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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. 13-035-184

PREFILED DIRECT TESTIMONY OF NEAL TOWNSEND

[COST OF SERVICE / RATE SPREAD / RATE DESIGN]

The UAE Intervention Group (UAE) hereby submits the Prefiled Direct Testimony of Neal Townsend on cost of service, rate spread and rate design issues.

DATED this 22nd day of May, 2014.

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

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing was served by email this 22nd day of May, 2014, on the following:

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BEFORE
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Direct Testimony of Neal Townsend

on behalf of

UAE

Docket No. 13-035-184

[Cost of Service / Rate Spread / Rate Design]

May 22, 2014

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DIRECT TESTIMONY OF NEAL TOWNSEND

INTRODUCTION

Q. Please state your name and business address.

A. My name is Neal Townsend. My business address is 215 South State Street, Suite 200, Salt Lake City, Utah, 84111.

Q. By whom are you employed and in what capacity?

A. I am a Director for Energy Strategies, LLC. Energy Strategies is a private consulting firm specializing in economic and policy analysis applicable to energy production, transportation, and consumption.

Q. On whose behalf are you testifying in this proceeding?

A. My testimony is being sponsored by the Utah Association of Energy Users Intervention Group (“UAE”).

Q. Please describe your professional experience and qualifications.

A. I have provided regulatory and technical support on a variety of energy projects at Energy Strategies since I joined the firm in 2001. Prior to my employment at Energy Strategies, I was employed by the Utah Division of Public Utilities as a Rate Analyst from 1998 to 2001. I have also worked in the aerospace, oil and natural gas industries.

Q. Have you previously testified before this Commission?

A. Yes. Since 1997, I have testified in eleven dockets before the Utah Public Service Commission on electricity and natural gas matters.

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 addresses the following cost-of-service, spread, and rate
37 design issues:

38 (1) Certain components of RMP's cost-of-service study.

39 (2) The appropriate spread of the revenue requirement increase that will
40 be determined in this case.

41 (3) The appropriate rate design approach for Schedules 8 and 9.

42 As I have not undertaken an exhaustive analysis of all cost of service, spread and
43 rate design proposals of RMP, absence of comment on my part regarding a

44 particular issue does not signify support (or opposition) toward the Company's
45 filing with respect to the non-discussed issue.

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

47 A. (1) RMP's cost-of-service study inappropriately imputes a significant
48 portion of the revenue credit associated with Special Contract 3, Schedule 21, and
49 Schedule 31 to the distribution, retail, and miscellaneous functions. I recommend
50 that the revenue associated with transmission voltage customers served on
51 Schedules 21 and 31, and the entirety of Special Contract 3 revenue, be
52 functionalized as production and transmission only.

53 (2) I recommend the Commission adopt a rate spread approach consistent
54 with that proposed in the direct testimony of RMP witness Joelle R. Steward,
55 which is guided by the results of the cost-of-service study, while not adhering
56 rigidly to class revenue deficiencies indicated by the study. Specifically, I
57 recommend that rate changes for each applicable schedule be determined based
58 on the percentage differentials relative to the mid-point increase, as illustrated in
59 Table TNT-2.

60 (3) The Commission should not adhere strictly to class revenue
61 deficiencies indicated by any given cost-of-service study for a number of reasons,
62 including the fact that the cost of service methods typically used in Utah do not
63 adequately recognize the cost-causative nature of Utah's seasonal loads, and that
64 other ratemaking principles, including the principle of gradualism, should be
65 employed to mitigate customer impacts.

66 (4) I recommend the Commission adopt a rate design approach for
67 Schedules 8 and 9 consistent with that recommended in the direct testimony of
68 Ms. Steward, in which the facilities, demand and energy charges are uniformly
69 increased to reflect the revenue requirement change.

70

71 **COST OF SERVICE**

72 **Q. Have you reviewed the class cost-of-service (COS) study presented by Ms.**
73 **Steward?**

74 A. Yes, the results of Ms. Steward's study are shown in Exhibit
75 RMP___(JRS-3).

76 **Q. Do you have any general comments on the Company's COS study?**

77 A. Yes. RMP's current cost apportionment method for production and
78 transmission plant and non-fuel expenses classifies these costs as 75 percent
79 demand-related and 25 percent energy-related, with the demand-related portion
80 allocated based on each class's contribution to the 12 monthly system coincident
81 peaks ("12 CP"). In my opinion, the current 12 CP allocation method does not
82 properly reflect the cost-causative nature of Utah's seasonal loads; fewer
83 coincident peaks would be more appropriate. However, I am not proposing any
84 specific changes to this method in this direct testimony because this issue is
85 currently under active discussion at the inter-jurisdictional allocation level in the
86 Multi-State Process ("MSP"). As a signatory to the existing MSP protocol and as
87 an active MSP participant, UAE's current intent is to address this issue at the

88 MSP level, and later at the state level. This intention may change depending, in
89 part, on cost of service changes or proposals that may be advocated by others in
90 this docket.

91 **Q. Do you have any specific concerns related to RMP's COS study?**

92 A. Yes. RMP's COS study includes \$33.3 million that is treated as a state
93 specific revenue credit to offset the costs of providing electric service to
94 customers. The revenues are related to Schedule 21 (Electric Furnace
95 Operations), Schedule 31 (Back-Up, Maintenance, and Supplementary Power),
96 and Special Contract 3. The Company does not calculate COS results for these
97 customer categories. Since these customer categories are not formally allocated
98 costs through the COS study, their "costs" are implicitly allocated amongst the
99 other customer classes, and the revenue associated with Schedule 21, Schedule
100 31, and Special Contract 3 is treated as a credit to offset these costs.

101 **Q. How has RMP treated this revenue credit in its COS study?**

102 A. RMP has imputed a portion of this revenue across all five functions
103 (production, transmission, distribution, retail, and miscellaneous) in its COS
104 study. For example, approximately \$5 million of the \$33.3 million is credited
105 against the distribution function costs.

106 **Q. Do you agree with RMP's proposed revenue credit treatment?**

107 A. No. Special Contract 3 revenues comprise the vast majority of the
108 revenue credit, accounting for \$28.6 million of the \$33.3 million total. Like
109 Schedule 9 industrial customers, Special Contract 3 takes service at transmission

110 voltage. Furthermore, based on my review of Ms. Steward's Exhibit
111 RMP__(JRS-5), approximately 79% of the Schedules 21 and 31 revenues, or \$3.7
112 million, is attributable to transmission voltage customers.¹ Thus, 97% of the total
113 revenue credit comes from transmission voltage customers. Distribution facilities
114 are not used to serve these customers. Therefore the costs they impose on the
115 system do not include distribution costs. In my opinion, it is not appropriate to
116 credit this revenue against distribution-related costs. Instead, all revenue resulting
117 from transmission voltage customers should be applied against the production and
118 transmission functions, consistent with the nature of the costs imposed by these
119 customers.

120 **Q. Have you assessed the impact of applying the transmission voltage revenue**
121 **credit solely to the production and transmission functions?**

122 A. Yes. I credited \$32.4 million (or approximately 97 percent of the total
123 state specific revenue credit) to the production and transmission functions.² I
124 present the results of the COS study with these revenues applied solely to the
125 production and transmission functions in UAE Exhibit COS 2.2. In Table TNT-1,
126 below, I compare the class increases required to achieve an equalized rate of
127 return at RMP's requested revenue requirement under RMP's COS approach to

¹ UAE Direct Exhibit COS 2.1 details the transmission and distribution voltage portions of the state specific revenue credit according to Exhibit RMP__(JRS-5).

² I functionalized the remaining \$963,031 revenue credit related to distribution voltage customers across all five functions, in the same manner as RMP.

128 the COS results with this revenue credit applied solely to production and
129 transmission costs.

Table TNT-1

**Comparison of RMP COS Revenue Change and Revenue Change with
Revenue Credits Applied to Production and Transmission Functions**

Sch. No.	Description	RMP COS Results (JRS-3)		COS Results with Revenue Credit Applied to P & T	
		Increase (Decrease) to = ROR	Percent Change	Increase (Decrease) to = ROR	Percent Change
1	Residential	52,729,492	7.97%	54,265,404	8.20%
6	General Service - Large	(20,505,727)	-3.94%	(20,893,854)	-4.01%
8	General Service - Over 1 MW	4,488,866	2.76%	4,311,931	2.65%
7,11,12	Street & Area Lighting	(1,450,159)	-11.96%	(1,353,249)	-11.16%
9	General Service - High Voltage	34,346,647	12.50%	33,343,224	12.13%
10	Irrigation	1,468,521	10.53%	1,482,976	10.63%
15	Traffic Signals	107,724	20.07%	110,546	20.59%
15	Outdoor Lighting	(440,355)	-31.92%	(441,163)	-31.97%
23	General Service - Small	(907,829)	-0.66%	(781,143)	-0.57%
SpC	Customer 1	5,359,489	19.72%	5,258,253	19.35%
SpC	Customer 2	1,055,432	3.01%	949,176	2.71%
	Total Utah Jurisdiction	76,252,101	4.13%	76,252,101	4.13%

133 **Q. What is your recommendation to the Commission on the proper treatment of**
134 **this revenue credit in the COS study?**

135 **A.** I recommend that the revenue credit associated with transmission voltage
136 customers be applied as a credit against production and transmission costs only.

137 **Q. Do you have any other recommendations related to the COS study at this**
138 **time?**

139 A. No, although as stated above, I do believe that changes to the current COS
140 methodology are appropriate to better reflect cost causation, particularly as it
141 relates to Utah's summer peaks.

142

143 **RATE SPREAD**

144 **Q. What revenue increase is RMP recommending for the Utah jurisdiction?**

145 A. The Company has requested a \$76,252,101, or a 4.05 percent overall Utah
146 revenue increase.

147 **Q. Have you reviewed the rate spread proposal presented by Ms. Steward?**

148 A. Yes, I have. As shown on RMP Exhibit ___(JRS-4), if Special Contract 2
149 and Annual Guarantee Adjustment ("AGA") revenues are excluded, this
150 \$76,252,101 represents a 4.13 percent overall Utah revenue increase. Ms.
151 Steward is proposing a rate spread in which customers served on Schedule 8
152 would receive a 4.09 percent increase, which represents the system average
153 increase excluding the revenue from Special Contract 2, Lighting schedules and
154 the AGA, adjusted to obtain the requested revenue requirement (which I will refer
155 to as the "Modified System Average" hereafter).³ Customers served on Schedule
156 6 would receive a 2.09 percent increase, approximately equal to 2 percent below
157 the Modified System Average increase. Customers served on Schedule 23 would
158 receive a 3.09 percent increase, approximately equal to 1 percent below the

³ RMP uses a Middle Point of 4.16%, which is the system average increase excluding Special Contract 2, Lighting schedules (except Traffic Signal Systems), and the AGA, which is then adjusted by -0.07% to reach the requested revenue requirement using the rate spread parameters.

159 Modified System Average increase. Residential customers on Schedules 1, 2, and
 160 3 would receive a 5.09 percent increase, approximately equal to 1 percent above
 161 the Modified System Average increase. According to the proposed rate spread,
 162 customers served on Schedules 9, 10, 21, and 31, plus the Special Contract 3
 163 customer would receive a 6.09 percent increase, approximately equal to 2 percent
 164 above the Modified System Average increase. Customers served on Schedule
 165 15T would receive a 7.09 percent increase, approximately equal to 3 percent
 166 above the Modified System Average increase. The remaining lighting customers
 167 would receive a 0 percent increase. The Special Contract 1 customer would
 168 receive a 4.05 percent increase, equivalent to the overall Utah increase. No
 169 increase is assumed for Special Contract 2. These rate changes relative to the
 170 Modified System Average increase are illustrated for each applicable schedule in
 171 Table TNT-2, below.

Table TNT-2

**Rate Change Differentials Relative to
 The Modified System Average Increase**

Schedule No.	Adjustment to Modified System Average
15T	3%
9, 10, 21, 31, Contract 3	2%
1, 2, 3	1%
8 (base point)	0%
23	-1%
6	-2%

175 **Q. What is your assessment of Ms. Steward's proposal?**

176 A. Given the COS results that RMP has presented and the adjusted COS
177 results that I prepared in this case, Ms. Steward's rate spread is reasonable. Under
178 Ms. Steward's recommended spread, classes earning returns below the system
179 average receive percentage rate increases that are above the average, and vice
180 versa, while the class earning close to the average retail return receives an
181 increase approximately equal to the system average increase. At the same time,
182 this spread proposal does not rigidly adhere to the class revenue deficiencies
183 indicated by RMP's COS study. Particularly given the deficiencies in the RMP
184 COS approach, I believe this is a reasonable approach.

185 **Q. Why is it reasonable to not adhere strictly to the class revenue deficiencies**
186 **indicated by RMP's COS study?**

187 A. The quantitative results of the cost of service analysis should provide only
188 general guidance for rate spread determinations. Informed judgment is also
189 required in applying the results of the quantitative analysis. As a general matter,
190 COS studies should yield under proper circumstances to other ratemaking
191 principles, such as the principle of gradualism, which takes into consideration the
192 impact of rate increases on various customer groups. In this proceeding, the
193 principle of gradualism is particularly important for customers taking service
194 under Schedule 9, in light of the failure of RMP's COS methodology to account
195 adequately for the significant impacts of Utah's summer peaks. In addition,

196 consideration should be given to the fact that Utah industries are still attempting
197 to recover from a harsh recession.

198 **Q. What is your rate spread recommendation?**

199 A. I recommend the Commission adopt a rate spread approach which is
200 guided by the relative rate changes for each schedule as proposed by Ms. Steward.
201 Specifically, I recommend that rate changes for each applicable schedule be
202 determined based on the percentage differentials relative to the Modified System
203 Average increase, as illustrated in Table TNT-2.⁴

204 **Q. What is your recommendation if the actual revenue increase granted by the
205 Commission is lower than that requested by RMP?**

206 A. If the revenue requirement approved by the Commission is less than that
207 requested by RMP, I recommend that the rate spread proposal illustrated in Table
208 TNT-2 be used as the starting point for spreading the approved revenue change.
209 Specifically, I recommend that each class's rate change relative to the Modified
210 System Average be preserved at a lower revenue requirement.

211 **Q. Do you have an example of how this approach would work?**

212 A. Yes. An example is presented in UAE Exhibit COS 2.3 using a
213 hypothetical revenue increase of \$10 million.

214

⁴ I note that UAE witness Kevin Higgins has proposed an adjustment in the Revenue Requirement phase of this docket related to a special contract revenue increase per the terms of the relevant contract. The outcome of this case may impact the level of special contract revenues to which the contractual increase is applied. I recommend that the Company be directed to reflect this small incremental revenue increase in its compliance filing in this case.

215 **SCHEDULES 8 AND 9 RATE DESIGN**

216 **Q. Have you reviewed RMP's proposed rate design for Schedules 8 and 9?**

217 A. Yes, the proposed rate designs, as presented in Exhibit RMP____(JRS-5),
218 utilize uniform increases in the facilities, demand and energy charges to reflect
219 the proposed revenue requirement change. In addition, the Company proposes to
220 increase the monthly customer charge associated with each schedule.⁵

221 **Q. What is your recommendation to the Commission on the proper approach to**
222 **designing rates for Schedules 8 and 9?**

223 A. I recommend the Commission adopt a rate design approach for Schedules
224 8 and 9 consistent with that recommended by Ms. Steward, in which the facilities,
225 demand and energy charges are uniformly increased to reflect the revenue
226 requirement change.

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

228 A. Yes, it does.

⁵ See RMP witness Joelle R. Steward direct testimony, p. 18.