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BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

In the Matter of the Application of Rocky Mountain Power for Authority to Change its Depreciation Rates Effective January 1, 2014	Docket No. 13-035-02
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PREFILED DIRECT TESTIMONY OF NEAL TOWNSEND

The UAE Intervention Group (UAE) hereby submits the Prefiled Direct Testimony of Neal Townsend.

DATED this 21nd day of June, 2013.

/s/ _____
Gary A. Dodge,
Attorney for UAE

BEFORE
THE PUBLIC SERVICE COMMISSION OF UTAH

Direct Testimony of Neal Townsend

on behalf of

UAE

Docket No. 13-035-02

June 21, 2013

23 **Q. Have you testified previously before any other state utility regulatory**
24 **commissions?**

25 A. Yes. I have testified in utility regulatory proceedings before the Arkansas
26 Public Service Commission, the Illinois Commerce Commission, the Indiana
27 Utility Regulatory Commission, the Kentucky Public Service Commission, the
28 Michigan Public Service Commission, the Public Utilities Commission of Ohio,
29 the Public Utility Commission of Oregon, the Public Utility Commission of
30 Texas, the Virginia Corporation Commission, and the Public Service Commission
31 of West Virginia. A more detailed description of my qualifications is contained in
32 Attachment A, attached to this testimony.

33

34 **OVERVIEW AND CONCLUSIONS**

35 **Q. What is the purpose of your testimony in this proceeding?**

36 A. My testimony responds to the depreciation study filed by PacifiCorp in
37 this docket. My testimony is limited to two issues - the steam production reserve
38 imbalance and the expected steam plant lives. The absence of comment on my
39 part regarding other issues does not signify support for (or opposition to) the
40 Company's filing with respect to the non-discussed issues.

41 **Q. Please summarize your conclusions and recommendations.**

42 A. In order to mitigate the potential rate impact resulting from closure of the
43 Carbon Plant, I recommend amortizing the depreciation reserve imbalance surplus
44 for steam plants other than the Carbon Plant through 2020. I also recommend

45 extending the plant lives for the Craig and Gadsby steam plants to match the
46 current planning assumptions.

47

48 **TREATMENT OF STEAM PRODUCTION RESERVE IMBALANCE**

49 **Q. What is meant by a “depreciation reserve imbalance”?**

50 A. A depreciation reserve imbalance exists when book accumulated
51 depreciation and theoretical reserve are not equal. When book accumulated
52 depreciation exceeds the theoretical reserve, a reserve surplus exists; the inverse
53 situation indicates a reserve deficit. The theoretical reserve represents the level of
54 depreciation reserve that should exist assuming that the currently-estimated
55 depreciation parameters (average service life, net salvage, and retirements) have
56 always been in place. With each depreciation study, estimated service lives and
57 net salvage are likely to change. Therefore the parameters which guided past
58 depreciation accruals likely differ from the most recent estimates.

59 **Q. Does PacifiCorp have a depreciation reserve imbalance for the Steam
60 Production Plant function?**

61 A. Yes, in total, the Steam Production Plant function has a reserve surplus of
62 \$48.3 million, based on plant as of December 31, 2011.¹ However, rather than
63 maintaining a single depreciation reserve account for the Steam Production
64 functional classification, as prescribed in the FERC Uniform System of Accounts,
65 PacifiCorp further allocates its accumulated depreciation reserve among the plant

¹ See pages 111-842 through 111-905 of the 2013 Depreciation Study for the Calculated Accrued (Theoretical Reserve) and Allocated Book Reserve by plant and account.

66 sites within the Steam Production function. Using PacifiCorp's allocation
67 methodology, the Carbon Plant singularly reduces the reserve surplus by \$61.0
68 million. Excluding the Carbon Plant, the Steam Production function has a reserve
69 surplus of \$109.3 million. This means that for steam plants other than Carbon,
70 PacifiCorp has collected from ratepayers \$109.3 million more in depreciation
71 expense than the level indicated by current depreciation parameters.

72 **Q. What is the proper treatment of depreciation reserve imbalances?**

73 A. According to the 1996 National Association of Regulatory
74 Commissioners' manual entitled "Public Utility Depreciation Practices" (NARUC
75 Manual), when a reserve imbalance exists, the decision as to whether and how to
76 correct the reserve imbalance is subjective. The NARUC Manual recommends
77 immediate depreciation accrual adjustments when imbalances are found to be
78 material, noting that "the use of an annual amortization over a short period of time
79 or the setting of depreciation rates using the remaining life technique are two of
80 the most common options for eliminating the imbalance."²

81 **Q. What is PacifiCorp's proposed treatment of the reserve imbalance?**

82 A. PacifiCorp's depreciation study utilizes the remaining life method, which
83 calculates a depreciation rate which eliminates the surplus or deficit allocated to
84 each plant site over the remaining life of each plant.

85 **Q. What is your assessment of PacifiCorp's approach to correcting the reserve**
86 **imbalance?**

² NARUC Manual, p. 189.

87 A. I recommend a more rapid amortization of the reserve imbalance for steam
88 plants other than the Carbon Plant. According to the stipulation in PacifiCorp's
89 last Utah general rate case, Docket No. 11-035-200, PacifiCorp is authorized to
90 amortize prudently-incurred "Remaining Carbon Balances" and removal costs
91 from the date of plant closure (estimated as April 2015) through 2020. While
92 UAE is not indicating support for PacifiCorp's projected \$56.8 million removal
93 costs, customers will likely experience a significant increase as a result of
94 removal cost amortization. In order to mitigate this potential rate impact, I
95 recommend amortizing the reserve surplus for steam plants other than the Carbon
96 Plant through 2020. By matching the amortization periods for the reserve surplus
97 and the Carbon Plant remaining balances and removal costs, the rate impact on
98 customers over this period is reasonably ameliorated.

99 **Q. What is the impact of amortizing the reserve surplus through 2020?**

100 A. I estimate that PacifiCorp's remaining life depreciation rates implicitly
101 include an annual credit of \$4.9 million for the reserve surplus for steam plants
102 other than the Carbon Plant, based on plant as of December 31, 2011. My
103 recommendation to amortize this \$109.3 million surplus through 2020 results in
104 an annual accrual credit of \$12.1 million. Therefore, UAE's recommended
105 adjustment reduces the annual depreciation accrual by approximately \$7.2 million
106 relative to PacifiCorp's proposal, or \$3.0 million on a Utah-allocated basis.³ The
107 impact of this adjustment is shown in UAE Exhibit 1.1 (TNT-1).

³ Please note that my calculations use plant balances as of December 31, 2011 because PacifiCorp's depreciation study did not calculate the theoretical reserve for December 31, 2013. Due to lack of

108 **EXPECTED PLANT LIVES**

109 **Q. What is your concern regarding expected plant lives?**

110 A. I am aware of at least two steam production facilities for which the
111 expected remaining plant life in PacifiCorp's depreciation study does not match
112 the expected remaining plant life that is otherwise indicated in planning
113 documents. Specifically, the Gadsby steam plant is assumed to retire in 2022 in
114 the depreciation study, but is not expected to retire until after 2032 according to
115 PacifiCorp's 2013 IRP. Similarly, the Craig plant is assumed to retire in 2034 in
116 the depreciation study, but is not planned to be retired until 2052.⁴

117 **Q. What are the consequences of a mismatch between the expected plant life in**
118 **the depreciation study and the actual planned plant life?**

119 A. If the remaining plant life assumed in the depreciation study is shorter than
120 what the Company is actually planning, then the annual depreciation rate will be
121 set too high, causing an unfair cost burden on current customers.

122 **Q. What are your recommended adjustments?**

123 A. PacifiCorp's depreciation rates should be recalculated assuming a 2032
124 retirement date for Gadsby and a 2051 retirement date for Craig.

125 **Q. What is the revenue requirement impact of your adjustments?**

126 A. The impact of these adjustments is shown in UAE Exhibit 1.2 (TNT-2).
127 These adjustments reduce annual Utah depreciation expense by \$267,000 for the

comprehensive workpapers with intact formulae provided by PacifiCorp, I was not able to replicate these calculations for December 31, 2013 plant balances. My recommendation to amortize the non-Carbon Plant surplus through 2020 could also be applied to December 31, 2013 plant balances.

⁴ PacifiCorp Response to DPU Data Request No. 8.1.

128 Gadsby plant and \$1,099,000 for the Craig plant. Note that these adjustments
129 were calculated on a standalone basis, i.e., the adjustments are not incorporated
130 into my proposal to amortize the Company's surplus steam plant reserves by
131 2020. If these adjustments are adopted in tandem with my surplus amortization
132 proposal, the latter would have to be recalibrated to take into account the longer
133 remaining lives at the Gadsby and Craig plants. PacifiCorp should be required to
134 perform this calculation as part of its compliance filing in this case. I did not
135 perform this calculation myself because the workpapers provided by the Company
136 in discovery did not include a working model of the Company's depreciation
137 study and therefore are insufficient for this purpose.

138 **Q. Does this conclude your direct testimony?**

139 **A.** Yes, it does.