

1                                   **REBUTTAL TESTIMONY OF KEVIN C. HIGGINS**

2

3   **Q.    Please state your name and business address.**

4    A.           Kevin C. Higgins, 39 Market Street, Suite 200, Salt Lake City, Utah,  
5           84101.

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

7    A.           I am a Principal in the firm of Energy Strategies, LLC. Energy Strategies,  
8           LLC is a private consulting firm specializing in the economic and policy analysis  
9           applicable to energy production, transportation, and consumption.

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

11   A.           My testimony is being sponsored by Utah Association of Energy Users  
12           Intervention Group (UAE).

13   **Q.    Are you the same Kevin C. Higgins who has filed direct testimony in this  
14           proceeding?**

15   A.           Yes, I am.

16   **Q.    What is the purpose of your rebuttal testimony?**

17   A.           My rebuttal testimony responds to cost-of-service and rate design issues  
18           that appear in the direct testimonies of Rebecca Wilson for the Division of Public  
19           Utilities; George Sterzinger for the Committee of Consumer Services; Charles E.  
20           Johnson for the Salt Lake Community Action Program, Crossroads Urban Center,  
21           and Legislative Watch; and Jeff Burks and Dave Nichols for the Utah Energy  
22           Office and James F. Gilliam for the Land and Water Fund of the Rockies.

23   **Q.    Please summarize the recommendations in your rebuttal testimony.**

1 A. I recommend that the Commission approve the 138 kv rate schedule  
2 proposed by Ms. Wilson, although I offer some observations and clarifications  
3 with respect to her proposed new rate schedule. I urge the Commission to reject a  
4 number of cost allocation and rate design proposals by Mr. Sterzinger and Dr.  
5 Johnson. With respect to the Demand-Side Resources (DSR) testimony presented  
6 by Mr. Burks, Mr. Nichols and Mr. Gilliam, I recommend that program design  
7 and cost recovery issues for DSR programs be determined in appropriate dockets  
8 established for those specific purposes.

9 **Rebecca Wilson**

10 **Q. Have you reviewed Ms. Wilson’s proposal for a new rate schedule for**  
11 **customers taking delivery at 138 kv?**

12 A. Yes, I have. PacifiCorp proposed to change Schedule 9 to prohibit service  
13 to customers with loads in excess of 50 MW, without offering a substitute  
14 schedule [see William R. Griffith direct testimony, p. 6-7 ]. Ms. Wilson opposes  
15 that proposal and also proposes a new cost-based firm rate schedule for  
16 customers taking service at 138 kv.

17 **Q. What is your assessment of Ms. Wilson’s proposal for a new rate for**  
18 **customers taking delivery at 138 kv?**

19 A. I agree with Ms. Wilson that PacifiCorp has not justified its proposal to  
20 eliminate a firm tariff rate option for larger customers. In addition, I agree with  
21 Ms. Wilson that a firm tariff schedule for customers taking service at 138 kv  
22 should reflect rates that are lower than Schedule 9 rates.

1           Customers taking service at high-voltage levels, such as 138 kv, have cost  
2 characteristics that differ significantly from customers taking service at lower  
3 voltage levels. For this reason, I agree with the concept Ms. Wilson has proposed  
4 – namely, the development of a cost-based rate schedule for customers taking  
5 service at 138 kv. I also agree with the basic objective she has pursued in her  
6 attempt to derive an appropriate cost-based rate, which is to scale down Schedule  
7 9 rates to capture the cost-of-service differential associated with 138 kv service.  
8 For purposes of this case, I recommend adoption of Ms. Wilson’s proposed rate  
9 schedule.

10           Certain clarifications should be made, however, with respect to Ms.  
11 Wilson’s proposal. In particular, it is important to note that the derived costs  
12 under the proposed new rate schedule are based on firm service, and thus, the new  
13 tariff would provide firm service. Second, Ms. Wilson’s proposal does not attempt  
14 to preclude customers with unique operating characteristics from negotiating  
15 special contracts with the utility. It is important to ensure that this flexibility be  
16 retained. Customers with unique operating, service, or cost characteristics,  
17 including those who can offer voluntary service interruptions or other system  
18 benefits, must remain free to negotiate appropriate rates and terms with  
19 PacifiCorp that reflect their unique situations. Any such contracts will, of course,  
20 remain subject to Commission approval.

21 **George Sterzinger**

22 **Q.    Have you reviewed the direct testimony submitted by Committee witness**  
23 **George Sterzinger?**

1 A. Yes, I have.

2 **Q. What is your assessment of the cost allocation proposals made by Mr.**  
3 **Sterzinger?**

4 A. Mr. Sterzinger has proposed a number of different changes to PacifiCorp's  
5 cost allocation, each of which appears designed primarily to improve the cost  
6 allocation for low-load-factor customer classes at the expense of other rate  
7 classes. Mr. Sterzinger's analysis contains serious errors of commission and  
8 omission, and his recommendations in this case should be rejected.

9 My analysis of Mr. Sterzinger's testimony focuses on three primary areas:  
10 (1) his inter-class allocation proposal, (2) his proposed treatment of revenue  
11 credits, and (3) his recommendations for special contracts.

12 **Q. Please describe Mr. Sterzinger's inter-class allocation proposal.**

13 A. On page 11 of Mr. Sterzinger's testimony, he recommends that, if the  
14 Committee's position on net power cost is adopted by the Commission, the  
15 resulting rate reduction should be spread on an equal percentage basis to most rate  
16 classes. He argues, however, that if PacifiCorp's position on net power cost is  
17 adopted by the Commission, the resulting rate increase should not be spread on an  
18 equal percentage basis for most rate classes (as proposed by PacifiCorp), but  
19 rather by assigning 50 percent of the increase to each class on an equal percentage  
20 basis and 50 percent on an equal per-kwh basis. Not surprisingly, Mr. Sterzinger's  
21 proposed allocation would have the effect of reducing the rate increase for  
22 relatively low-load-factor customer classes, such as Residential Rate 1, and  
23 increasing rates for higher-load-factor customer classes.

1 **Q. What is Mr. Sterzinger’s justification for his proposed inter-class cost**  
2 **allocation?**

3 A. Mr. Sterzinger’s justification is his view that the main cause of a  
4 significant rate increase in this case would be production-related, and that such an  
5 increase should not result in a higher per-kwh increase for customers who have  
6 relatively large distribution components in their rates.

7 **Q. Do you agree with this view?**

8 A. No, I do not.

9 **Q. Why do you disagree?**

10 A. Mr. Sterzinger’s analysis ignores the fact that the various customer classes  
11 are starting with unequal rates of return. Even if an *incremental* cost increase were  
12 entirely production-related, the cost-of-service analyses in this case show that  
13 customer classes are not currently making equal contributions to *total cost*  
14 recovery. In particular, the Division’s cost-of-service study shows that  
15 Residential Rate 1 is providing below-average returns. By ignoring the relative  
16 starting positions of the various rate classes, Mr. Sterzinger’s approach largely  
17 ignores cost-of-service analysis as a basis for spreading any large potential rate  
18 increase – a serious flaw in his recommendation. Instead, he offers an ad hoc,  
19 energy-weighted alternative. I recommend that his proposal for inter-class cost  
20 allocation of a large potential rate increase be rejected.

21 **Q. Turning now to the subject of revenue credits, can you comment on Mr.**  
22 **Sterzinger’s recommendations?**

1 A. Yes. Mr. Sterzinger makes a number of assertions and recommendations  
2 concerning the treatment of revenue credits. His testimony on this subject  
3 contains a number of misstatements of fact and errors of omission. In the rebuttal  
4 that follows, I will re-state the salient features of his argument and point out the  
5 errors and problems with his proposal.

6 **Q. Please proceed.**

7 A. Let me begin with Mr. Sterzinger's discussion of the treatment of revenue  
8 credits with respect to special contracts. Proceeding through his testimony, Mr.  
9 Sterzinger makes the following statements in sequence:

10 (1) "...[R]evenue from the wholesale sales is allocated to Special Contract  
11 Customers." [p. 14, line 23 – p. 15, line 1]

12 (2) "...[N]either [Special Contracts nor wholesale sales] are assigned or  
13 allocated capacity costs of generation." [p. 15, lines 7-9]

14 (3) "The \$11 million that is allocated to Special Contracts under the  
15 Company's methodology should be reallocated to the other customer  
16 classes that do pay a fixed share of capacity costs." [p. 15, lines 15-17]

17 In this sequence of statements, Mr. Sterzinger begins with an unduly broad  
18 statement regarding the revenue credit treatment of special contracts, moves to an  
19 incorrect assertion of fact regarding the allocation of capacity costs, and then  
20 concludes with a recommendation to reallocate revenue credits to the benefit of  
21 his clients.

22 **Q. What is "unduly broad" about the statement that "revenue from the**  
23 **wholesale sales is allocated to Special Contract Customers"?**

1 A. This statement is unduly broad because revenue from wholesale sales is  
2 *not* allocated to special contract customers *generally*, but only to *firm* special  
3 contract customers, who represent a relatively small percentage of special contract  
4 revenue and generation requirements. Mr. Sterzinger’s broad statement gives the  
5 reader the impression that revenue credits are being allocated also to *non-firm*  
6 special contract customers (who represent the majority of special contract  
7 revenue), when in fact no allocation of revenue credits to non-firm special  
8 contract customers takes place in the cost of service studies before the  
9 Commission.

10 **Q. What about Mr. Sterzinger’s statement that special contracts are not**  
11 **assigned or allocated capacity costs of generation?**

12 A. Mr. Sterzinger is simply wrong on this point. *Firm* special contract  
13 customers – the ones who receive the revenue credits in question – *are* allocated  
14 capacity costs of generation in the cost of service studies. This is shown in Mr.  
15 Taylor’s cost of service study, UP&L Exhibit DLT-3, Tab 4.2, and Dr. Nelson’s  
16 cost of service Study, Division Exhibit 11.3.

17 **Q. Please comment on Mr. Sterzinger’s recommendation that the \$11 million**  
18 **that is allocated to Special Contracts should be “reallocated to the other**  
19 **customer classes that do pay a fixed share of capacity costs.”**

20 A. This recommendation is obviously a non-sequitur, as the customer class  
21 from which the revenue credit is being expropriated under Mr. Sterzinger’s  
22 proposal – the firm special contract class – is allocated capacity costs in the cost

1 of service studies. Moreover, there is a further problem with Mr. Sterzinger's  
2 recommendation.

3 **Q. What is that?**

4 A. Mr. Sterzinger's recommendation is flawed by a significant error of  
5 omission. Even if, for some reason, one decided to remove the revenue credit that  
6 is allocated to firm special contract customers, these customers are also being  
7 allocated over \$12 million in *purchased power costs*. [See PacifiCorp Exhibit  
8 DLT-3, Tab 4.1, p. 5] Mr. Sterzinger apparently wishes to continue to have firm  
9 special contract customers allocated *costs* associated with PacifiCorp's wholesale  
10 purchases while depriving them of any revenue credit from wholesale sales. This  
11 highly selective approach is clearly inequitable. I recommend that the  
12 Commission reject his recommendation regarding the revenue credit treatment of  
13 special contract customers.

14 **Q. Do you wish to comment on any other revenue credit issues in Mr.  
15 Sterzinger's testimony?**

16 A. Yes. Mr. Sterzinger points out that in classifying Sales for Resale revenue  
17 credits, PacifiCorp uses a classification in its Utah inter-class allocation that  
18 differs from the classification used in its inter-jurisdictional allocation. Namely, in  
19 the Utah inter-class allocation, 87 percent of the revenue credit is allocated using  
20 the SG factor (75 percent demand, 25 percent energy), whereas in the inter-  
21 jurisdictional allocation, 98 percent of the revenue credit is allocated using the SG  
22 factor. Mr. Sterzinger recommends changing the classification used in the Utah  
23 inter-class allocation to match the inter-jurisdictional allocation.



1 **Q. What does all of this mean?**

2 A. First, it is useful to offer a word about the end game here. All other things  
3 being equal, advocates for customers with relatively low load factors (such as  
4 residential customers) prefer to have *costs* allocated with a weighting toward  
5 *energy* usage (where the customers' usage is relatively low compared to other  
6 classes), but *revenues* allocated in an *opposite* fashion, with a weighting toward  
7 *demand* (where the customers' usage is relatively high compared to other classes).  
8 This rate case is no different. Predictably, the effect of Mr. Sterzinger's  
9 recommendation here would be to increase the revenues credited to low-load-  
10 factor customers.

11 Now, I will turn to Mr. Sterzinger's observation about inconsistency. First,  
12 I note that concern for consistency between jurisdictional and class cost-of-service  
13 is not a new issue for Utah stakeholders. This specific topic was addressed in the  
14 "Utah Allocation Task Force Report," issued in December 1999, following a  
15 debate on this subject during the 1997 PacifiCorp rate case. As documented in the  
16 task force report [p. 13], it is clear that the major consistency concern was  
17 consistency between the demand/energy allocation of Sales for Resale *revenues*  
18 and the demand/energy allocation of the *costs* of making those sales. I agree with  
19 that concern. As a practical matter, resolving this concern means ensuring  
20 consistency between Sales for Resale revenue credits and Purchased Power costs.  
21 In other words, equitable treatment of Utah customers requires that the  
22 demand/energy allocation used for Sales for Resale credits be consistent with the  
23 demand/energy allocation used for Purchased Power costs.

1 **Q. Is PacifiCorp’s allocation of Sales for Resale revenues and Purchased Power**  
2 **costs consistent with this view of equitable treatment of Utah customers?**

3 A. Yes, it is. In this docket, for inter-class allocation purposes, PacifiCorp has  
4 used the same classification for Sales for Resale credits as it has for Purchased  
5 Power costs: 87 percent SG, and 13 percent energy. [See DLT-3, Tab 4.1.  
6 Compare p. 3, col. D, lines 144-46 to p. 5, col. D, lines 321-23.]

7 **Q. Does Mr. Sterzinger’s proposal for changing the demand/energy**  
8 **classification promote the equitable treatment of Utah customers?**

9 A. No, it does not. Mr. Sterzinger’s proposal would result in a disparity  
10 between the allocation used for revenue credits and the allocation used for  
11 purchased power costs. This disparity would unfairly favor lower-load-factor  
12 customers at the expense of higher-load-factor customers, without justification.

13 **Q. Turning now to Mr. Sterzinger’s discussion of special contracts, do you**  
14 **agree with Mr. Sterzinger’s characterization of the “losses” associated with**  
15 **these contracts?**

16 A. No. On pages 24-25 of his confidential testimony, Mr. Sterzinger  
17 compares the average revenue received from special contracts – the majority of  
18 which is non-firm power – with a per-unit generation cost from PacifiCorp’s cost-  
19 of-service study, as well as with expected power purchase costs. Mr. Sterzinger’s  
20 comparisons are invalid. The comparison to generation costs is not on an apples-  
21 to-apples basis. The fully-embedded PacifiCorp generation cost reflects firm  
22 service, whereas the special contract sales are primarily non-firm. Non-firm

1 contracts, by design, are intended to cover the utility's *variable* cost, while  
2 making a contribution toward fixed cost.

3 Similarly, the comparison to purchased power costs is inappropriate.  
4 Special contract customers are part of the company's native retail load and the  
5 allocated cost of serving such customers cannot properly be determined by a  
6 simple comparison to short-term market prices that may be encountered in serving  
7 wholesale customers.

8 In addition, PacifiCorp's net power costs in this case are being vigorously  
9 challenged by the Committee, the Division, UAE, and other parties, as costs that  
10 are unduly inflated by PacifiCorp's wholesale sales obligations during a period of  
11 abnormally high market prices. If, instead, special contracts are evaluated in terms  
12 of the cost of PacifiCorp's own resources, they will not show losses as depicted  
13 by Mr. Sterzinger.

14 **Q. On page 25 of his testimony, Mr. Sterzinger states that PacifiCorp has been**  
15 **involved in “buying back” special contracts from Utah customers. Do you**  
16 **believe this is an accurate characterization?**

17 A. No, it is not. In response to the extremely high wholesale prices  
18 experienced in the western market over the past year, PacifiCorp aggressively  
19 pursued load-reduction programs with its retail customers. In that connection,  
20 certain special contract customers negotiated demand reduction agreements with  
21 PacifiCorp. The customers reduced energy consumption – and the output of their  
22 final products – in exchange for compensation designed to make the utility (and  
23 by extension the other customers it serves) better off. To characterize these

1 reciprocal arrangements as “contract buybacks” is misleading and unhelpful to  
2 any issue involved in this case.

3 **Q. On page 26 of his testimony, Mr. Sterzinger recommends that the**  
4 **Commission should “articulate now that [Special Contracts] are not**  
5 **economically firm contracts,” and he goes on to describe the circumstances**  
6 **under which the Commission should allow PacifiCorp to interrupt service**  
7 **beyond what may be permitted in the customers’ contracts. Do you think this**  
8 **is good advice?**

9 A. No. Mr. Sterzinger is recommending that special contracts be treated as  
10 economically interruptible – presumably without regard for any applicable  
11 contractual language. Special contracts, each of which has been specifically  
12 approved by the Commission, contain a variety of negotiated terms and  
13 provisions. Some of the contracts identify circumstances under which the  
14 delivery of power may be interrupted; some do not. The company cannot simply  
15 ignore the terms of these contracts and I do not believe it is sound advice to  
16 recommend that the Commission require PacifiCorp to abrogate them.

17 **Q. Do you wish to comment about any other aspects of Mr. Sterzinger’s**  
18 **discussion of Special Contracts?**

19 A. On page 26, lines 14-20, of his direct testimony, Mr. Sterzinger argues that  
20 current special contracts should, in essence, be re-priced to pass through full  
21 incremental costs based on wholesale prices during certain periods. In his view,  
22 Special Contract customers are always to be treated as “last in” and their usage  
23 priced using the most expensive power. His approach fails to acknowledge that

1 special contract customers are themselves native load customers who are  
2 purchasing power from a monopoly provider that has an obligation to serve, and  
3 that these customers are entitled to receive service at just and reasonable rates. His  
4 recommendations regarding the treatment of special contract customers should be  
5 rejected.

6 **Charles E. Johnson**

7 **Q. On pages 25-31 of his direct testimony, Charles E. Johnson recommends that**  
8 **the Commission require all Schedule 6, Schedule 9 and special contract**  
9 **customers who have the appropriate metering to pay time-of-day rates. Do**  
10 **you agree with his proposal?**

11 A. No. While I support the use of rate designs that improve price signals,  
12 forcing all Schedule 6, Schedule 9, and special contract customers onto time-of-  
13 day rates without careful analysis of the cost and other consequences would be  
14 rash and imprudent. There could be serious cost consequences and dislocations  
15 for individual customers forced to undergo such a rate design change. Moreover,  
16 Dr. Johnson has failed to properly account for other important considerations.

17 **Q. What other considerations has Dr. Johnson not taken into account?**

18 A. An especially important consideration is cost-of-service. The purpose of  
19 Dr. Johnson's recommendation is to use price signals to change customer energy  
20 usage patterns in such a way as to lower aggregate generation costs: absent the  
21 expectation of such price-induced usage changes, there would be little value in  
22 such a recommendation. Yet the customer classes targeted by Dr. Johnson's  
23 recommendation are being allocated costs in this docket based on test year data –

1 which in turn is based on existing/historical rate design and usage patterns.  
2 Fairness dictates that if the rate design for certain customer classes were to be  
3 radically altered to induce generation-cost-saving behavior, then the cost-of-  
4 service analysis would also have to be adjusted to reflect the changed usage  
5 pattern expected. Otherwise, these customer classes would be over-allocated  
6 costs.

7 **Q. What is your recommendation to the Commission regarding Dr. Johnson's**  
8 **mandatory time-of-day rate proposal?**

9 A. The issue should be rejected absent a detailed analysis of all relevant  
10 factors, including, but not necessarily limited to: (1) an evaluation of the hours  
11 that comprise the appropriate peak period(s), (2) the impact on various customer  
12 sub-groups of enacting mandatory time-of-day rates, and (3) an evaluation of the  
13 cost-of-service adjustments needed to properly allocate costs if time-of-day rates  
14 were to be mandated.

15 **Q. Are there other aspects of time-of-day pricing that would be worth**  
16 **investigating?**

17 A. Yes. It may be worthwhile to evaluate whether current voluntary programs  
18 should be modified to shorten the peak period. Such a change may provide the  
19 opportunity for improving price signals to program participants without creating  
20 the customer dislocations that would likely arise from a mandatory program.

21 **Demand-Side Resource Issues**

22 **Q. Do you have any comments on the rate design testimony of the Utah Energy**  
23 **Office and the Land and Water Fund of the Rockies?**

1 A. Yes. Mr. Burks, Mr. Nichols and Mr. Gilliam all address rate design  
2 issues relating to Demand-Side Resource (DSR) programs. Generally, each  
3 recommends the use of a “tariff rider” for cost recovery of DSR costs. Each also  
4 discusses certain specifics of program design, such as annual  
5 adjustments/balancing accounts, a shared savings mechanism, and a self-direction  
6 option. Mr. Nichols even provides specific per-kwh charges that could be  
7 imposed on various rate schedules to recover a specific level of DSR funding.

8 In my view, debating the details of DSR cost recovery is premature and  
9 inappropriate in this case. DSR program design and appropriate cost recovery  
10 mechanisms should not be decided here in the abstract, but rather should be  
11 resolved as part of other dockets in which specific DSR programs are designed  
12 and approved, and/or in which specific amounts of cost recovery and specific cost  
13 recovery mechanisms are evaluated and approved.

14 The referenced testimony supports the use of “tariff riders” to fund DSR  
15 programs, but any funding mechanism will have relative drawbacks and  
16 advantages. The imposition of any funding mechanism for DSR requires a  
17 detailed analysis in the context of specific DSR programs, and should be deferred  
18 for consideration to the appropriate dockets.

19 **Q. Does this conclude your rebuttal testimony?**

20 A. Yes, it does.