

**BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH**

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<b>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</b>	)	
	)	
	)	<b><u>Docket No. 09-035-23</u></b>
	)	
	)	<b><u>DPU Exhibit No. 2.0</u></b>
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**Pre-Filed Direct Testimony of**

**Thomas C. Brill, Ph.D.**

**DIVISION POSITION AND RECOMMENDATIONS**

**For the Division of Public Utilities**

**Department of Commerce**

**State of Utah**

**October 8, 2009**

1 **Direct Testimony of Thomas C. Brill, Ph.D.**

2 **I. INTRODUCTION**

3 **Q. Please state your name and occupation.**

4 A. My name is Dr. Thomas C. Brill. I am employed by the Division of Public Utilities  
5 (Division or DPU) of the Utah Department of Commerce as a Technical Consultant.  
6

7 **Q. What is your business address?**

8 A. Heber M. Wells Office Building, 160 East 300 South, Salt Lake City, Utah, 84114.  
9

10 **Q. On whose behalf are you testifying?**

11 A. The Division.  
12

13 **Q. Do you have any exhibits that you are filing that accompany your testimony?**

14 A. Yes. My resume is attached as DPU Exhibit 2.1. DPU Exhibit 2.2 summarizes the  
15 Division's adjustments. DPU Exhibits 2.3 and 2.4 provide exhibits of responses to data  
16 requests on the budget adjustment issue. DPU Exhibits 2.5 presents the Jurisdictional  
17 Allocation Model (JAM), while DPU Exhibits 2.6 through 2.8 provide the JAM Rate  
18 Base Template, the JAM Depreciation Template, and the JAM Retirement Template.  
19

20 **Q. Please outline the projects you have worked on since coming to the Division.**

21 A. I joined the Division in June 2005. I managed the Division's team that investigated  
22 PacifiCorp's (Company or PacifiCorp's dba Rocky Mountain Power) general rate case

23 applications in 2006, 2007, and 2008 (Docket Nos. 06-035-21, 07-035-93, and 08-035-  
24 38). Since 2007, I have coordinated the Division's participation in the Company's  
25 Requests for Proposals (RFP) in Docket Nos. 05-035-47, 07-035-94, and 08-035-95. I  
26 am managing the rate case team for the Division in this docket.

27

28 **Q. Have you previously testified before the Commission?**

29 A. Yes. I provided the Division Summary and Policy Recommendations Testimony in  
30 Docket No. 07-035-93 on April 7, 2008 in the Company's 2007 general rate case and in  
31 Docket No. 08-035-38 on February 12, 2009 in the Company's 2008 general rate case. I  
32 also provided the Stipulation Settlement Testimony in Docket No. 06-035-21 on August  
33 17, 2006 in the Company's 2006 general rate case.

34

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

36 A. My testimony introduces the Division's witnesses who testify in this phase of the docket,  
37 as well as a Division witness who testified in an earlier phase of the docket. I will  
38 present the Division's overall revenue requirement recommendation, along with a brief  
39 explanation of the adjustments recommended by each witness. In addition, I present the  
40 Division's recommendations regarding specific policy considerations.

41

42 **Q. What is the Division's recommendation for revenue requirement?**

43 A. The Division recommendation for revenue requirement is \$8.5 million on a Utah-  
44 allocated basis. Beginning with the Company's filing of \$66.9 million on June 23, 2009,

45 the Division's first adjustment adopts the DSM Stipulation from Docket No. 09-035-T14,  
46 a SMUD increase of \$2.0 million. The Division then made a total of \$58.4 million in  
47 adjustments to arrive at a revenue requirement recommendation of \$8.5 million. The  
48 Division adjustments were a \$22.2 return on equity (ROE) adjustment, a total of \$16.4  
49 million in net power cost adjustments, and a total of \$19.9 million in various auditing  
50 adjustments. DPU Exhibit 2.2 summarizes each of the Division adjustments. These  
51 adjustments are discussed in detail in testimony provided by separate Division witnesses.

52

## 53 II. BACKGROUND AND OVERVIEW

54 **Q. Will you briefly review the background and factual framework surrounding this**  
55 **docket?**

56 A. Yes. On April 16, 2009 Rocky Mountain Power filed a Notice of Intent to File General  
57 Rate Case and Request for Approval of the Test Period. In this Notice, the Company  
58 proposed to use a 12-month ending December 31, 2010 forecasted test period and  
59 requested Utah Public Service Commission (Commission) approval of the proposed test  
60 period. The Company also filed summary support and justification for this test period.  
61 On May 14, 2009 a Notice of Test Period Stipulation was filed with the Commission by  
62 various parties. The Stipulation, among other matters, identified a 12-month ending June  
63 30, 2010 future test period utilizing an average (13 month) rate base, identified future  
64 single item rate cases, and agreed to the timing of the next General Rate Case. On June  
65 1, 2009 the Commission issued a Report and Order adopting the Test Period Stipulation.

66 On June 23, 2009 the Company filed an application with the Commission for an increase  
67 to its retail rates in Utah of approximately \$66.9 million.

68

69 **III. INTRODUCTION OF WITNESSES AND ACCOMPANYING ADJUSTMENTS**

70 **Q. Please identify the Division's witnesses for the revenue requirement phase of this**  
71 **docket.**

72 A. DPU witness 1.0 is Mr. Charles Peterson, who previously filed testimony in this case on  
73 September 17, 2009. His testimony addressed ROE and issues related to the cost of  
74 capital requested by the Company. I am DPU witness 2.0. DPU witness 3.0 is Mr.  
75 Michael McGarry of Blue Ridge Consulting Services, Inc. (Blue Ridge). Mr. McGarry  
76 will present various accounting adjustments on behalf the DPU. He will also discuss the  
77 Company's commodity hedging operations and strategies. DPU witness 4.0 is Mr. David  
78 Thomson. He will cover adjustments related to budget target, airplane expenses due to  
79 deferred taxes, and rent. DPU witness 5.0 is Mr. Joseph Mancinelli of R.W. Beck, who  
80 was retained by the Division in this case for cost of service issues. Mr. Mancinelli will  
81 address COS issues and adjustments. In addition, Mr. Mancinelli will introduce and enter  
82 as an exhibit the Division's Logan Model. (The Division's Logan Model has been  
83 reviewed by RMP, and RMP has concluded that the Logan Model is an alternative model  
84 that renders the same results as the RMP model. In the Logan Model, formulas and error  
85 checking are more straightforward, with changes much easier to make.) DPU witness 6.0  
86 is Mr. George Evans of Slater Engineering, who was retained by the Division in this case  
87 for net power cost issues. Mr. Evans will discuss net power cost adjustments. DPU

88 witness 7.0 is Mr. Matthew Croft. He will address adjustments to the Company's Lead  
89 Lag study, the Washington Public Utility Tax, and a budget adjustment from average to  
90 midyear. Mr. Croft also ran the Jurisdictional Allocation Model (JAM) for the Division.  
91 DPU witness 8.0 is Ms. Brenda Salter, who covers distribution overhaul, uncollectible  
92 expenses, PERCO adjustments, and green tag revenue. DPU witness 9.0 is Mr. Jonathan  
93 Nunes of R.W. Beck. Mr. Nunes will address load forecasting issues. DPU witness 10.0  
94 is Dr. Joni Zenger. She will describe a Division adjustment concerning wind plant  
95 prudence, as well as several policy concerns related to wind resources development.  
96 DPU witness 11.0 is Dr. William (Artie) Powell, who will provide additional detail on  
97 the Division's wind integration cost adjustment. Dr. Powell also addresses certain  
98 contracts affecting net power costs. DPU witness 12.0 is Mr. Douglas Wheelwright. He  
99 will address PacifiCorp's hedging policies. DPU witness 13.0 is Mr. James Dalton. Mr.  
100 Dalton will present additional net power cost adjustments. DPU witness 14.0 is Mr.  
101 Charles Peterson. He will address adjustments to wind plants and special contracts. The  
102 Division will introduce additional witnesses when appropriate in the rate design phase of  
103 this case.

104

105 **Q. What ROE did the Division recommend for this case?**

106 A. The Division is recommending an ROE of 10.50 percent, which, as previously  
107 mentioned, was supported by Division witness Mr. Peterson (DPU Exhibit No. 1.0). The  
108 table below sets forth the Division's recommendation regarding overall weighted average

109 cost of capital (WACC) as discussed in Mr. Peterson’s testimony (cf. page 7 in DPU  
110 Exhibit No. 1.0):

111

<u>Component</u>	<u>Structure</u>	<u>Cost</u>
Long-Term Debt	49.20%	5.98%
Preferred Stock	0.30%	5.41%
Common Stock	50.50%	10.50%
WACC	100.00%	8.26%

112

113 **Q. Did the Company’s rate case filing have a similar adjustment as the last rate case**  
114 **filing in which the forecasted calculation of non-power O&M expenses was reduced**  
115 **to a budget target amount?**

116 A. Yes. In RMP Exhibit SRM-2 of the current rate case filing, adjustment 4.19 reduces the  
117 calculated forecasted non-power O&M expenses to a 2009/2010 budget target amount.  
118 This adjustment reduction to Utah-allocated O&M costs is \$3,819,971.

119

120 **Q. Why did the Company calculate future test period costs using previous rate case**  
121 **methods and then reduce those costs to the Company’s 2009/2010 budget target?**

122 A. The Company states in Steven R. McDougal’s testimony lines 446 to 454 the following:  
123 “With certain exceptions the Company intends to align the non-power cost O&M in this  
124 case to the amount in the budget. Since the adjusted actual expenses are higher than

125 budget, in this case escalated non-power cost O&M is adjusted downward to reflect the  
126 budgeted level. A limited number of adjustments to budget were made for the following  
127 items: averaging of overhaul and insurance expenses, non-utility advertising, ETO  
128 credits, and labor adjustments. Adjustment 4.19 is dependent upon other adjustments in  
129 this filing as shown on page 4.19.2 and will change accordingly if other adjustment  
130 amounts change.”

131  
132 The DPU notes that the Company’s target budget is an average of an adjusted 2009 total  
133 OMAG budget number and an adjusted 2010 total OMAG budget number. Thus, in  
134 addition to data for the test period, data for six months prior to the test period and six  
135 months after the test period have been averaged into the budget target adjustment that the  
136 Company is saying will reflect the O&M expense for the test year period. DPU witness  
137 Mr. Croft will address this issue in more detail in direct testimony.

138  
139 **Q. What are the Division’s concerns with the budget adjustment 4.19?**  
140 A. The Division’s primary concern with the Company’s budget adjustment is that it is not  
141 subject to audit. It cannot be audited, because it is not, with few exceptions, at the  
142 appropriate FERC account level of detail. The rate case is prepared at the FERC account  
143 level, yet the budget adjustment is not done by FERC account. In addition, the Division  
144 has other concerns with how the budget adjustment is calculated, the use of total  
145 Company numbers, and the timing in the preparation of the budget compared to the rate  
146 case. The Division’s concern over the budget adjustment resulted in a number of



147 questions addressed to the Company. Exhibit 2.3 provides the confidential response to a  
148 Division data request. Exhibit 2.4 provides the response to other Division and Office of  
149 Consumer Services data requests.

150

151 **Q. Based on the above, what will be the Division policy in this rate case for its**  
152 **adjustments to the non-power O&M expenses?**

153 A. The Division will assume its adjustments for non-power O&M costs are a reduction or  
154 addition to the Company's final non-power O&M cost in its rate case filing. The target  
155 budget presented by the Company does not contain adequate FERC-level detail to  
156 correspond to a FERC-based historical cost to adjust for known and measurable changes  
157 and escalations.

158

159 The Division conducted its review and audit of the rate case filing using the amount and  
160 detail found in FERC-level accounting using historical costs, adjusted for known and  
161 measurable changes, and escalations for forecasted non-power O&M costs in the  
162 currently filed general rate case. Its adjustments will be based on the audit of those  
163 known and measurable changes and escalations.

164

165 **Q. Is it possible that by both accepting adjustment 4.19 and adding additional O&M**  
166 **cost adjustments that the Division could be double-counting some adjustments?**

167 A. Yes, that is a possibility that Division staff discussed at some length. However, because  
168 there was no way to determine whether any particular adjustment was or was not already

169 included in adjustment 4.19, and because the burden of proof in this case is on the  
170 Company to justify its costs, we determined that it was most appropriate to propose our  
171 adjustments and allow the Company to respond. If the Company can firmly document,  
172 with appropriate evidence, that any of our non-power O&M adjustments have already  
173 been included in 4.19, we are willing to withdraw such adjustments in the future.

174

175 **Q. Please explain the methodology used to model the adjustments proposed by the**  
176 **various Division witnesses.**

177 A. PacifiCorp's June 2010 JAM was used in conjunction with the various "template"  
178 spreadsheets and Division work papers in order to model the adjustments proposed by the  
179 various Division witnesses. The individual templates were provided with Company  
180 witness Mr. Steven McDougal's Direct Testimony. These adjustments were then entered  
181 into the "Adjustments" tab in the JAM. The following exhibits correspond to these  
182 templates:

183 DPU Exhibit 2.5 – DPU JAM

184 DPU Exhibit 2.6 – DPU Rate Base Spreadsheet

185 DPU Exhibit 2.7 – DPU Depreciation and Spreadsheet

186 DPU Exhibit 2.8 – DPU Retirement Spreadsheet

187

188 Some of the adjustments proposed by the Division had the effect of changing the  
189 Company's adjustment 4.19. This change is also reflected in the "Adjustments" tab. The  
190 June 2010 JAM was re-calculated using the Rolled-In method in order to provide the

191 June 2010 Rolled-In Revenue Requirement. The revenue requirement under Rolled-In  
192 was then compared to the Revenue Requirement under Revised Protocol. The  
193 Commission's Order in Docket No. 02-035-04 regarding inter-jurisdictional cost  
194 allocation indicates the lesser of Revised Protocol and Rolled-In, each adjusted by the  
195 appropriate stipulated premium or cap respectively, will be used as Utah's revenue  
196 requirement. In this case the Rolled-In methodology yielded a lower revenue  
197 requirement.

198

199 **Q. Did you prepare a summary of the Division's adjustments that you describe above?**

200 A. Yes. Attached to my testimony is DPU Exhibit 2.2, which summarizes each of the  
201 Division's adjustments. This spreadsheet originated from the "Adjustment Summary"  
202 tab in DPU Exhibit 2.5 (DPU JAM). In general, all of the adjustments in DPU Exhibit  
203 2.2 may differ slightly from what is included in other Division exhibits due to the effect  
204 of the MSP cap, taxes, and how the JAM is run.

205

206 **Q. Please describe the methodology that you used in entering the inputs into the JAM.**

207 A. Each of the accounting adjustments were entered into the model in the order listed in  
208 DPU Exhibit 2.2. For instance, the first adjustment entered into the JAM was Division  
209 Witness Mr. Peterson's adjustment to the Company's cost of capital and the last  
210 adjustment entered was Division Witness Dr. Powell's QF contracts adjustment.

211

212 **IV. THE DIVISION'S POLICY RECOMMENDATIONS**

213

214 **Q. Early resolution of the test year issue has been a previous Division recommendation.**

215 **Does this remain the case?**

216 A. Yes. The Division looks forward to a test year procedural process that will provide for  
217 early resolution of the appropriate test year. That early resolution of the test year in the  
218 current rate case was achieved.

219

220 **Q. Has the Division taken any action to address the Company's hedging activities?**

221 A. Yes. The Division retained Blue Ridge Consulting Services, Inc. (Blue Ridge) via a  
222 competitive bid process to assist the Division's Staff with the evaluation of net power  
223 costs in the Company's current rate case before the Commission. Blue Ridge's scope  
224 included evaluating the reasonableness of RMP's net power costs and related hedging  
225 costs included in those costs.

226

227 As part of that evaluation, Blue Ridge proposed to complete an analysis of the  
228 Company's fuel price hedging/risk management policies and practices. Blue Ridge's  
229 analysis of the Company's hedging and risk management program focused on an  
230 evaluation of the following areas:

- 231
- 232 • Identification of risk tolerance
  - 233 • Establishment of risk management goals and guidelines
  - 234 • Definition of risk metrics
  - 235 • Establishment of procedures and authority for execution of hedges
  - 236 • Procedures for managing credit risk
  - 237 • Establishment of measurement and reporting procedures including accounting and compliance

238 Division Staff also requested that Blue Ridge provide an assessment of how the  
239 Company's hedging policies compare to those used in other states or jurisdictions in the  
240 United States.

241  
242 Blue Ridge performed a high-level review of the Company's commercial trading and risk  
243 management hedging procedures and practices and developed a report with findings,  
244 conclusions, and recommendations for the Division to consider requesting that the  
245 Company implement to enhance its commercial trading and risk management functions.

246  
247 Mr. Michael J. McGarry, Sr. President/CEO of Blue Ridge is testifying in this proceeding  
248 and will summarize Blue Ridge's findings and conclusions related to the Company's  
249 hedging activities. In addition, Mr. George Evans is testifying to certain Division-  
250 sponsored net power costs adjustments.

251  
252 **Q. Based on Blue Ridge's review, does the Division have any specific recommendations**  
253 **related to the Company's hedging and risk management?**

254 A. Yes. In addition to the operational and procedural recommendations associated with the  
255 Company's Commercial and Trading Policies and Practices outlined in Blue Ridge's  
256 report, which Mr. McGarry summarizes in his testimony, the Division believes that the  
257 Commission should adopt a "pre-approval" policy of the Company's hedging strategy. A  
258 pre-approval process is also proposed in Mr. Wheelwright's testimony. This process can  
259 be fully developed discussed and litigated within the context of Docket No. 09-035-21,

260 which was opened for the purpose of reviewing the Company's hedging strategy and  
261 practice. The primary benefit of this pre-approval process is that it will: a) provide the  
262 Commission with a complete picture and allow all parties the opportunity to review and  
263 comment on the Company's strategy and whether it is in the best interest of the Company  
264 and its customers; and b) will help to mitigate the second guessing that is inherent in any  
265 hedging program. The Division strongly believes that this approach will not negate the  
266 Company's responsibility to act prudently, efficiently, and in the best interest of its  
267 customers.

268

269 **Q. What can you conclude about the prudence of the Company's decisions in acquiring**  
270 **wind resources?**

271 A. Division witness Dr. Joni Zenger addresses this matter in her testimony. The Division  
272 maintains it needs to make sure that all of the decisions are prudent, the costs are  
273 justified, and there is a net benefit to Utah ratepayers on future wind acquisitions. The  
274 Division intends to conduct a prudence review of all future wind projects that the  
275 Company proposes bringing into rate base. In order to do so, we make the following  
276 recommendations to the Commission:

- 277
- The Commission should require the Company to report detailed accounting of its  
278 capital wind projects, especially BOP costs, rather than lump sum numbers.
  - The Company should be required to submit a notification letter to the  
279 Commission at the time that each wind plant comes in service.  
280

- 281           • The Division recommends that the Commission look closely at proposed multiple  
282           wind resource projects that are built adjacent to others and determine in fact if  
283           they should be considered a single project.

284

285           Dr. Zenger's testimony also raises substantive concerns about the manner in which the  
286           Company has developed recent wind resource projects.

287

288   **Q. Mr. Mancinelli's testimony presents cost of service results. What is the Division's**  
289   **recommended rate spread among the classes?**

290   **A.** For a number of reasons, the Division does not believe that it would be appropriate to  
291   attempt to exactly match the cost of service results found in Mr. Mancinelli's Exhibit 5.8.  
292   For one, Mr. Nunes testimony casts considerable doubt upon the load forecasting that is  
293   an input into the cost of service analysis. Thus, Mr. Mancinelli's results have a margin of  
294   error that he is unable to address. In addition, cost of service results should always be  
295   interpreted carefully to avoid undue changes in rate direction for specific classes.  
296   Finally, because the Division's suggested revenue increase is only \$8.4 million, it would  
297   be difficult to "fine tune" the cost of service with such a small increase even if it were  
298   desirable. We would thus propose that the Division's proposed revenue increase be  
299   allocated only to Schedules 9 and 10 in proportion to their contribution to the cost of  
300   service.

301

302 **Q. Some of the smaller rate classes also show significant deviation from the cost of**  
303 **service. Why are you not recommending changes to their rates?**

304 **A.** For the classes that are shown as significantly overpaying (street and outdoor lighting),  
305 were we to allocate a decrease proportionate their share of the cost of service, the result  
306 would be an insignificant amount. Moreover, we do not wish to send a price signal that  
307 would encourage increased use of energy in these classes. For the remaining class that is  
308 shown as significantly underpaying (traffic signals), again, pro-rating the amount of any  
309 rate change would also result in insignificant dollar amounts.

310

311 **Q. Is there any other reason to focus solely on classes 9 and 10?**

312 **A.** Yes there is. For several rate cases in a row, cost of service studies have suggested that  
313 these two rate classes are underpaying. Whenever rate increases are allocated evenly  
314 across classes, underpaying classes have the amount of their under-contribution widened.  
315 Because there is a trend of studies showing these classes are underpaying, we are  
316 concerned that evenly distributing this increase will exacerbate an ongoing cost of service  
317 issue.

318

319 **Q. What, then, are the amounts by which you propose raising rates for Schedules 9 and**  
320 **10?**

321 **A.** The table below show both how the Division calculated the increase and the suggested  
322 amounts.

323



324

	Adjusted COS per DPU Exhibit 5.8	Class Revenue per DPU Exhibit 5.8	Share of COS (Class / Total)	Class Increase (Share * Increase)	Percent Increase in Class Revenue
Schedule 9	173,456,318	159,688,687	92.993%	7,868,197	4.927%
Schedule 10	13,070,469	10,962,790	7.007%	592,893	5.408%
Total	186,526,787	170,651,477	100.000%	8,461,090	
DPU Proposed Revenue Requirement Increase			8,461,090		

325

326

327 **Q: Do you have any other issues you would like to address?**

328 A: Yes. The Division has held settlement discussions with the Company and the Office of  
329 Consumer Services regarding certain income tax related issues including, (1) full  
330 normalization of all temporary book-tax differences and (2) a change in method of  
331 accounting for income tax purposes. A settlement on these issues will, among other  
332 things, affect the Division's recommendations on a final revenue requirement and  
333 increase in retail rates for Rocky Mountain Power in Docket No. 09-035-23. The parties  
334 have, at this time, an agreement in principle on these issues. The Division anticipates that  
335 a final settlement agreement is forthcoming and will be filed with the Commission in the  
336 near future. Furthermore, the Division anticipates that a Commission order can be  
337 entered in time to be included in this docket. In the event that an agreement is not  
338 reached or the Commission rejects the settlement proposal, the Division reserves the right  
339 to address these issues in rebuttal testimony or at another time during this case.

340

341

**VI. CONCLUSION**

342 **Q. In conclusion, please restate the Division's recommendation for revenue**  
343 **requirement.**

344 A. The Division recommendation for revenue requirement is \$8.5 million. The Division  
345 first added the \$ 2.0 million SMUD adjustment from the DSM Stipulation then made a  
346 total of \$58.4 million in adjustments to arrive at a revenue requirement recommendation  
347 of \$8.5million. The Division adjustments were a \$22.2 ROE adjustment, a total of \$16.4  
348 million in net power cost adjustments, and a total of \$19.9 million in various auditing  
349 adjustments.

350

351 **Q. Does this complete your testimony?**

352 A. Yes it does.