significant amount of additional tonnage of coal from the Skyline and Dugout Coal Mines. He then states that the Company's customers can expect the value of the benefit to be approximately $21 million based on what he purports to be current market conditions.[7] He bases this conclusion on what he portrays as the current market price of Utah coal at $46 per ton.[8] Based on publically available information, I have to question Mr. Lasich's development of the benefit in fuel savings to customers. First, he has not included the impact of the carrying costs of the increase in the fuel stock in his determination of the $21 million. In addition, I believe that he is overstating the true cost of Utah coal and is inconsistent with other information contained in this filing. At $46 per ton and assuming 11,000 mmbtu per ton coal, the price per mmbtu for this coal is approximately $2.09 per mmbtu. However, in the Department of Energy/Energy Information Administration (DOE/EIA) March 2009 mine mouth coal price history and forecast, it shows that "west" coal which would include Utah is currently $.85 per

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[7] Rebuttal testimony of A. Robert Lasich, page 5, lines 94-95.
[8] Rebuttal testimony of A. Robert Lasich, page 5, lines 93.

mmbtu or only 40% of Mr. Lasich's purported price of the coal at $2.09 per mmbtu. Even further, Mr. Lasich claims that prices are increasing. The DOE/EIA report shows an increase of **<u>only $.03 per mmbtu or 4% between now and 2020.</u>** I have included this EIA report as Surrebuttal Exhibit DPU (3.10SR). As such, I question the veracity of Mr. Lasich's benefit analysis. Mr. Lasich's then continues with a discussion of the factors which **<u>may</u>** lead to a supply disruption.[9]

Q. Do you agree with Mr. Lasich's assessment of the possibility of a major supply disruption?

A. No. Mr. Lasich's portrayal is somewhat shocking as it appears to say that the coal from its current sources is likely to vanish after the next five years. However, my review of publically available information makes no such forecast. Further, if the market saw the potential for a major supply disruption, future prices would reflect those events.

Q. Do you have any comments concerning Mr. Lasich's portrayal of the errors in your calculation of your proposed coal inventory adjustment?

A. Yes. I disagree with Mr. Lasich's criticism of the use of 13-month average versus using beginning and ending month averages at lines 138 to 141. The accepted practice is to use a 13-month rolling average which accommodates and properly reflects the changes in the value of the fuel stocks during the course of the review period.

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[9] Rebuttal Testimony of A. Robert Lasich at page 6, lines 120-133.

Mr. Lasich's next criticism was that I used incorrect figures for the consumed tonnage at the Hunter Plant. As noted in my direct testimony, my information was based on publically reported plant information (i.e., FERC Form 1). I have included that source document as Surrebuttal Exhibit DPU (3.11SR) which is marked "privileged". Line 38 of pages 402 through 403.3 of the FERC Form 1 as submitted by the Company clearly shows "Quantity of (Units) Fuel Burned". This was the source of my information. Nowhere on this document does it show that this amount excludes the joint owners' amount as alleged by Mr. Lasich.

Therefore, I stand by my calculations and source information. Finally, with respect to the high ash coal located at the prep plant (Lasich rebuttal at page 7 lines 152-154), no where in his rebuttal does Mr. Lasich state that the Company is not requesting rate base treatment of this segregated pile of high ash coal. In fact, Mr. Lasich states "this coal will be utilized in future blending…." and suggests its value as a means of optimizing burn temperatures.[10] Until the Company can demonstrate that these 334,309 tons of high ash coal are not in the rate base, my calculations properly include them.

Q. How do you respond to Company Witness Mr. Wilson's Rebuttal?

A. At lines 124-142 of his rebuttal, Company Witness Mr. Wilson rejects my adjustment to remove SERP benefits from the Company's requested increase. He states that both Office of Consumer Services' Witness Ms. Donna Ramas and I are mistaken that these expenses are excessive and unnecessary. Company

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[10] Rebuttal testimony of A. Robert Lasich at page 7, lines 158 to 159.

Witness Mr. Wilson has not provided any evidence that these discretionary expenses are necessary for the provision of utility service and thus directly related to ratepayers and customers. The Company's shareholders are the first in line to benefit from attracting high quality executives. Mr. Wilson has not refuted this point. In addition, Mr. Wilson does not address OCS Witness Ms. Ramas' point at lines 1565 to 1570 of her direct testimony that PacifiCorp has been denied SERP expense in another of its jurisdictions (Oregon). Further, the District of Columbia Public Service Commission does not allow SERP expenses in rates for customers of Potomac Electric Power Company. Accordingly, SERP expenses should be borne by shareholders.

Q. DOES THIS CONCLUDE YOUR SUPPLEMENTAL TESTIMONY?

A. Yes.