

BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

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<b>In the Matter of the Application of</b>	)	<b>Docket No. 09-035-15</b>
<b>Rocky Mountain Power for</b>	)	<b>Surrebuttal Testimony of</b>
<b>Approval of its Proposed Energy</b>	)	<b>Michele Beck</b>
<b>Cost Adjustment Mechanism</b>	)	<b>For the Office of</b>
	)	<b>Consumer Services</b>

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January 5, 2010

1           **Introduction**

2   **Q.    WHAT IS YOUR NAME, OCCUPATION AND BUSINESS ADDRESS?**

3   A.    My name is Michele Beck. I am the Director of the Office of Consumer  
4        Services (Office or OCS). My business address is 160 East 300 South,  
5        Salt Lake City.

6

7   **Q.    HAVE YOU PREVIOUSLY FILED DIRECT AND REBUTTAL**  
8        **TESTIMONY IN THIS CASE?**

9   A.    Yes.

10

11   **Q.    WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

12   A.    I will respond to some general assertions made by the Company in  
13        rebuttal testimony about the Office's position in this case; demonstrate that  
14        none of the evidence provided in rebuttal obviates the need to address the  
15        threshold issues raised by the Office before any ECAM could be found to  
16        be in the public interest; and expand upon the Office's recommendations  
17        to the Commission regarding how to proceed in this case.

18

19        **Response to General Characterizations of the Office's Position**

20   **Q.    THE COMPANY'S WITNESS MR. DUVALL STATED THAT HE IS**  
21        **DISAPPOINTED THAT PARTIES DESIRE TO CONTINUE TO SET**  
22        **RATES THROUGH PROTRACTED LITIGATION OVER COMPUTER**

23 **MODELING TECHNIQUES AND INPUTS. DOES HE ACCURATELY**  
24 **PORTRAY THE OFFICE'S POSITION IN THIS CASE?**

25 A. No. The Office's view is that the Company has not met its evidentiary  
26 burden to demonstrate that changing the recovery method for NPC would  
27 be in the public interest. Further, the Office has shown that an ECAM  
28 mechanism could not be in the public interest unless two threshold issues  
29 are first resolved. Mr. Duvall's characterization of this position as a desire  
30 to set rates based on modeling techniques does not recognize the full  
31 spectrum of alternatives and, more importantly, does not acknowledge  
32 that the Company must bear the burden of demonstrating its case rather  
33 than simply having all parties coming together and giving their  
34 preferences.

35

36 **Q. DR. MCDERMOTT STATES THAT INTERVENORS' CONCERNS**  
37 **ABOUT SHIFTING RISK IS BASED UPON AN APPARENT**  
38 **CONCLUSION THAT PRUDENTLY INCURRED COSTS ARE**  
39 **CURRENTLY BORNE BY SHAREHOLDERS. (MCDERMOTT**  
40 **REBUTTAL, LINES 80 – 85) HAS THE OFFICE MADE SUCH A**  
41 **CONCLUSION?**

42 A. No. The Office has not concluded that shareholders are currently  
43 responsible for any costs that have been found to be prudently incurred.  
44 Further, the Office is not confusing the concept of shifting risk with shifting  
45 costs. This issue is intricately tied to one of the threshold issues that the

46 Office has raised. I will explain the specific example of a shifted risk due  
47 to the Company's resource planning decisions associated with over-  
48 reliance on market energy later in this testimony when I address those  
49 threshold issues.

50

51 **Q. DR. MCDERMOTT INDICATES THAT "ALLEGED DESIGN FLAWS IN**  
52 **THE PROPOSED ECAM SEEM TO PERMEATE THE CONCERNS OF**  
53 **SOME OTHER INTERVENORS." (MCDERMOTT REBUTTAL, LINES**  
54 **28-29) ARE THE OFFICE'S CONCERNS WITH THE ECAM LIMITED TO**  
55 **DESIGN ISSUES?**

56 A. No. The Office has specifically raised two threshold issues that must be  
57 resolved before *any* ECAM can be found to be in the public interest.

58

59 **Q. THE DIVISION'S WITNESS MR. PETERSON INDICATES THAT**  
60 **GENERALLY "THE PARTIES APPEAR TO CONFLATE THE**  
61 **SPECIFICS OF THE COMPANY'S ECAM PROPOSAL AND THE**  
62 **BROADER QUESTION OF WHETHER SOME SORT OF ECAM FOR**  
63 **PACIFICORP MAY BE IN THE PUBLIC INTEREST." (PETERSON**  
64 **REBUTTAL, LINES 30-32) WHAT IS YOUR RESPONSE?**

65 A. The Office is not confused about the difference between whether *this*  
66 ECAM, as filed, is in the public interest and whether *any* ECAM could be  
67 in the public interest. The Office was very clear that, at a minimum, the  
68 two threshold issues of appropriate level of reliance on market energy and

69 appropriate policies for natural gas hedging must both be resolved before  
70 any ECAM could be found to be in the public interest. In addition, the  
71 Office does not believe it would be a productive or efficient use of the  
72 regulatory process for the Commission to label all of the shortcomings of  
73 this or any ECAM as design flaws to be addressed in a subsequent phase,  
74 as requested by the Division. Too many flaws and issues have been  
75 raised by the parties in Phase I to simply move forward into Phase II with  
76 the hope that the outcome could be in the public interest just because it is  
77 theoretically possible.

78

79 **Threshold Issues**

80 **Q. PLEASE SUMMARIZE THE OFFICE'S THRESHOLD ISSUES THAT**  
81 **YOU RAISED IN DIRECT TESTIMONY AND HAVE REFERENCED IN**  
82 **THIS TESTIMONY.**

83 A. The Office believes that no ECAM could be found to be in the public  
84 interest until the issues of natural gas hedging and appropriate reliance on  
85 market energy have been satisfactorily addressed and resolved by the  
86 Commission. Because these are issues that would need to be resolved  
87 in advance of implementing an ECAM in order to protect consumers, the  
88 Office has labeled them as "threshold" issues in this case.

89

90 **Q. WHAT IS THE COMPANY'S RESPONSE TO THE OFFICE'S**  
91 **TESTIMONY ABOUT THESE THRESHOLD ISSUES?**

92 A. Mr. Duvall testifies that there is no reason to delay implementation of this  
93 ECAM to examine the issue of over-reliance on market energy. He  
94 suggests that to do so would amount to a “double standard.” (Duvall  
95 rebuttal, lines 443 -448) Mr. Graves testifies that there is no reason to  
96 delay implementation of this ECAM to review the Company’s hedging  
97 practices and suggests that consumer advocates and regulators may not  
98 be able to understand the issues until reviewing them in an ECAM  
99 framework. (Graves rebuttal, lines 605-619)

100

101 **Q. IN WHAT FORUM DOES THE COMPANY PREFER TO HAVE THE**  
102 **APPROPRIATE LEVEL OF RELIANCE ON MARKET ENERGY**  
103 **REVIEWED?**

104 A. Mr. Duvall stated that “the Company believes that the integrated resource  
105 planning process is the proper forum to consider the issue of the level of  
106 reliance on market energy.” (Duvall rebuttal, lines 448 – 449) He further  
107 endorsed both the IRP and the resource procurement process as being  
108 robust, transparent, and “actively monitored by Utah parties and the Utah  
109 Commission.” (Duvall rebuttal, lines 393 – 395)

110

111 **Q. DO YOU AGREE THAT THE RESOURCE PLANNING AND**  
112 **PROCUREMENT PROCESSES ARE ROBUST?**

113 A. While I agree that these processes could be considered to be robust, I do  
114 not agree that the outcomes have been. We have yet to see a generating

115 resource to result from the Energy Procurement Act. The resource  
116 chosen in the last all-source RFP was cancelled and the current all-source  
117 RFP was suspended and recently re-started. The Commission's Orders  
118 either acknowledging or not acknowledging the Company's IRP provide  
119 some guidance to the Company, but rarely endorse (or provide explicit  
120 changes to) the Company's planning assumptions, resource selection  
121 criteria or action plan.

122

123 Nonetheless, Mr. Duvall claims that the Company's plan is "reasonably  
124 consistent with the last direction the Commission provided the Company  
125 on this issue." Apparently, Mr. Duvall believes that the Commission has  
126 not provided input to the Company since its acknowledgement of the 2004  
127 IRP, despite having a forty-four page order that does *not* acknowledge a  
128 more recent (2007) IRP. In that order, the Commission clearly indicated  
129 that "PacifiCorp management retains responsibility for its decisions."

130 (Docket No. 07-2035-01, Report and Order, issued February 6, 2008, p. 5)

131 However, if an ECAM is implemented, customers would bear many of the  
132 significant risks and costs resulting from the Company's decisions whether  
133 to build new resources or to rely on the market.

134

135 Ultimately, I believe that Mr. Duvall's choice of words is quite telling about  
136 these processes. It is true that they are "actively monitored by Utah  
137 parties and the Utah Commission." However, I am not sure to what extent

138 Utah parties or the Utah Commission actually influence the outcome of the  
139 Company's resource decisions through these processes.

140

141 **Q. WHY IS IT IMPORTANT TO THE OFFICE TO EXAMINE THE**  
142 **APPROPRIATE LEVEL OF RELIANCE ON MARKET ENERGY?**

143 A. This is the specific example of the risk shifting to which I referred earlier in  
144 my testimony. The greater the extent to which the Company relies on  
145 market energy, the greater the exposure to the risk of future market price  
146 spikes. If the risk of market price spikes is small, it would make sense to  
147 maximize use of available market energy. However, if the risk is higher, it  
148 would make sense to balance that risk with a greater amount of  
149 investment in Company-owned generating resources (or long-term  
150 contracts with other specific resources.) Under the current method of  
151 recovering NPC through base rates, rates are set on normalized market  
152 prices. Therefore, it is the Company, not its customers, who is initially  
153 exposed to the risk of future price spikes<sup>1</sup>. Under an ECAM, this risk would  
154 be entirely shifted to customers.

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<sup>1</sup> Although in the case of protracted high market prices or multiple price spikes, the Company would certainly file a new general rate case. Since the 240-day time period for such a case to be determined is less than the lead time for constructing new resources, these costs would likely be passed through to consumers for some period of time. Further, the Company would have the option of petitioning for interim relief, as it did during the Western Power Crisis.

156 **Q. COULD THE ISSUE OF APPROPRIATE LEVEL OF MARKET ENERGY**  
157 **SIMPLY BE ADDRESSED THROUGH APPROPRIATE ECAM DESIGN?**

158 A. Not very easily and certainly not completely. Addressing the issue of  
159 appropriate levels of electric market purchases would not be easy  
160 because such a design would contain a level of complexity that may  
161 exceed the tolerance and preference of regulators and intervenors.  
162 Addressing this issue through ECAM design would not be complete  
163 because it would need to be accompanied with a change in the type of  
164 guidance and oversight provided in the IRP process.

165

166 Even the Company acknowledges the importance of this regulatory  
167 oversight as evidenced by Mr. Graves' statement that "regulatory  
168 oversight of the IRP process should result in an optimal mix of long-term  
169 resources." (Grave rebuttal, lines 497 – 500) The most recently completed  
170 IRP (2007) did not result in such an outcome; rather, the Commission  
171 stated that it could not "determine from either the information in the IRP or  
172 from parties' comments that the Company's preferred portfolio is either  
173 "optimal" or "robust." " (Docket No. 07-2035-01, Report and Order, issued  
174 February 6, 2008, p. 39) Thus, changes to the IRP process would also be  
175 required to ensure that the outcome of *each* IRP was a determination that  
176 could be used to evaluate the prudence of ongoing NPC that would  
177 potentially be recovered through an ECAM. I am not confident that such  
178 changes could occur in the current regulatory environment; one in which

179 Company representatives have questioned in some forums the ongoing  
180 relevance and validity of the IRP process in general.

181

182 **Q. HOW DOES THE COMPANY PREFER TO ADDRESS THE ISSUE OF**  
183 **NATURAL GAS HEDGING?**

184 A. It isn't clear. No Company witness provides a specific recommendation as  
185 to how the hedging should be overseen. Mr. Graves suggests that "it will  
186 take some time and experience with the ECAM before it is known whether  
187 the hedging risk goals should be revised to better match customer  
188 preferences." (Graves rebuttal, lines 617-619) However, without explicitly  
189 addressing the Company's hedging practices, there would be no reason to  
190 expect that the current practices would continue whether or not preferred  
191 by consumers. Mr. Graves also minimizes the significance of hedging  
192 when he states that "much of the way the ECAM risks ultimately will be felt  
193 by customers does not even depend on how the Company hedges its  
194 procurement, but on how it recovers the variances in rates over time."  
195 (Graves rebuttal, lines 626-628) This statement does not recognize the  
196 higher costs that could be associated with hedging policies nor the link  
197 between hedging and the ECAM. However, I do agree with Mr. Graves  
198 that the method of recovering the variances in rates is a design issue.

199

200 **Q. DOES THE COMPANY ACKNOWLEDGE THAT ITS HEDGING**  
201 **POLICIES LIKELY INCREASES THE OVERALL COST OF**  
202 **ELECTRICITY TO CUSTOMERS?**

203 A. Yes. Dr. McDermott acknowledges that “mitigating volatility has an ex  
204 ante cost relative to not hedging, i.e. an “insurance premium” is paid.”  
205 (McDermott rebuttal, lines 244-245) Dr. McDermott provides additional  
206 clarity on this issue of the costs of hedging within another example when  
207 he states directly “that on an ex ante basis, hedging would be expected,  
208 on balance, to increase the cost of electricity for the customer.”

209 (McDermott rebuttal, lines 418-419) The examination he recommends (of  
210 the “tradeoff between reduced volatility and higher ex ante fuel costs”) is  
211 precisely the type of analysis the Office proposes should take place prior  
212 to the implementation of any ECAM.

213

214 **Q. DOES THE COMPANY ACKNOWLEDGE A LINK BETWEEN HEDGING**  
215 **AND AN ECAM?**

216 A. Yes. Mr. Graves acknowledges the link in his suggestion that reports on  
217 hedging practices and hedging success could be a routine aspect of future  
218 ECAM filings and reviewed periodically within that process. (Graves  
219 rebuttal, lines 504 – 510, 532-536, 652-654)

220

221 **Q. WHY IS IT IMPORTANT TO THE OFFICE TO EXAMINE THE HEDGING**  
222 **PROCESSES?**

223 A. As it currently stands, customers pay a premium for the hedging, but also  
224 pay a known amount for net power costs as reviewed and determined in a  
225 heavily scrutinized rate case. If this ECAM is implemented, then  
226 customers are also responsible for costs that exceed projections (or  
227 receive the benefits of costs that are lower). However, the hedging  
228 practice (as described in the Direct Testimony of Dr. Schell) is such that  
229 there is little potential for benefits of natural gas prices falling below what  
230 was expected.

231

232 It would be patently unfair to expect customers to pay a premium for  
233 reducing price volatility and also create a pass-through mechanism for  
234 price volatility without first determining the proper balance of price stability  
235 versus overall costs. Further, as I stated in my direct testimony, without a  
236 thorough examination of the proper hedging policies, the Company could  
237 change its hedging policies without regard for customer preferences  
238 regarding volatility. Before customers assume responsibility for any  
239 volatility in costs, they should have the opportunity to provide input in the  
240 management of those costs in an adjudicated proceeding before the  
241 Commission.

242

243 **Q. COULD THESE ISSUES SIMPLY BE ADDRESSED IN THE DESIGN OF**  
244 **AN ECAM?**

245 A. No. The Company's hedging policy is a multiple-year strategy. Certain  
246 types of changes, if found to be in the public interest, could take years to  
247 implement.<sup>2</sup> Therefore, a determination of an appropriate hedging policy  
248 must be made prior to the consideration of any kind of ECAM design.

249

250 **Q. DR. MCDERMOTT RESPONDED TO THE OFFICE'S**  
251 **RECOMMENDATIONS REGARDING THE THRESHOLD ISSUES BY**  
252 **STATING THAT THEY "SHOULD BE TREATED ON A LEVEL PLAYING**  
253 **FIELD WITH OTHER CATEGORIES OF NET POWER COSTS." HOW**  
254 **DO YOU RESPOND TO HIS SUGGESTION?**

255 A. The Office agrees that gas hedging and electric market energy costs  
256 should be "treated on a level playing field" if and when any ECAM-type  
257 mechanism is designed. However, significant additional examination of  
258 these issues would be necessary to create the "level playing field" to  
259 which the Company refers.

260

261 If appropriate levels of market energy are best examined in the IRP  
262 process (as suggested by the Company), then the IRP process must be  
263 redesigned to do so prior to the design or implementation of an ECAM.  
264 Otherwise, the electric market energy purchases could not receive the

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<sup>2</sup> See OCS witness Dr. Schell's Direct Testimony for a specific description of the Company's hedging policies. In particular, some of the confidential portions describe why this would be true.

265 same kind of regulatory review that other costs potentially included in an  
266 ECAM would receive. How could prudence of electric market purchases  
267 be evaluated if a standard for determining prudence is expected to be set  
268 in another process and does not exist?

269

270 Similarly, if hedging practices and success could be reported on and  
271 evaluated as a routine part of ECAM filings (as suggested by the  
272 Company), then a standard for evaluation must be determined before  
273 such filings are made.

274

#### 275 **Summary and Recommendations**

276 **Q. PLEASE SUMMARIZE THE OFFICE'S VIEWS AT THIS POINT IN THE**  
277 **CASE.**

278 A. The Office continues to believe that the Company has not met its burden  
279 in demonstrating that an ECAM is needed and in the public interest.  
280 Further, the Office believes that no ECAM design can be found to be in  
281 the public interest unless and until the two threshold issues of natural gas  
282 hedging and appropriate reliance on market energy have been addressed  
283 and resolved by the Commission.

284

285 **Q. WHAT IS YOUR RESPONSE TO THE DIVISION'S SUGGESTION THAT**  
286 **THE THRESHOLD ISSUES CAN BE ADDRESSED INDEPENDENTLY**  
287 **OF OR PARALLEL WITH THE DESIGN OF AN ECAM?**

288 A. Although the Division and the Office apparently agree on the need to  
289 address these issues, the Office disagrees that it can be done  
290 independently of or parallel with the design of an ECAM. These are  
291 issues that must be done sequentially. As I discussed above, it would be  
292 impossible to design an ECAM to be in the public interest or to review an  
293 ECAM to ensure prudence without first knowing what standard is to be  
294 met. The issues of the proper natural gas hedging policies and  
295 appropriate reliance on market energy are two issues for which a standard  
296 has not yet been developed. Until such a standard exists, we cannot  
297 move forward with the ECAM process.

298

299 **Q. WHAT ARE THE OFFICE'S RECOMMENDATIONS TO THE**  
300 **COMMISSION ON HOW TO PROCEED WITHIN THIS DOCKET?**

301 A. The Office's primary recommendation is that the Commission should  
302 reject the Company's filing. The Company has not met its evidentiary  
303 burden to demonstrate that an ECAM is necessary and in the public  
304 interest. Rather than simply denying the Company's petition, the  
305 Commission could provide a specific plan to address the threshold issues  
306 that have been raised and guidance regarding the type of specific design  
307 elements that the Company could address in a future ECAM filing to be  
308 made after the threshold issues have been resolved. If the Commission  
309 were now simply to move forward into Phase II, it would send the wrong  
310 signals to the Company regarding its burden of proof. Further, it is difficult

311 to envision how the public interest standard could be met with a wide open  
312 ECAM design phase with parties working toward the theoretical possibility  
313 of an ECAM design that could be in the public interest.

314

315 The Office has raised many concerns, both with *this* ECAM and with such  
316 mechanisms in general. We will acknowledge that *some* of these  
317 concerns could be addressed through careful attention to the design of an  
318 ECAM, as explained in Mr. Chernick's recommendations. However, the  
319 Office maintains that the two threshold issues of natural gas hedging and  
320 appropriate reliance on market energy must be addressed prior to any  
321 additional design considerations and suggests two alternatives for doing  
322 so. The Commission could utilize the open dockets associated with the  
323 2008 IRP (Docket No. 07-2035-01) and the investigation of hedging  
324 policies (Docket No. 09-035-21). Alternatively, the Commission could also  
325 address the threshold issues within this ECAM docket by postponing  
326 design to Phase III and creating a new Phase II for the purpose of  
327 resolving threshold issues. In either case, the Office would request and  
328 recommend that the Commission establish a specific schedule that  
329 includes input from all interested parties and a deliberative process with  
330 an outcome that includes specific guidance and ruling from the  
331 Commission on these issues.

332

333 Finally, the Office recommends that if the ECAM issue reaches the stage  
334 that addresses design, that the Commission closely manage the process.  
335 In order to effectively address all of the issues that have been raised, the  
336 process may need to be separated into subparts or addressed in a  
337 manner other than the typical pre-filed testimony and hearings.

338

339 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

340 A. Yes it does.

341