Gary A. Dodge, #0897
HATCH, JAMES & DODGE
10 West Broadway, Suite 400
Salt Lake City, UT 84101
Telephone: 801-363-6363
Facsimile: 801-363-6666
Email: gdodge@hjdlaw.com
Attorneys for UAE Intervention Group

BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

In the Matter of the Application of PacifiCorp for Approval of Its Proposed Electric Service Schedules & Electric Service Regulations	DOCKET NO. 06-035-21

PREFILED DIRECT TESTIMONY OF KEVIN C. HIGGINS

[TEST PERIOD]

The UAE Intervention Group hereby submits the Prefiled Direct Testimony of Kevin C. Higgins on test period issues.

DATED this 9th day of June, 2006.

____
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 9th day of June, 2006 to the following:

Edward A. Hunter
Jennifer Martin
STOEL RIVES LLP
201 South Main Street, Suite 1100
Salt Lake City, UT 84111
eahunter@stoel.com
jhmartin@stoel.com
Attorneys for PacifiCorp

Michael Ginsberg
Patricia Schmid
ASSISTANT ATTORNEY GENERAL
500 Heber M. Wells Building
160 East 300 South
Salt Lake City, UT 84111
mginsberg@utah.gov
pschmid@utah.gov
Attorneys for Division of Public Utilities

Reed Warnick
Paul Proctor
ASSISTANT ATTORNEY GENERAL
160 East 300 South, 5th Floor
Salt Lake City, UT 84111
rwarnick@utah.gov
pproctor@utah.gov
Attorneys for Committee of Consumer Services

F. Robert Reeder
Vicki M. Baldwin
PARSONS BEHLE & LATIMER
One Utah Center
201 South Main Street, Suite 1800
P.O. Box 45898
Salt Lake City, UT 84145-0898
BobReeder@pblutah.com
VBaldwin@pblutah.com
Attorneys for UIEC

Dale F. Gardiner
PARRY ANDERSON & GARDINER
60 East South Temple, #1200
Salt Lake City, Utah 84111
dfgardiner@parrylaw.com
Attorneys for AARP

Thomas W. Forsgren
2868 Jennie Lane
Holladay, Utah 84117
twforsgren@msn.com
Attorneys for AARP

Michael L. Kurtz
Kurt J. Boehm
BOEHM, KURTZ & LOWRY
36 East Seventh Street, Suite 1510
Cincinnati, Ohio 45202
Mkurtz@bkllawfirm.com
kboehm@bkllawfirm.com
Attorneys for Kroger Company

C. Scott Brown (4802)
Colleen Larkin Bell (5253)
180 East 100 South
P.O. Box 45360
Salt Lake City, Utah 84145-0360
scott.brown@questar.com
colleen.bell@questar.com
Attorneys for Questar Gas Company

Peter J. Mattheis
Eric J. Lacey
BRICKFIELD BURCHETTE RITTS & STONE
1025 Thomas Jefferson Street, N.W.
800 West Tower
Washington, D.C. 20007
PJM@bbrslaw.com
Attorneys for Nucor Steel

Gerald H. Kinghorn
Jeremy R. Cook
PARSONS KINGHORN HARRIS
111 East Broadway, 11th Floor
Salt Lake City, UT 84111
ghk@pkplawyers.com
Attorneys for Nucor Steel

Marco B. Kunz
451 S. State Street, # 505A
Salt Lake City, UT
marco.kunz@slcgov.com
Attorneys for Million Solar Roofs Partnership/Salt Lake City Corporation

Lt Col Karen White
Capt Damund E. Williams
AFLSA/ULT
Utility Litigation Team
139 Barnes Drive, Suite 1
Tyndall AFB, FL 32403-5319
Karen.White@tyndall.af.mil
Damund.Williams@tyndall.af.mil
Attorneys for FEA

Thomas E. Bingham
Utah Manufacturer's Association
136 E. South Temple, Suite 1740
Salt Lake City, UT 84111
tom@umaweb.org

Lee R. Brown
US Magnesium LLC
238 North 2200 West
Salt Lake City, UT 84116
lbrown@usmagnesium.com

Utah Ratepayers Alliance
Betsy Wolf
764 South 200 West
Salt Lake City, UT 84101
bwolf@slcap.org

Arthur F. Sandack
IBEW Local 57
8 East Broadway, Ste 510
Salt Lake City, Utah 84111
asandak@msn.com

Ronald J. Day
Central Valley WRF
800 West Central Valley Road
Salt Lake City, UT 84119
dayr@cvwrf.org

Roger J Ball
1375 Vintry Lane
Salt Lake City, Utah 84121
roger.ball@gmail.com

PREFILED DIRECT TESTIMONY

Of

KEVIN C. HIGGINS

[Test Period]

On behalf of UAE Intervention Group

In the Matter of the Application of PacifiCorp for Approval of Its Proposed Electric Service Schedules & Electric Service Regulations

Docket No. 06-035-21

June 9, 2006

<u>Introduction</u>

Q. Please state your name and business address.

A. Kevin C. Higgins, 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 Principal in the firm of 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. My academic background is in economics, and I have completed all coursework and field examinations toward a Ph.D. in Economics at the University of Utah. In addition, I have served on the adjunct faculties of both the University of Utah and Westminster College, where I taught undergraduate and graduate courses in economics. I joined Energy Strategies in 1995, where I assist private and public sector clients in the areas of energy-related economic and policy analysis, including evaluation of electric and gas utility rate matters.

Prior to joining Energy Strategies, I held policy positions in state and local government. From 1983 to 1990, I was economist, then assistant director, for the Utah Energy Office, where I helped develop and implement state energy policy. From 1991 to 1994, I was chief of staff to the chairman of the Salt Lake County Commission, where I was responsible for development and implementation of a broad spectrum of public policy at the local government level.

Q. Have you previously testified before this Commission?

A. Yes. Since 1984, I have testified at least fifteen times before the Utah Public Service Commission on electricity and natural gas matters.

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

A. Yes. I have testified in over forty other proceedings on the subjects of utility rates and regulatory policy before state utility regulators in Alaska, Arizona, Colorado, Georgia, Idaho, Illinois, Indiana, Kansas, Michigan, Minnesota, Nevada, New York, Ohio, Oregon, South Carolina, Washington, West Virginia, and Wyoming.

A more detailed description of my qualifications is contained in UAE Exhibit TP1.1 (KCH-1), attached to my direct testimony.

Overview and conclusions

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

A. My testimony addresses the matter of the most appropriate test period to be used in this general rate proceeding.

Q. What are your primary conclusions and recommendations?

A. I conclude that the best test period to be used in this general rate proceeding is Calendar Year 2006, consisting of the period January 1, 2006 through December 31, 2006. In my opinion, Calendar Year 2006 best reflects the conditions PacifiCorp will encounter during the period the rates will be in effect. Of the test periods for which data has already been filed in this case, the one that most closely corresponds to Calendar Year 2006 is the "Mid Period," consisting of October 1, 2005 through September 30, 2006.

Basis for Determining Test Period

Q. On what basis must test period be determined in Utah?

A. The determination of a public utility's test period is addressed in Section 54-4-4(3) of the Utah Code, which states:

> (a) If in the commission's determination of just and reasonable rates the commission uses a test period, the commission shall select a test period that, on the basis of the evidence, the commission finds best reflects the conditions that a public utility will encounter during the period when the rates determined by the commission will be in effect.
>
> (b) In establishing the test period determined in Subsection (3)(a), the commission may use:
>
> (i) a future test period that is determined on the basis of projected data not exceeding 20 months from the date that a proposed rate increase or decrease is filed with the commission under Section 54-7-12;
>
> (ii) a test period that is:
>
> (A) determined on the basis of historic data; and
> (B) adjusted for known and measurable changes; or
>
> (iii) a test period that is determined on the basis of a combination of :
>
> (A) future projections; and
> (B) historic data.
>
> (c) If pursuant to this Subsection (3), the commission establishes a test period that is not determined exclusively on the basis of future projections, in determining just and reasonable rates the commission shall consider changes outside the test period that:

(i) occur during a time period that is close in time to the test period;

(ii) are known in nature; and

(iii) are measurable in amount.

Q. Did the Legislature adopt intent language associated with this statute?

A. Yes. The Legislature adopted intent language stating:

> "The intent of the legislature in passing S.B. 61, Public Utility Related Amendments, is to have the Public Service Commission select a test period for setting utility rates based on the best evidence presented to the Public Service Commission without any presumption for or against either a historical or a future test period."

Q. Based on your experience in utility regulation, and without attempting to render a legal opinion, how do you interpret the plain language of this statute taken in combination with the Legislature's intent language?

A. There are three "generic" test period options available for setting rates in Utah, and the Commission is free to choose the best test period based on the evidence. Significantly, <u>there is no presumption either for or against an historical or future test period</u>. The particular importance of this latter statement is that an argument structured along the lines that "a future test period must be chosen because the rate effective period is in the future – and, by definition, a future period best reflects the future" is not sufficient grounds for determining the appropriate test period in Utah.

Q. Please explain.

A. Rate-effective periods are *always* in the future. Therefore, in determining test period, it is not valid to rely on the tautological assertions that "the future best reflects the future," or "the rate effective period best reflects the rate effective period," as reliance on such arguments equates to a presumption in favor of a future test period. Such a presumption would be inconsistent with the stated intent of the legislature. Moreover, such an argument attempts to deprive the Commission of the right to exercise its discretion to consider all of the relevant factual and policy issues inherent in a test year determination. The legislature clearly did not intend to deprive the Commission of its obligation and right to consider all relevant factors in selecting a test year.

Q. Has the Commission provided any guidance with respect to determination of test period?

A. Yes. In its order approving the test period stipulation in the previous PacifiCorp general rate case, issued October 20, 2004 in Docket No. 04-035-42, the Commission identified various factors that need to be considered in selecting a test period. The factors identified in the Commission's Order include the general level of inflation; changes in the utility's investment, revenues or expenses; changes in utility services; availability and accuracy of data to the parties; ability to synchronize the utility's investment, revenues and expenses; whether the utility is in a cost increasing or cost declining status; incentives to efficient management and operation; and length of time the new rates are expected to be in effect.

In that same order, the Commission also discussed some important policy concerns implicated by future test periods. These concerns include diminished economic examination and accountability, replacement of actual results of operations data with difficult-to-analyze projections, ability of parties to effectively analyze the Company's forecasts, dampening of the efficiency incentive of regulatory lag, playing to the

Company's strength from control of critical information, and shifting of the risks of the future to ratepayers.

Q. Do you share these concerns expressed by the Commission concerning future test periods?

A. Yes, I do. Let me also state the obvious: as a general matter, making forecasts in the energy business often proves to be an exercise in humility. It is well understood that energy prices are volatile and difficult to forecast with accuracy. Further, I acknowledge that the Calendar Year 2006 test period I am recommending relies entirely on projections of data, and from that standpoint, is also a future test period.[1] As such, it is subject to the concerns expressed by the Commission. However, I believe that these concerns are sufficiently mitigated by the fact that the Calendar Year 2006 forecasts are relatively close in time, and line up well with the start of the rate-effective period. I believe the concerns expressed by the Commission are more pertinent to a more "aggressive" future test period, such as that advocated in this proceeding by PacifiCorp, which extends well beyond the test period I am recommending.

<u>Test Period Proposed by PacifiCorp</u>

Q. What is PacifiCorp's proposal for the test period to be used in this proceeding?

A. PacifiCorp is proposing to use a test period ending September 2007 to support its adjusted rate increase request of $194 million. The Company's rate increase request was filed in early March 2006, and the Company's proposed test period ends about 19 months

[1] The 2006 data filed by PacifiCorp in its application for a rate increase are projections.

later. This means that its proposed test period extends nearly to the maximum point in the future allowed by Utah law.

Q. What is the relationship between PacifiCorp's proposed test period and the Company's historical costs and revenues?

A. As explained by various PacifiCorp witnesses, the Company prepared a Base Case using normalized historical data for the 12-month period ending September 2005. The Company's Base Case showed PacifiCorp experiencing a Utah revenue deficiency of $20 million.[2]

PacifiCorp then prepared a forecast of costs and revenues for the subsequent 12-month period ending September 2006, which I refer here to as the "Mid Period." As described in the pre-filed direct testimony of J. Ted Weston, this exercise included the development of a load forecast; forecasting of expected labor costs; application of inflation factors to non-labor operation, maintenance, administrative, and general expenses; and projection of net power costs using the Company's GRID model. In addition, as indicated by PacifiCorp witness Jeffrey K. Larsen, the Company used capital budgeting information to project plant-related costs. The Company also projected its capital structure and debt costs for the Mid Period.

To reach the Company's proposed test period, the Mid Period forecast was then extended for an additional full year; that is, an additional round of forecasts for inflation, labor costs, loads, net power costs, capital expenditures, debt costs, and capital structure were added to the Mid Period results.

[2] Exhibit UP&L__(JTW-2), BASE PERIOD, Tab 1, page 1.0

Q. Do you agree with PacifiCorp's conclusion that its proposed test period is the most appropriate for setting rates in this proceeding?

A. No, I do not. I believe that a future test period that is closer in time than PacifiCorp's proposed period is a more reasonable choice. A future test period such as Calendar Year 2006 will use one less round of forecasts and thus provide a more certain basis for establishing rates that would go into effect in December 2006. Further, under the Company's proposal, customers in December 2006 would be paying for capital investment that had not yet occurred – and might not occur as planned. In addition, customers would be paying for projected 2007 inflation before 2007 had even arrived. They would also be paying for expected labor cost increases before the employees received the raises in question. And they would be paying for the cost of equity infusions before the Company's shareholders provided the requisite additional capital. Such a result is inconsistent with the "used and useful" concept of utility regulation, is unfair to ratepayers, and is not good public policy.

Q. Are the arguments advanced by PacifiCorp witness Jeffrey K. Larsen against the use of a historical test period applicable to your proposal?

A. No. I am not proposing a historical test period – nor am I even proposing a hybrid of historical and projected data. Like PacifiCorp, I am proposing a future test period. The fundamental difference between our proposals lies in how far into the future we believe the test period projections should go.

Q. On page 13 of his pre-filed direct testimony, Mr. Larsen testifies that the performance of previous PacifiCorp test year forecasts relative to actual results cannot be fully evaluated at this point. Do you wish to comment?

A. I agree that the "jury is still out" on fully evaluating how well PacifiCorp's previous test period projections compare to actual results. Nevertheless, as I will show below, we can still draw some useful inferences from data available today.

Advantages of a Calendar Year 2006 Test Period

Q. You state that an advantage of a Calendar Year 2006 test period is that its projections are closer in time than PacifiCorp's proposal. Why is that an advantage?

A. Projections of prices, loads, and costs that are closer in time to the present will generally be more reliable than projections further out. As described above, PacifiCorp's forecast of its proposed test period utilizes a "Mid Period" forecast as a basic step, before adding an additional round of projections. Any errors in the Mid Period forecast will be built into the base from which the Company's proposed test period is projected. Further errors in the additional round of projections can have a compounding effect. In contrast, the Calendar Year 2006 projection would only extend three months beyond the Mid Period forecast.

Q. Are there other advantages to projections that are closer in time, besides reducing forecast error?

A. Yes. Besides forecasting economic variables, future test periods require projections of how rapidly the utility will implement its capital expenditure programs. In reality, these plans may not unfold as projected. According to Mr. Larson's testimony, the Company's capital expenditure projections for its proposed test period are comprised largely of budget targets by category, as opposed to specific projects. I see this as a disadvantage of using an aggressive future test period. In contrast, I believe a test period that employs a more near-term projection of a utility's capital expenditure program – when projects are known with greater specificity – will prove to be more reliable, and thus, more appropriate for ratemaking.

Q. Is there evidence that PacifiCorp's previous test year projections for capital expenditures in Utah have deviated from actual implementation?

A. Yes. In the previous general rate case, filed in August 2004, PacifiCorp used a projected test period of April 2005 through March 2006. In the current rate case, PacifiCorp filed actual results through September 2005; as such, that month provides the most recent actual plant balances in the current filing.

As part of its 2004 filing, PacifiCorp projected that Utah Distribution Plant would increase by a net amount of $98 million over the April 2005 to March 2006 test period. This information is reproduced in UAE Exhibit TP1.2 (KCH-2). In that proceeding, the Company projected that by September 2005, the Distribution Plant balance would be $1.846 billion. The filing in this case shows the actual plant balance for September 2005 was $1.825 billion – more than $20 million short of the test year projection in the previous rate case. This shortfall represents more than 20 percent of the increase in Utah Distribution Plant that was projected in the previous case.

This result illustrates one of my chief concerns in using an aggressive future test period. In monitoring the utility's performance in meeting its capital investment forecast, it is natural for parties to focus on the timing of "big-ticket" items such as new generation plant. However, distribution investment involves a much larger volume of smaller projects and is less likely to gain equal notice. Yet distribution investment involves significant rate base dollars and is assigned 100 percent situs. If PacifiCorp's proposed test period is adopted in this case, and PacifiCorp again misses the distribution investment mark by over 20 percent, Utah ratepayers will wind up overcharged.

Q. Does forecast error have other implications for costs charged to Utah customers, aside from the direct impacts that occur when expenses are over-estimated?

A. Yes. There are special concerns that arise because PacifiCorp is a multi-jurisdictional utility. Forecast error can also result in Utah being allocated a greater share of interjurisdictional costs than is warranted. The allocation of interjurisdictional costs involves not just incremental costs or investment, but more significantly, it involves the allocation of all the generation and transmission costs and plant of the entire six-state system. Consequently, if Utah's allocated share of interjurisdictional costs increases, a greater portion of the existing system costs are shifted to Utah. If such a shift occurs as a result of forecast error, Utah customers may be unfairly penalized.

Q. Is there evidence that the use of an aggressive future test period in the past would have produced an unwarranted increase in Utah's interjurisdictional cost allocation?

A. Yes. One of the most important allocation factors used in spreading interjurisdictional costs across the PacifiCorp states is the SG Allocation Factor. The SG Allocation Factor is derived from an analysis of the system's monthly coincident peaks (or "12 CP"). It is used to allocate a significant portion of generation and transmission plant and fixed O&M expenses.

As I indicated above, in the previous general rate case, PacifiCorp proposed a future test period of April 2005 through March 2006. In that case, PacifiCorp's projections of system coincident peak loads resulted in Utah receiving an SG Allocation Factor of 41.9081%[3]. The passage of time is showing this to be too high. The Company's filing in this case shows that the SG Allocation Factor for Utah over the historical period October 2004 through September 2005 was only 39.6596 %[4] – a material difference when it comes to allocating billions of dollars of plant and expenses.

To make a more direct comparison to the April 2005 through March 2006 test period, I combined the historical data for the period April 2005 through September 2005 with PacifiCorp's Mid Period projections for October 2005 through March 2006. This is shown in UAE Exhibit TP 1.3 (KCH-3), in which I calculate an updated SG Allocation Factor for the test period April 2005 through March 2006 of 40.1628%. This result can be compared directly to the Company's projection of the SG Allocation Factor from the

[3] Exhibit UP&L ___ (JTW-1) Tab 10, page 10.1.1 (UT Docket No. 04-035-42)
[4] Exhibit UP&L__(JTW-2), BASE PERIOD, Tab 10.1, page 10.1.1.

prior rate case of 41.9081%. Again, this is a significant difference in light of the billions of dollars of plant and expenses that are being allocated on the PacifiCorp system.

Q. The Commission has indicated that one of the factors for determining test period is the ability to synchronize the utility's investment, revenues and expenses. Under your proposed test period, would these items be synchronized?

A. Yes. I am proposing a fully-projected test period that requires no out-of-period adjustments. As such, investment, revenues and expenses would be fully synchronized.

Q. In light of the fact that PacifiCorp has not filed a Calendar Year 2006 test period, how can your proposal be implemented?

A. As I discussed above, PacifiCorp has filed a Mid Period test year, extending from October 2005 through September 2006, and its proposed future test period, extending from October 2006 through September 2007. Consequently, all the information is available for a Calendar Year 2006 test period. If my proposal is adopted, I recommend that PacifiCorp be required to re-present its rate case filing by consolidating the last nine months of its Mid Period test year with the first three months of its Future test year. In the alternative, the Mid Period test year could be used as a proxy, with out of period adjustments through the end of Calendar Year 2006. Another alternative is to use the Mid Period test year, ending September 2006, which is also a fully-projected future test period.

Q. The Commission has indicated that other factors for determining test period include changes in the utility's investment, revenues, expenses or services. Does your proposed test period account for such changes?

A. Yes. My proposed test period would account for projected changes through December 31, 2006. This would line up well with the start of the rate-effective period that PacifiCorp has requested – December 11, 2006. My proposal would not account for projected changes that would occur in 2007 and beyond – nor do I believe it should.

Q. The Commission has also indicated that the availability and accuracy of data to the parties is a factor in determining test period. Do you wish to comment?

A. Based on the information I have reviewed in preparing this testimony, I believe that PacifiCorp has done a good job in making data available to the parties – a situation that was assisted by the information requirements for this case established in the settlement of the prior one. At this juncture of the rate case, I have not formed a complete opinion regarding the accuracy of the data presented by the Company. However, as I indicated earlier, the availability and accuracy of data are necessarily diminished as longer-term forecasts are used.

Q. The Commission has stated that the general level of inflation is a factor in determining test period. Do you wish to comment?

A. My interpretation of this statement is that in determining whether to adopt a historical test period, the Commission would consider whether a utility was experiencing significant inflationary pressures that would require appropriate adjustments to compensate for known increases in the price level. In adopting a prospective test period, this concern is addressed by making assumptions about inflation that are incorporated into the utility's forecasted costs.

However, I wish to add a caution regarding this practice, particularly as it relates to an aggressive future test period, such as PacifiCorp has proposed. As an economist, I have concerns about pricing formulations that reinforce inflation. This can occur when *projections* of inflation are built into formulas that are then used to set administratively-determined prices, such as utility rates. Such pricing mechanisms help to make inflation a self-fulfilling prophesy. As a matter of public policy, this is a concern. It is one thing to adjust for inflation; it is another to help guarantee it. This problem is less pronounced using the Calendar Year 2006 test period I have proposed.

Q. The Commission has also stated that it will consider whether the utility is in a cost increasing or cost declining status. Please comment on the appropriateness of your proposal with regard to this factor.

A. In general, a utility that is facing increasing costs will benefit from – and therefore, prefer – an aggressive future test period. Conversely, a utility facing a declining cost situation will benefit from – and prefer – an historical test period.

The “near-term” projected test period I am proposing sits between these two extremes. In my view, it is a reasonable mechanism for addressing both increasing-cost and declining-cost situations.

Q. The Commission has indicated that another factor to be considered is incentives to efficient management and operation. Please comment on this.

A. In addressing this point, it is useful to draw a distinction between efficient management and operation *per se*, and achieving *lower rates* through efficient management and operation. They are not necessarily the same thing.

Once rates are set, either through a historical test period or a projected test period, a well-run utility will seek to be as efficient as possible, because all cost savings will flow to the bottom line – at least until the next general rate case. In that sense, I view the choice of test period to be relatively neutral with respect to achieving efficient management and operations *per se*.

But there can be a marked difference with respect to achieving *lower rates* through efficient management and operation. With a projected test period, a utility might anticipate the cost of a future activity to be a given level "x" some 12 to 20 months into the future, and build that projected cost into rates. If, during the intervening period, the utility finds a way to perform that activity more efficiently, the cost savings flow to the Company. The incentive to be efficient exists, but the benefits are not experienced in rates until they are reset pursuant to a subsequent case. For this reason, efficiency gains are more likely to be captured by shareholders than by ratepayers the further into the future the test period is projected.

Q. The Commission has also indicated that the length of time the new rates are expected to be in effect may be a factor in determining test period. Please comment.

A. It is difficult to predict how long new rates may stay in effect. I believe the most reasonable approach is to set rates targeting the time that rates are schedule to take effect, and then allow actual conditions to determine when the next rate case is necessary. In addition, I might point out that an aggressive future test period might be somewhat less objectionable if it were accompanied by a "stay-out" provision that precludes subsequent rate increases for some period of years.

Q. You mentioned the concept of "used and useful;" what role do you believe that concept should play in the test year context?

A. A fundamental principle of utility regulation is that a public utility should be permitted to earn a reasonable return on its investment in facilities after they have become "used and useful" for the utility's public service within the state. As explained by the Utah Supreme Court in describing some "basic principles" of utility regulation: "It is only to the extent the facilities developed are used and useful to the consumer that they are included in the rate base." (Committee of Consumer Services v. Public Service Commission, 595 P.2d 871, 874 (Utah 1979)). From a policy perspective - without attempting to address legal issues - the concept of pre-paying a return on a utility's projected investment in future facilities that have not yet been completed – and indeed, might not be completed according to the projected schedule – is fundamentally inconsistent with the "used and useful" concept.

Q. Please summarize your recommendations to the Commission.

A. The best test period to be used in the general rate proceeding is Calendar Year 2006, consisting of the period January 1, 2006 through December 31, 2006. In my opinion, a Calendar Year 2006 test period best reflects the conditions PacifiCorp will encounter during the period the rates will be in effect, and is a superior choice compared to the more aggressive future test period proposed by PacifiCorp. A future test period such as Calendar Year 2006 will use one less round of forecasts and thus provide a more certain basis for establishing rates that would go into effect in December 2006. Further, under the Company's proposal, customers in December 2006 would be paying for capital investment that had not yet occurred – and might not occur as planned. In addition, customers would be paying for projected 2007 inflation, expected labor cost increases, and the cost of equity infusions before these costs were actually incurred.

Q. Does this conclude your direct testimony?

A. Yes, it does.