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BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

In the Matter of the Application of Pacificorp for Approval of its Proposed Electric Rate Schedules & Electric Service Regulations	: :	Docket Nos. 01-035-01

PREFILED DIRECT TESTIMONY OF DR. BRUCE GODFREY

FOR THE UTAH FARM BUREAU FEDERATION

COST OF SERVICE/RATE SPREAD

JUNE 15, 2001

Q. Please state your name, address of your residence and occupation.

A. I am E. Bruce Godfrey. I live at 657 East 1900 North, Logan, Utah. I am a professor in the Department of Economics at Utah State University.

Q. What is your professional and educational background?

A. I was raised on an irrigated farm in southern Idaho. I received Bachelor's and Master's degrees in Agricultural Economics from Utah State University. I also received a Doctor of Philosophy from Oregon State University. I was on the staff at the University of Idaho for nearly seven years before joining the staff at Utah State University in 1977. I have a copy of my personal vitae marked Exhibit EBG-1 that will give you additional detail concerning my education and experience.

Q. Are there items in Exhibit EBG-1 upon which you wish to comment that may be of particular interest at this time?

A. Yes. I am somewhat unique in terms of my academic appointment because I have responsibilities in all three areas that are emphasized by Utah State University and other similar land grant universities---teaching, research, and extension. My teaching responsibilities this past year included a senior level class in farm and ranch management, a sophomore/junior level class in agricultural marketing and a graduate class in natural resource economics. I have also taught a number of other classes in the general area of agricultural economics. My research for many years has focused on the economic problems associated with the use of publicly and privately owned resources. I have secured numerous research and extension grants that have been designed to address problems faced by farmers and ranchers. Two of these grants are from the Utah Tax Commission and the Utah Department of Agriculture and Food. These grants require the development of farm budgets for agricultural enterprises throughout the state (crop budgets are done for all major crops in every county in the state). As a result, I commonly work with farmers, ranchers and other professionals in obtaining the data for the budgets. I have also worked on several projects that have involved irrigation problems including water use and quality. My extension assignment involves work with farmers and ranchers throughout the state. Much of this work has focused how farmers and ranchers can manage the risks they face as producers. In addition, I serve on several regional and national committees that involve evaluating problems faced by farmers and ranchers throughout the western region as well as the nation. I am also currently serving as the secretary-treasurer of the Western Agricultural Economics Association, a member of the national Farm Business Management Career Development event for the Future Farmers of America. My vitae indicates that I have prepared budgets for the primary crops grown on irrigated lands for every county in Utah as well as other agricultural enterprises.

Q. Can you give us an example of these budgets?

A. Yes. An illustrative example is the production budget for soft white wheat in Box Elder County shown in Exhibit EGB-2.

Q. What does this budget indicate?

A. This wheat budget indicates that the net returns to the fixed factors (land and operator management) were just over $ 100 per acre. If a farmer carried a high debt load for land at current interest rates the net returns would be negative (interest costs alone at 10 % on a debt of $1000 per acre would be essentially equal to the net returns with out debt). Thus, farmers who are highly leveraged to buy land (debt is greater than equity) would find growing wheat to be an unprofitable enterprise. This is one reason why there has been a shift from grain production to other crops (primarily forages) in Utah since 1996. But, the returns from these crops are generally not high. Low profits for crop enterprises, however, allows livestock operations to obtain inexpensive feed which increases their net returns. As a result, the net returns to agricultural operations varies widely and depends upon the crop and/or livestock enterprises the individual farmer emphasizes.

Q. What are some other factors that affect the variation in farm income?

A. The variation between operators is most commonly due to differences in the productivity of the lands being farmed, the management skills of the operator, the enterprises that contribute to overall farm profitability and the constraints faced by individual operators such as the source and amount of irrigation water available. Variation over time is commonly most affected by weather and the prices paid for inputs and prices received for the products produced.

Q. Can you give the Commission a general idea of what has been happening to the prices farmers have been receiving for their crops?

A. The prices received by farmers have become more volatile over time. Exhibit EBG-3 shows the average prices farmers received for grains during the past several years. Prices for all grains peaked in the mid 1990s and are generally lower today than they were for most of the past decade. The price of forages has been more stable as illustrated in Exhibit EBG-4. These data show that the price of corn silage has remained nearly constant, the price of primarily grass and grass mixtures (other hay) has declined since 1989 while the price of alfalfa hay has generally increased since 1991. The last 4-5 years have been especially difficult years for grain producers and is one of the reasons why many farmers in Utah have shifted from grain production to other crops.

Q. What has been happening to the prices farmers pay for inputs?

A. The prices of most farm inputs have generally risen but, there are exceptions. For example, Exhibit EBG-5 shows that the cost of farm labor has essentially doubled since 1987 and increased nearly a third since 1995. Diesel fuel has increased more than 50% since 1998 as shown on Exhibit EBG-6. These trends are different from interest rates for example, which have declined slightly (Exhibit EBG-7). Recent changes in input prices is perhaps best illustrated by fertilizer prices. The data in Exhibit EBG-8 indicates that fertilizer prices have been fairly stable. These historic trends were altered significantly in 2001 when prices for nitrogen (all forms) increased about 50 percent from the prices paid in 2000. As a result, farmers have either reduced their use of nitrogen or experienced a decline in profitability.

Q. What do you conclude from these figures and your knowledge of agriculture in general?

A. The profitability of crop enterprises which are the primary enterprises of concern to irrigators in Utah is generally low and is expected to remain low for the next few years.

Q. How do you suggest the Commission take into account this information?

A. Electric power is a major cost for many crop farmers. Obviously, if the Commission determines that PacifiCorp's costs are increasing, farmers should expect the price of their electric power to reasonably increase along with everyone else. Yet in determining just and reasonable rates, the Commission is empowered to take into consideration the economic impact of its rate decisions on specific classes of customers. Section 54-3-1 of the Code states:

> The scope of definition "just and reasonable" may include, but shall not be limited to, the cost of providing service to each category of customer, [and the] **economic impact of charges on each category of customer** * * *.

My chief concern as an agricultural economist who works with farmers in Utah is with PacifiCorp's proposal that recommends an increase for Schedule 10 users substantially above that proposed for other customer classes. This recommendation is apparently based on the Company's cost of service study, which shows that the Schedule 10 class is dramatically under-earning for the test year in this case. Such a disproportionate increase would be particularly detrimental to crop farmers who are already experiencing low net returns. It is also puzzling and counterintuitive to me that Schedule 10 costs for the test year are so out of line with the company's system average costs.

Q. Why do you say that the cost of service results for Schedule 10 are counterintuitive?

A. In Docket No. 97-035-01 the company's filed cost study claimed Schedule 10 had a revenue shortfall of 8.5%. It is my understanding that the Committee of Consumer Services expert Mr. Yankel in that case made certain unopposed adjustments to allocation factors used by the company which brought Schedule 10 costs much closer to average rate of return for that test year. In Docket No. 99-035-01 PacifiCorp filed a cost study for the calendar years 1996 through 1998. This study showed Schedule 10 with a .6% revenue surplus in 1996, a 2.4% shortfall in 1997, and a 1.26% shortfall for 1998. Now in this docket, the company's cost of service study results show Schedule 10 slipping precipitously to a revenue shortfall 12.7% for the test year. I am not expert in how cost studies are developed for public utilities, but there are no empirical data I'm aware of that would explain such a dramatic increase in costs for irrigation customers relative to other customer classes. To the contrary, data provided to me by Mr Yankel indicates that the Schedule 10 total load has been relatively flat and even declining in recent years, except for the test year in this case, which has a large unexplained surge in usage for Schedule 10 above historical levels. Data from the 1997 Census of Agriculture indicates that the number of irrigated farms declined between 1992 and 1997 while the number of acres that were irrigated in Utah increased by about 6 percent. It should also be noted that the increase in acreage occurred at the same time that energy use by Schedule 10 users declined. These trends suggest that the methodology used in PacifiCorp's cost studies must be attributing costs to Schedule 10 users that are not consistent with a decline in the number of farms and energy used by this class of users.

Q. Now that it appears PacifiCorp has slipped from a status of overcapacity to capacity scarcity, do you have any recommendations to the Commission on how Schedule 10 rates could be structured to promote off-peak usage?

A. Yes. The Commission should first consider reestablishing interruptible rates like those offered in the old Class B and C options that were eliminated in the 1997 rate case. Approximately two-thirds of the irrigators in the state were on an interruptible tariff before these classes were eliminated, and many irrigators would likely choose this alternative again if it was available. This has the possibility of a net gain to the system because many farmers can withstand the loss of power for short periods of time when the demand for other uses are high, provided the savings are great enough in the long run to pay for the loss of power in the short run.

Q. What other alternatives have been considered by farmers who use electricity to pump water for irrigation?

A. The Commission should also consider the possibility of adjusting the service territory of PacifiCorp to shift some irrigation loads in rural areas to rural cooperatives. Meetings were held this spring with representatives of the Utah Rural Electrical Association and the Utah Farm Bureau pumpers committee. Some of these rural electrical coops have excess capacity, commonly service compatible rural communities/farmers, and have some interest in providing power to farmers and others in rural communities that are currently being served by PacifiCorp. This is particularly true in those areas that are adjacent to areas that are currently being served by a rural electrical cooperative. For example, some farmers obtain power from both PacifiCorp and a rural cooperative because they have farms in areas that are served by both entities. Farmers in rural areas of the state have been particularly interested in the price of power from PacifiCorp because the rates charged by the rural coops are relatively low and are not expected to increase in the short run. It might be a win/win situation to shift some of the rural loads from PacifiCorp to one or more of the rural cooperatives.

Q. Does this conclude your testimony?

A. Yes.

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	:	Docket Nos. 01-035-01

I hereby certify that I mailed a true and correct copy of the PREFILED DIRECT TESTIMONY OF DR. BRUCE GODFREY, this 18TH day of November, 2012, postage prepaid, to the following:

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