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, Consisting of a General Rate Increase of Approximately $161.2 Million per Year, and for Approval of a New Large Load Surcharge	Docket No 07-035-93 ROGER J BALL'S RESPONSE MOTION TO ROCKY MOUNTAIN POWER'S MOTION TO STRIKE HIS RATE OF RETURN DIRECT & REBUTTAL TESTIMONY

On 8 May 2008, Rocky Mountain Power (RMP, Company) responded to my *Rate of Return Direct Testimony* and *Rate of Return Rebuttal Testimony* (collectively, *Testimony*), pre-filed on 31 March and 28 April respectively, by moving the Commission to strike it.

INTRODUCTION

I respectfully move the Commission to deny RMP's *Motion* because it was filed out of time.

However, RMP's *Motion* contains two points of significance that I will answer in this response.

First, the Company argues that, for rate of return evidence to be probative, a witness must "utilize financial models to estimate the return expected by investors in utility companies with risks corresponding to those of the company whose rates are being set" based upon "facts and methods of analysis generally accepted by relevant experts" and, because my Testimony does not meet those criteria, it is not probative or relevant and is contrary to principles established in *Bluefield*, *Hope*, *Daubert*, *Kumho*, *Patey*, *Franklin*, *UP&L*, *MFSCo*, and *USWest*, and should be stricken.[1]

[1] *Bluefield Water Works Co v Public Service Commission*, 262 US 679, 692 (1923) (*Bluefield*); *Federal Power Commission v Hope Natural Gas Co*, 320 US 591, 603 (1944) (*Hope*); *Daubert v Merrill Dow Pharmaceuticals, Inc*, 509 US 579 (1993) (*Daubert*); *Kumho Tire Co v. Carmichael*, 526 US 137 (1999) (*Kumho*); *Patey v Lainhart*, 1999 UT 31, ¶¶ 15-19, 977 P2d 1193 (*Patey*); *Franklin v Stevenson*, 1999 UT 61, ¶¶ 13-18, 987 P2d 22 (*Franklin*); *Utah Power & Light v Public Service Commission*, 152 P2d 542 (Utah 1944) (reliance on *Hope*) (*UP&L*); *Mountain Fuel Supply Co v Public Service Commission*, 861 P2d 414, 427 (Utah 1993) (citing *Bluefield* and *Hope*) (*MFSCo*); and *Re USWest Communications, Inc*, 1997 WL 875832, *438 (Utah PSC 1997) (*USWest*).

This argument entirely mistakes what those opinions held, and I respectfully move the Commission to deny the *Motion*.

Second, RMP points out that three of its 13 witnesses filed direct testimony regarding rate of return with its *Application for General Rate Increase* on 17 December 2007, and that "(o)ther than Mr Ball, all witnesses filed testimony on March 31, 2008, responding to the Company's cost of capital testimony". It then argues that, because my testimony "did not even mention the Company's direct testimony on cost of capital, let alone attempt to rebut it … (it) could not respond to (my) testimony responsive to (its) direct case because (I) had not yet responded to (its) direct testimony." This led the Company to conclude that my testimony was untimely and should be stricken. This argument is unfounded, the conclusion is erroneous, and I respectfully move the Commission to deny the *Motion*.

ROCKY MOUNTAIN POWER'S MOTION IS OUT OF TIME AND SHOULD BE DENIED

In the words of its own *Motion*:

> Rocky Mountain Power … moves the Commission to strike the Rate of Return Testimony of Roger J Ball dated on March 31, 2008 …
>
> DATED: May 8, 2008.

The Commission's Rule, UAC §R746-100-4D, Times for Filing, states:

> Motions directed toward initiatory pleadings shall be filed before a responsive pleading is due; otherwise objections shall be raised in responsive pleadings. Motions directed toward responsive pleadings shall be filed within ten days of the service of the responsive pleading.

RMP's *Motion* was not directed towards an initiatory pleading; the Rule doesn't provide a time for filing a motion in response to pre-filed written testimony distinct from the time from filing a motion directed towards responsive pleadings. The Motion was filed 38 days after my *Direct Testimony*, 30 days later than the language of the Rule requires. In the alternative, giving the Company the

benefit of the most liberal interpretation of the Rule, the *Motion* wasn't even filed within 30 days of the *Direct Testimony*. Either way, it was out of time, and should be denied.

Since The Company's *Motion* conflates my *Rate of Return Direct* and *Rebuttal Testimony*, it is difficult, if not impossible, to identify any of the arguments therein that are specific to the latter, so I respectfully move the Commission to deny it in its entirety.

MY RATE OF RETURN TESTIMONY IS TIMELY

My testimony was timely filed and served in accordance with the Commission's scheduling orders in this Docket.

Rocky Mountain Power's *Motion* fails to establish any basis – in statute, rule, case-law, order, or elsewhere – requiring my *direct* testimony to respond, or confining it to responding, to the Company's witnesses' direct testimony. The fact that I did not conform to RMP's unfounded expectations does not render my *Testimony* untimely and, as I will show, it was entirely proper for me to make other relevant points in that *Testimony*. I respectfully move the Commission to deny RMP's *Motion*.

MY RATE OF RETURN TESTIMONY IS NOT CONTRARY TO ESTABLISHED STANDARDS FOR DETERMINING RATE OF RETURN

In its *Motion*, RMP incorrectly claims that:

> … the United States Supreme Court has established that determination of the cost of capital to be used in setting just and reasonable utility rates is based on returns on investment being realize (sic) in other business enterprises with comparable risks. Contrary to this clear and well-established principle, Mr. Ball suggests that these principles do not apply in this case …

I have neither testified nor argued that the Commission ought not to consider the analyses of the earnings of other utilities and recommendations of statistical witnesses, but while the Company's *Motion* may establish some basis for its claim that the returns earned by similar utilities should be

considered in determining an authorised rate of return for RMP, none of the precedents it quotes establish that as the only evidence relevant to be considered.

The Commission is hardly so deprived of a wide range of statistical opinion that it needed mine, having received, in contradistinction to that of Company witness Samuel C Hadaway, statistical rate of return direct, rebuttal, and surrebuttal testimony of the kind RMP seems fixated on, and with clearly different opinions about the members of proxy groups, and diverse analyses and recommendations, from Utah Division of Public Utilities (Division) witnesses William (Artie) Powell and Charles E Peterson, and Utah Committee of Consumer Services (Committee) witness Daniel J Lawton.

Among many other things, in *Hope* the US Supreme Court opined that:

> We held in Federal Power Commission v Natural Gas Pipeline Co [2] … that the Commission was *not bound to the use of any single formula or combination of formulae* in determining rates. Its ratemaking function, moreover, involves the making of '*pragmatic adjustments*.' And when the Commission's order is challenged in the courts, the question is whether that order 'viewed in its entirety' meets the requirements of the Act. Under the statutory standard of 'just and reasonable' *it is the result reached not the method employed* which is controlling. It is *not theory but the impact* of the rate order which counts … The rate-making process under the Act, ie, *the fixing of 'just and reasonable' rates*, involves a *balancing of the investor and consumer interests*. Thus we stated in the Natural Gas Pipeline Co case that '*regulation does not insure that the business shall produce net revenues*' …The conditions under which *more or less might be allowed* are not important here. (Emphases added.)

So the object of this phase of this proceeding is actually to determine an authorised rate of return that will enable the Commission later to fix just and reasonable rates that balance the interests of stockholders and ratepayers. The Commission should consider not just the testimony of RMP's, Division's, and Committee's statistical witnesses, but a broader range of evidence. Indeed, if that should lead the Commission to setting a rate of return that "does not insure that the business shall produce net revenues", the Natural Gas Pipeline Co opinion indicates that would not be unlawful, provided the resulting rates were just and reasonable.

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[2] *Federal Power Commission v Natural Gas Pipeline Co*, 315 US 575, 592, 593 S, 62 SCt 736, 745, 746.

After all, rate-of-return regulation of monopoly utilities is supposed to be a surrogate for competition, competition is brutal, and companies in the competitive sector lose money, declare bankruptcy, are taken over, or simply go out of business, all the time. Regulators ought not to set rates that are confiscatory for stockholders, but neither should they set rates that featherbed a utility, insulating it at the expense of ratepayers from the consequences of management's decisions.

RMP, naturally, offers an interpretation of *Bluefield*, *Hope*, *et al*, focused on the interests of stockholders by advocating earnings "commensurate with returns on investments in other enterprises having corresponding risks". Arguably, those precedents may require the Commission to *consider* such statistical analysis, but they do not *require it* to *limit its investigation* to such evidence, and they certainly do not require anyone to limit their testimony to it. Indeed, according to the *Hope* Court quoted above, the Commission should equally consider the interests of ratepayers. If it accepts the Company's argument that only statistical evidence can be considered in this phase of the proceeding, it will ignore the fact that PacifiCorp management has consistently, in numerous cases over a period of several years, agreed to rates that it knew would deliver much lower returns than it now seeks, and it will neglect the fact that using a forecasted rate-base and expenses will shift risk from stockholders to ratepayers. Looking only to other utilities spread geographically (and over a much wider area than "the same general part of the country" to which the *Bluefield* Court referred) and ignoring changes historically in RMP's own circumstances would be to disregard significant parts of the *Hope* Opinion. The result would be quite circular: the tendency would inevitably be towards a single rate for all similar utilities, taking no account of statutory, structural, or other changes affecting the one under review in particular. And it would quite likely result in rates that are confiscatory of ratepayers' property.

My *Testimony* is not contrary to the law established by the US and Utah supreme courts and followed by the Commission, and I respectfully move the Commission to deny RMP's *Motion*.

MY RATE OF RETURN TESTIMONY IS RELEVANT AND PROBATIVE

The Company's Motion states that:

> expert opinion evidence must be provided by an expert qualified by *knowledge, skill, experience, training or education*, must be reliable and must be based on *facts and methods of analysis generally accepted* by *relevant experts*. (Emphases added.)

It doesn't question my "knowledge, skill, experience, training or education", but represents that *Daubert*, *Kumho*, *Patey*, and *Franklin* require that, for a witness to be qualified as an expert, his evidence "must be based on facts and methods of analysis generally accepted by relevant experts", inferring that those are limited to the compilation of earnings data for proxy groups of other utilities, and analyses such as CAPM and DCF, so that the only "relevant experts" are statisticians. RMP avers that *Bluefield* and *Hope* oblige the Commission to ensure that its authorised rate of return is "commensurate with returns on investments in other enterprises having corresponding risks." And it asserts that *UP&L*, *MFSCo*, and *USWest* made that principle the law in Utah. But that is not what these precedents established.

Daubert clarified that the adoption of *Federal Rules of Evidence* superseded the "general acceptance" test in *Frye*.[3] The Court's opinion quoted *Federal Rules of Evidence* 402 and 401. The comparable *Utah Rules of Evidence* say, in 402:

> All relevant evidence is admissible, except as otherwise provided by the Constitution of the United States or the Constitution of the state of Utah, statute, or by these rules, or by other rules applicable in courts of this state. Evidence which is not relevant is not admissible

and, in 401:

> "Relevant evidence" means evidence having *any tendency* to make the existence of *any fact* that is *of consequence to the determination* of the action more probable or less probable than it would be without the evidence. (Emphasis added.)

The *Daubert* Court opined that: "The Rule's basic standard of relevance thus is a liberal one"; "Nothing in the text of this Rule establishes 'general acceptance' as an absolute prerequisite to

[3] *Frye v United States*, 54 App DC 46,47, 293 F 1013, 1014 (1923) (Frye).

admissibility"; "the word 'knowledge' … applies to any body of known facts or to any body of ideas inferred from such facts or accepted as truths on good grounds"; "Unlike an ordinary witness, … an expert is permitted *wide latitude to offer opinions, including those that are not based on firsthand knowledge or observation*"; and "Vigorous cross-examination, (and) presentation of contrary evidence … are the traditional and appropriate means of attacking shaky but admissible evidence. See Rock v Arkansas, 483 US 44, 61 (1987)." For reasons that are unclear to me, RMP forwent the opportunity to present evidence contrary to mine on the impact of a future test year, or PacifiCorp's repeated motions for this Commission to approve rates that it knew would generate much lower returns than it now seeks, on RMP's rate of return. It is entirely a matter for RMP to decide what to file in this proceeding, but when no-one offers evidence effectively countering mine, I am entirely accurate in stating that my *Testimony* is uncontroverted.

Kumho expanded upon *Daubert*, clarifying that *Federal Rule of Evidence* 702 (and therefore *Utah Rule of Evidence* 702) distinguishes between "scientific, technical, or other specialized knowledge" on the part of an expert witness. RMP doesn't claim I lack the scientific, or technical, or other specialized, knowledge, etc, to qualify as an expert witness on rate of return, merely that I didn't exercise it in a specific way that the Company opines is the only legitimate way, an assertion that it has failed to provide a firm foundation for.

In *Patey*, in which the witness was a general dentist who regularly performs endodontic surgery, and whom the trial court found qualified to testify as an expert, the Court opined that "(Rule) 703 has broadened the basis for an expert's testimony by specifying that facts or data used in forming an opinion or inference need not be admissible if of the type reasonably relied on by experts in the witness' field of expertise." It quoted *Utah Rule of Evidence* 703:

> The facts or data in the particular case upon which an expert bases an opinion or inference may be those perceived by or made known to the expert at or before the hearing. If of a type reasonably relied upon by experts in the particular field in forming opinions or inferences upon the subject, the facts or data need not be admissible in evidence

and the *Advisory Committee Notes* to *Federal Rule of Evidence* 703:

> Thus a physician in his own practice bases his diagnosis on information from numerous sources and of considerable variety, including statements by patients and relatives, reports and opinions from nurses, technicians and other doctors, hospital records, and X rays. Most of them are admissible in evidence, but only with the expenditure of substantial time in producing and examining various authenticating witnesses.

Franklin doesn't appear to be a relevant precedent here. Expert testimony in that case related to recovery of repressed memory, which the Court held to be inadmissible because scientific evidence did not reliably support the techniques used. Other than labeling part of it "an incredible claim", which is something for the Commission to determine, RMP hasn't attacked any scientific, technical, or other specialised basis for my *Testimony*, only that I have not joined the battle of statistics over the selection of proxy groups, the analysis of their rates of return, or the recommendation of a rate, or range of rates, of return for the Company. But nothing requires me to; certainly nothing in *Bluefield*, *Hope*, *Daubert*, *Kumho*, *Patey*, *Franklin, UP&L*, *MFSCo*, or *USWest*.

I base my opinions and inferences on information from many and varied sources, including things that I have read, heard, and observed over many years, as the *Patey* Court opined that I am entitled to do. One highly relevant skill that I am able to deploy is an ability to gather information from a wide range of sources, including professionals in many different areas of expertise, and synthesize it into a strategic overview.

Utah Rule of Evidence 702 says:

> if scientific, technical, or other specialized knowledge will assist the trier of fact to understand the evidence or to determine a fact in issue, a witness qualified as an expert by knowledge, skill, experience, training, or education may testify thereto in the form of an opinion or otherwise.

My objective in filing my *Testimony* was to help the Commission – in keeping with *Hope*, *Kumho*, and *Utah Rule of Evidence* 702 – understand evidence and determine facts that are highly pertinent to its efforts to make "pragmatic adjustments" to RMP's authorised rate of return, leading to a "rate order that will fix "just and reasonable rates", balancing … the investor and consumer interests."

My expertise in these regards is unchallenged in RMP's Motion, and I am therefore entitled to be "permitted wide latitude to offer opinions, including those that are not based on firsthand knowledge or observation." The *Daubert* Court made clear that the *Frye* "general acceptance" doctrine that RMP holds dear no longer applies.

Having established that I am entitled to offer evidence, opinions, and explanations bearing directly on the Commission's determination of an authorised rate of return for RMP, several elements of my testimony are clearly admissible because they bear directly on that determination. For instance, on lines 38–46 and 59–94 of my *Direct Testimony* I reviewed the facts of the past 4 PacifiCorp general rate cases and, based upon those facts, testified on lines 107–120 that:

> in its last four cases, the Company has not only freely entered into agreements, but has taken the lead in advocating them to the Commission, that have resulted in its getting increases amounting to less than half of what it requested.
>
> The utility has similarly agreed to nominal authorised rates of return on equity markedly lower than it initially requested, and the rate increases it has freely agreed to accept and has taken the lead in representing to the Commission would result in just and reasonable rates have effectively prevented PacifiCorp from realising even those reduced RoEs.
>
> It is hard to imagine that management was unaware that it could not possibly attain the attenuated RoEs it had agreed to, given that the stipulated rate increases were so much smaller a fraction of the amounts requested than the settlement RoEs were of the rates sought.
>
> But on top of that, the Company voluntarily accepted stay-out provisions, restricting its ability to file further petitions for rate relief when it became beyond doubt that it was not achieving the RoEs it had stipulated to.

I then offered my opinion, based upon the foregoing, that:

> PacifiCorp doesn't need and cannot justify either the $99.8M rate increase in its revised application or the 10.75% RoE in its original application, and it doesn't expect to get either from these proceedings.

I testified on Senate Bill 61 before a Senate Standing Committee in 2003, have observed its effect on the settlement of subsequent PacifiCorp rate cases, and the effect of settlement on the percentage of the Company's requests that have been agreed and approved, and am well informed on the language of the revised statute and its effects on requested revenue requirements. I testified

on House Bill 320 before a House Standing Committee, and participated in every meeting of the Interim Committee and of the working groups on the Bill in 2000, and lobbied the House Speaker, Majority Leader and relevant committee members extensively. I have learned a great deal about Utah Power & Light prior to its takeover by PacifiCorp. I am well-informed about PacifiCorp's policies and decisions from that time until the ScottishPower takeover and their effect on Utah ratepayers, having been actively involved at a strategic level in Commission proceedings for the past 11 years, including the Inter-jurisdictional Allocations and MSP cases. And I have closely observed the purchase, by Mid-American Energy Holdings (MEHC) on behalf of Berkshire Hathaway (BH), of PacifiCorp from ScottishPower.

Based upon that experience, I am qualified to testify as an expert on House Bill 320, Senate Bill 61, what they reveal about the utilities' legislative strategy, and their impact upon the balance of risk between stockholders and ratepayers, and the justness and reasonableness of rates, and on Berkshire Hathaway's investment strategy. My opinion that there is no connection between the testimony of Dr Hadaway and reality regarding what rate of return will motivate MEHC or BH to invest additional capital in PacifiCorp is based upon that experience and is appropriate expert testimony. As is my testimony that the amount identified in PacifiCorp's Supplemental Direct Testimony on 6 March 2008 as immediately consequential upon the use of an wholly forecasted calendar 2008 test period, compared with an historic period with known and measurable changes.

My *Testimony* is relevant and probative, and I respectfully move the Commission to deny RMP's *Motion*.

CONCLUSION

I first addressed the question of the shift of risk from stockholders to ratepayers in this first PacifiCorp general rate case in which the Commission intends to use an entirely projected test

period in my 25 January 2008 *Test Year Testimony* and again in my 4 February *Test Year Rebuttal Testimony*. My *Testimony* expanded upon the matter. Dissenting parties have had ample time to put forward their countervailing testimony, but none have. Instead, RMP moves the Commission to rule out any consideration of the part this shift of risk plays in determining an authorised rate of return. It would be improper for the Commission to limit its consideration to the narrow statistical issues that the Company advocates.

Dr Hadaway's testimony repeatedly uses the terms "risk" and a "risk premium", referring to the concept that the margin of cost of equity over cost of borrowing compensates owners for the additional risks of their unsecured investment over secured loans. The Company's Motion cites *USWest*, in which the Court, referring to *Bluefield* and *Hope*, opined:

> As we have stated many times, these cases counsel us to reach a decision which gives investors the opportunity to earn returns sufficient to attract capital and that are comparable to returns investors require to assume the same *degree of risk* in other investments they might make. Investors' required return, the opportunity cost of capital, is the utility's cost of capital. (Emphasis added.)

My *Testimony* addresses what should happen in the determination of an authorised rate of return to balance "the investor and consumer interests" when the "degree of risk" to which the owners of this particular utility are exposed changes. It is highly relevant to the question before the Commission in this phase of the proceeding, it is probative, and it is timely. Whether it could not, would not, or simply did not, RMP has failed to offer evidence to counter it, and no other party has addressed it, yet the Company wants the Commission to strike it. Based upon years of observation of group behaviour and study of organisational psychology, it is my expert opinion that the Company was unable to counter it, and is very afraid of the consequences if it is admitted.

I move the Commission to deny Rocky Mountain Power's *Motion*.

Respectfully submitted on 19 May 2008,

/s/

Roger J Ball

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing Roger J Ball's Response Motion to Rocky Mountain Power's Motion to Strike His Rate of Return Direct and Rebuttal Testimony in Docket 07-035-93 was served upon the following by electronic mail on 19 May 2008:

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