

1 **Q. Please state your name, business address and title.**

2 A. My name is Charles E. Peterson; my business address is 160 East 300 South, Salt Lake City,
3 Utah 84114; I am a Technical Consultant in the Utah Division of Public Utilities (Division,
4 or DPU).

5
6 **Q. On whose behalf are you testifying?**

7 A. The Division.

8
9 **Q. Are you the same Charles E. Peterson who has filed testimony for the Division in Phase
10 I and Phase II regarding the ECAM in this matter?**

11 A. Yes.

12
13 **Q. What is the purpose of your surrebuttal testimony regarding hedging and front office
14 transactions in this matter?**

15 A. My surrebuttal testimony responds to comments made by PacifiCorp witness Gregory N.
16 Duvall in his rebuttal testimony dated July 2010 regarding front office transactions, or FOTs,
17 and related resource issues. Division witness Douglas Wheelwright will respond to Mr.
18 Duvall's comments regarding hedging.

19
20 **Q. Please summarize the Division's concerns regarding FOTs.**

21 A. The Division's concerns regarding FOTs have been expressed in comments to the
22 Company's recent Integrated Resource Plans (IRPs). Division witness Douglas Wheelwright
23 also outlined these concerns under the heading "Market Purchases Issues" in his direct
24 testimony in this Docket dated June 16, 2010, at lines 68-190. The Division and other parties
25 have been concerned that the Company is relying too much on wholesale market purchases
26 (i.e., FOTs) to cover its expected load both currently and especially in the future. This
27 reliance on FOTs may put ratepayers, and the Company, at more risk to market volatility and
28 potential supply shortages than is currently being modeled in the Company's IRP. For
29 example, one potential risk that does not seem to be modeled is the situation where the
30 Company, if it has owned plant, can choose between running its plant and purchasing on the

31 market depending on which is most economic. If it does not have the owned plant to cover its
32 load, the Company has no choice but to purchase on the market and thereby subject itself and
33 ratepayers to the risks of the wholesale market. Worse yet, if the Company has insufficient
34 owned resources and there is a major shortage of power or inability to bring power into
35 PacifiCorp's system, reliability could be seriously jeopardized. In its Report and Order in the
36 2008 IRP Docket, the Commission also expressed its concerns about the Company's reliance
37 on the wholesale market and ordered additional analysis by the Company in future IRPs.¹
38

39 **Q. Please summarize the points regarding FOTs and related issues made by Mr. Duvall in**
40 **his July 2010 rebuttal testimony.**

41 A. Mr. Duvall argues that the FOT issue need not be resolved in this Docket.² He believes that
42 the IRP process is the best place to determine the appropriate level of market reliance.³ He
43 seems to imply that the Commission's Acknowledgement of the Company's 2008 IRP
44 constitutes an endorsement of the level of market purchases to satisfy peak demand.⁴ He
45 argues that there are risks to customers from over-building and claims that Company has
46 saved ratepayers a considerable amount of money by its restraint.⁵ He believes that the level
47 of market reliance implicit in the Commission's revenue requirement Order in the 2009 rate
48 case, Docket No. 09-035-23, supports the idea that the Commission is satisfied with the
49 current level of market purchases.⁶
50

51 Mr. Duvall characterizes part of Mr. Wheelwright's June 16, 2010 testimony regarding
52 market purchases as "The DPU also suggests that to deal with concerns about market
53 purchases, the Commission should exclude market purchases or only allow cost recovery for
54 market purchases that cover a specific percentage of annual or peak load, implying that the
55 current level of market reliance is not 'optimal.'"⁷

¹ Public Service Commission, Report and Order, Docket No. 09-2035-01, dated April 1, 2010, pp. 30-31.

² Rebuttal Testimony of Gregory N. Duvall, Docket No. 09-035-15, July 2010, lines 29-54.

³ Ibid., lines 44- 51, 69-71.

⁴ Ibid., lines 71-73.

⁵ Ibid., lines 56-65and confidential lines 66-68.

⁶ Ibid., lines 80-83.

⁷ Ibid., 225-229; see also lines 334-351.

56

57 Mr. Duvall disagrees with the characterization that an ECAM could reduce the Company's
58 incentives to build.⁸

59

60 **Q. What is your comment regarding the contention that the FOT issue need not be**
61 **resolved in this Docket?**

62 A. The Division has consistently taken the position that the FOT issue need not be resolved
63 before the Commission considers and possibly approves the implementation of an ECAM for
64 the Company. In this regard the Division and Company are in agreement. At the same time,
65 the Division recognizes that the Commission ordered further consideration of this issue in its
66 Report and Order in Phase I of this Docket.⁹ The Division summarized its position on this
67 matter through Mr. Wheelwright's June 16, 2010 direct testimony and discussed it further in
68 the direct testimony in Phase II that I filed on behalf of the Division on August 4, 2010.

69

70 **Q. Does the Division believe that the IRP process is the best place to evaluate the**
71 **Company's level of FOTs?**

72 A. I want to comment on Mr. Duvall's statement that Mr. Wheelwright acknowledged that
73 market reliance and hedging are best addressed in the IRP process.¹⁰ I have been unable to
74 discover where Mr. Wheelwright made that acknowledgment. For his part Mr. Wheelwright
75 specifically contradicts Mr. Duvall's assertion in his surrebuttal testimony in this Docket.¹¹
76 Generally, the arguments made by Mr. Wheelwright against the IRP process being best
77 suited to evaluate the Company's hedging program would also apply to FOTs. Nevertheless,
78 the IRP is one place to continue to evaluate the levels of market purchases.

79

80 To answer the question directly, in my testimony filed on August 4, 2010 in this Docket I
81 recommended bringing the FOT issue into the ECAM to the extent that the Company could
82 file for adjustments to the ECAM sharing percentage based upon its adherence to its own

⁸ Ibid., lines 320-333.

⁹ Public Service Commission, Report and Order, Docket No. 07-2035-01, dated February 6, 2008, p. 17.

¹⁰ Duvall, Op. Cit. lines 44-47.

¹¹ Douglas Wheelwright, DPU SR Exhibit 2.0, August 10, 2010, lines 93-118.

83 goals set forth in the IRP. The requirement that the Company provide additional reports and
84 analysis in future IRPs may result in recommendations to open a separate docket to evaluate
85 the issue or may indicate a “steady-as-she-goes” policy posture. The Division believes that
86 some FOTs may be prudent and the Division believes the Company should manage its FOT
87 portfolio for the long-term financial health of the Company and for the benefit of ratepayers.
88

89 **Q. Does the Division understand that the Acknowledgement of an IRP by the Commission**
90 **implies some sort of endorsement of the Company’s preferred portfolio and Action**
91 **Plan, including the level of FOTs?**

92 A. No. The Division understands Acknowledgement of an IRP only means that the Company
93 sufficiently followed the Commission’s IRP guidelines in preparing its IRP. It does not
94 necessarily mean that the Commission agrees with the substantive content of the IRP. To the
95 specific point of FOTs, Mr. Duvall shows that he’s aware that the Commission is also
96 concerned regarding the Company’s reliance on FOTs when he cites the Commission’s
97 Report and Order in the 2008 IRP wherein the Commission raises its own concerns and
98 orders further analysis of FOTs in future IRPs.¹² At several points in its IRP Order, the
99 Commission clearly states those concerns – a few of these are quoted below:

100

101 **The Company’s explanation that it will change its plan to acquire**
102 **resources if expected [energy not served] grows too large is not**
103 **comforting...¹³**
104

105 **We are concerned with the Company’s stated confidence in managing the**
106 **risk associated with reliance on the market for a significant portion of its**
107 **customers’ power requirements, especially combined with its comfort**
108 **with planning to a 12 percent planning reserve.¹⁴**
109

110 **We note, once again, acknowledgement does not guarantee favorable**
111 **ratemaking treatment of future resource acquisition decisions. Indeed,**
112 **we are not convinced the Preferred Portfolio is the optimal portfolio.¹⁵**

¹² Duvall, Op. Cit. at lines 132-138 and lines 309-313.

¹³ Report and Order, PacifiCorp Integrated Resource Plan, April 1, 2010, Docket No.09-2035-01, p. 24.

¹⁴ Ibid., p. 29.

¹⁵ Ibid., p. 58.

113
114 The Division does not believe the Commission's Acknowledgement of the 2008 IRP in any
115 way supports the Company's level of FOTs.
116

117 **Q. Mr. Duvall claims that ratepayers could be at risk from over-building generation plant.**
118 **Do you have comments about that claim?**

119 A. Yes. Mr. Duvall is correct that a company might build more generation than it needs for its
120 native load or that it can support by wholesale sales. Such building might even appear
121 prudent at the time construction was undertaken and subsequently in hindsight prove to be
122 based upon forecasts that turn out to be wrong; nevertheless, ratepayers could be left to pay
123 for the over-capacity. This possibility aside, there is little evidence that PacifiCorp and its
124 ratepayers are currently facing this risk.
125

126 **Q. In confidential testimony, Mr. Duvall claims that ratepayers have benefited from the**
127 **Company postponement of a Lakeside II power plant and by relying on FOTs instead.**
128 **What do you think about this claim?**

129 A. I have three comments. First, the Company and ratepayers may be the fortuitous beneficiaries
130 of circumstances that were not specifically known or forecast by the Company when it
131 postponed Lakeside II. The depth of the economic recession was not well known at the time.
132 Had load growth continued or resumed at its previous pace that decision might not appear in
133 hindsight as attractive as it does now. Second, the savings claimed by Mr. Duvall is itself a
134 forecast and may or may not come to pass. The Division believes that, at best, it is premature
135 to praise the Company's FOT practices based upon the evidence from the Lakeside II
136 postponement. Third, Mr. Duvall's discussion of risk in this context seems to address solely
137 price or cost risk. He seems not to acknowledge that, regardless of cost, reliance upon the
138 power market creates a reliability risk. If the Company has insufficient owned generation to
139 meet demand and there is a regional shortage through any combination of low hydro, high
140 demand, unplanned shutdown, and transmission outages, the Company could be forced to
141 curtail load, thus passing significant costs on to customers.
142

143 **Q. Mr. Duvall points out that some level of FOTs were allowed into rates by the**
144 **Commission in Docket No. 09-035-23. What support do you believe this gives to the**
145 **Company's position?**

146 A. Mr. Duvall is correct that the NPC approved by the Commission in Docket No. 09-035-23
147 include wholesale market purchases. The Division is not challenging the current level of
148 FOTs given that, with the Company's current resources, they are necessary to meet
149 customers' needs. Nor, implicitly, in my direct testimony in this Docket filed on August 4,
150 2010 does the Division challenge the level of FOTs as set forth in the Company's 2008 IRP
151 Update. The Division believes that it would be imprudent for regulators to order the
152 Company to eliminate or to rapidly reduce FOTs. Such actions would not likely be in the best
153 interests of the Company or its ratepayers. The Division proposes to give the Company
154 incentives, first to keep to its own proposed level of FOTs through 2015, and then reduce the
155 level of FOTs somewhat by 2020 subject to further analyses and, of course, conditions on
156 those future dates. Therefore, Mr. Duvall's arguments about FOTs being in rates have no
157 impact on the Division's position.

158
159 However, any contention that FOTs have been allowed in rates is an indication of
160 Commission satisfaction with the current state of affairs should be disabused by the
161 Commission's comments regarding market purchases in its Report and Order on the
162 Company's 2008 IRP.¹⁶

163
164 **Q. What do you think about Mr. Duvall's characterization of Mr. Wheelwright's**
165 **comments regarding what the Commission might do regarding FOTs in this ECAM**
166 **Docket?**

167 A. I believe the quote taken from Mr. Duvall's rebuttal testimony cited above (see lines 50-53
168 above) mischaracterizes Mr. Wheelwright's testimony and certainly mischaracterizes the
169 Division's position. Contrary to Mr. Duvall's statement, Mr. Wheelwright does not
170 recommend that "the Commission should exclude market purchases or only allow cost
171 recovery for market purchases that cover a specific percentage of annual or peak load." as

¹⁶ See footnote 1, above.

172 should be clear from a complete reading of Mr. Wheelwright's testimony; nor does the
173 Division recommend as prudent such action by the Commission. Later in lines 334-351, Mr.
174 Duvall gives a more balanced presentation of what Mr. Wheelwright said. The Division's
175 position is that through the ECAM the Commission may provide incentives to the Company
176 to keep on track with its FOT goals as set forth in the Company's IRP.

177

178 **Q. As cited above, Mr. Duvall does not believe that an ECAM would reduce the**
179 **Company's incentives to build additional generation capacity. Do you agree with his**
180 **analysis?**

181 A. No. In economic theory there is always a trade-off between risk and return. In the
182 Company's ECAM proposal, the risk of recovery for NPC is reduced to nearly zero.
183 However, in the case of building plant or purchasing a plant, not all costs may be recovered
184 in rates. Furthermore, the construction of a major generation plant ties up a large amount of
185 funds that might be, in the short run at least, more profitably invested elsewhere. At a
186 minimum, there is an incentive to delay construction or purchase under the Company's
187 ECAM proposal, especially when the Company proposes that funds held in the ECAM pass-
188 through account earn interest at the Company's cost of capital.

189

190 There is another issue that deserves some comment in this regard. In lines 330-333 Mr.
191 Duvall suggests that since the Company only earns a return on its investment (and, under its
192 ECAM proposal, potentially on balances in the pass-through account), it has every incentive
193 to build. This "natural propensity" of a rate base regulated utility to build is theoretically
194 correct. However, it has seemingly not spurred the Company in recent years to an aggressive
195 generation acquisition program. There are several reasons that the Company might not
196 engage in an acquisition program. One reason is simply that load demand does not justify
197 acquisition of any additional generation capacity; this was one basis for the Company's
198 postponement of Lakeside II. Another reason is that there is a risk of recovery, but in the
199 Company's case, Mr. Duvall seems to argue that that is not a solid basis for the Company not

200 to build or otherwise acquire plant.¹⁷ There is a third reason that should be kept in mind in
201 this discussion and that is the demands and requirements of the parent holding company. If
202 the parent holding company has investment opportunities that are thought to be capable of
203 earning more than the allowed rates of return, then there will likely be pressure on the utility
204 to postpone or otherwise minimize investment so that funds can be distributed or kept by the
205 parent in order to pursue its other opportunities. In the short- to intermediate-term it could be
206 difficult for regulators to clearly discover such a diversion of funds, or possibly to do much
207 about it. Thus, an ECAM could help the utility to meet its load requirements while allowing
208 the parent holding company to make other capital investments.

209

210 **Q. What are your conclusions?**

211 A. In some respects the Division agrees with the positions taken by Mr. Duvall. Perhaps the
212 most significant agreement is that the Division agrees that it is not necessary to resolve the
213 FOT issue before an ECAM could be implemented. The Division also agrees that it is
214 possible that the Company could find itself in the future with too much generation capacity
215 and that's a risk to ratepayers, although there is no current evidence that that will happen.
216 While the Division remains concerned about the level of FOTs, the Division does not at this
217 point deem it prudent to eliminate FOTs altogether or reduce hastily. On the other hand, the
218 Division believes that the Company has yet to demonstrate that its current level of FOTs is
219 optimal. (As an aside, the Company's own IRPs have demonstrated that reducing FOTs
220 reduces risk with a negligible increase in costs.)¹⁸

221

222 In supporting his position, Mr. Duvall mischaracterizes the Division's position in places. The
223 Division disagrees with Mr. Duvall that there is no disincentive for the Company to acquire
224 owned resources as a result of an ECAM. The Commission Acknowledgement of the
225 Company's 2008 IRP does not represent support for its level of FOTs. While the IRP process

¹⁷ Duvall, op. cit., lines 318-333.

¹⁸ For a discussion of this and related issues see the Division's PacifiCorp 2008 Integrated Resource Plan, Report and Recommendations (Errata), Docket No. 09-2035-01, June 18, 2009, pp. 32-35; and Division Memorandum, *In the Matter of the Acknowledgment of PacifiCorp's 2006 Integrated Resource Plan*: Docket 07-2035-01 (Filed on May 30, 2007 as "2007 Integrated Resource Plan"), August 31, 2007, pp.42-43.

226 is one place to consider and develop the correct level of FOTs, the Commission may want to
227 consider giving guidance to the Company regarding FOTs that may have more “teeth” than
228 IRP non-acknowledgment. My ECAM design testimony, filed on August 4, 2010 in this
229 Docket, presents one method of doing so.

230

231 In sum, the most significant position of Mr. Duvall is his agreement with the Division that
232 the resolution of the market purchase issue need not be resolved in this Docket. Otherwise,
233 Mr. Duvall does not successfully rebut any Division position regarding FOTs, and the
234 Division continues to advocate for its position regarding FOTs both in this Docket and in the
235 IRP process.

236

237 **Q. Does this conclude your testimony?**

238 A. Yes

239