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BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

In the Matter of the Application of Rocky Mountain Power for Approval of Its Proposed Energy Cost Adjustment Mechanism	Docket No. 09-035-15
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PREFILED REBUTTAL TESTIMONY OF KEVIN C. HIGGINS

PHASE II

The Utah Association of Energy Users (“UAE”) hereby submits the Prefiled Rebuttal Testimony of Kevin C. Higgins in this docket on Phase II design issues.

DATED this 15th day of September, 2010.

/s/ _____
Gary A. Dodge,
Attorneys for UAE

CERTIFICATE OF SERVICE

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BEFORE
THE PUBLIC SERVICE COMMISSION OF UTAH

Rebuttal Testimony of Kevin C. Higgins

on behalf of

UAE

Docket No. 09-035-15

Phase II

September 15, 2010

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

2

3 **Introduction**

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

5 A. My name is Kevin C. Higgins. My business address is 215 South State
6 Street, Suite 200, Salt Lake City, Utah, 84111.

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

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

11 **Q. Are you the same Kevin C. Higgins who filed direct testimony on behalf of**
12 **UAE in Phase II of this proceeding?**

13 A. Yes, I am.

14

15 **Overview and Conclusions**

16 **Q. What is the purpose of your rebuttal testimony in this Phase II of the**
17 **proceeding?**

18 A. My rebuttal testimony responds to: (1) the discussion of renewable energy
19 credits (“RECs”) in the supplemental direct testimony of RMP witness Gregory
20 N. Duvall; and (2) the ECAM sharing mechanism presented in the direct
21 testimony of Division of Public Utilities (“Division”) witness Charles E Peterson.
22 I also discuss Mr. Peterson’s treatment of load growth in the ECAM design.

23 **Q. Please summarize your rebuttal testimony.**

24 A. (1) I recommend that the Commission defer making any determination
25 regarding the inclusion of REC revenues in an ECAM at this time. Instead, I
26 recommend that the Commission first consider on its merit the proper ratemaking
27 treatment of the incremental REC revenues identified in UAE's application for a
28 deferred accounting order in Docket No. 10-035-14. I believe that the new Major
29 Plant Additions ("MPA") rate case ("MPA II") is the appropriate venue for this
30 determination. In my opinion, the incremental REC revenues that have been
31 deferred starting February 22, 2010 should be recognized as a credit to customers
32 to be applied against any new revenue requirement determined in the MPA II
33 proceeding.

34 (2) I recommend against adoption of the Division's proposal to increase
35 the sharing percentage assigned to customers to 80 percent by 2015 if RMP meets
36 certain conditions; similarly, I recommend against adoption of the Division's
37 proposal to increase the customer sharing percentage again to 90 percent in 2020
38 if RMP meets certain additional conditions. I do not agree that the fundamental
39 design of the ECAM sharing percentage should be modified to increase customer
40 risk. The sharing percentage should reflect the need for RMP to have strong
41 incentives to perform efficiently and to minimize fuel and purchase power
42 expenses, subject to reliability constraints and risk management objectives. I
43 believe this objective can be reasonably accomplished with a 70/30 sharing
44 mechanism; increasing the customer responsibility beyond this apportionment is

45 excessive and unnecessary. Moreover, the Division's proposal, which involves
46 potential adjustments in 2015 and 2020, appears fundamentally incompatible with
47 the Division's core proposal that any ECAM be structured as a four-year pilot
48 program.

49 (3) I recommend against adoption of the Division's proposal to include an
50 additional tier in which 100 percent of cost responsibility would be allocated to
51 customers. I do not agree that absolving the Company of sharing cost
52 responsibility within any tier is appropriate. Allocating 70 percent of the
53 deviation to customers (as occurs in my recommended design) is already a
54 significant reduction in risk for the Company (and increase in risk to customers)
55 relative to the status quo.

56 (4) In my direct testimony, I recommended inclusion of a load growth
57 adjustment factor in the ECAM rate design. The Division does not include an
58 explicit load growth adjustment because the mechanics of the Division's proposal
59 already incorporate the effects of load growth. Thus, there is no conceptual
60 inconsistency between the Division's treatment of load growth and my
61 recommended treatment, although the Division's measurement of incremental
62 revenues from load growth is broader than mine because it includes incremental
63 margins from distribution (whereas my adjustment is limited to generation and
64 transmission).

65

66 **Response to Mr. Duvall**

67 **Q. What does Mr. Duvall propose in his supplemental testimony with respect to**
68 **the treatment of REC revenues?**

69 A. Mr. Duvall amends RMP's ECAM proposal to include REC revenues in
70 the ECAM calculation; although Mr. Duvall does not explicitly address the
71 mechanics of his proposal, the implication of adopting his recommendation would
72 be to include in the Company's proposed ECAM balancing account any
73 deviations in REC revenues relative to the REC revenues already reflected in
74 Utah rates.

75 Mr. Duvall supports his recommendation by stating that REC revenues are
76 "volatile and unpredictable and fit well with the NPC included in the ECAM."
77 Mr. Duvall also notes that REC revenues are dependent on the actual levels of
78 generation from renewable resources such as wind and hydro resources; Mr.
79 Duvall further asserts that "REC revenues are dependent upon illiquid, volatile,
80 and non-transparent market prices."¹

81 **Q. What is your response to Mr. Duvall's proposal?**

82 A. I recommend that the Commission defer making any determination
83 regarding the inclusion of REC revenues in an ECAM at this time. Instead, I
84 recommend that the Commission first consider on its merit the proper ratemaking
85 treatment of the incremental REC revenues identified in UAE's application for a
86 deferred accounting order in Docket No. 10-035-14. Adopting RMP's new
87 recommendation to include RECs in an ECAM at this time would effectively
88 preempt consideration on its merit of a ratemaking determination associated with

¹ Supplemental direct testimony of Gregory N. Duvall – Phase II, lines 22-26.

89 UAE's application, even though UAE's proposal has serious public interest
90 implications and UAE's application preceded RMP's filing of its revised position
91 on the inclusion of REC revenues in an ECAM.

92 In my Phase II direct testimony, I recommended that the deferred REC
93 revenues associated with UAE's application for a deferred accounting order
94 should be addressed and incorporated into rates in the next rate case proceeding.
95 RMP has since filed a the MPA II rate case and is proposing to increase rates by
96 \$39 million associated with that application. In the MPA II application, RMP is
97 also proposing to increase rates by \$30.8 million associated with the allowed
98 recovery from the Company's first MPA case, and to recover another \$15.7
99 million in deferrals from that case.

100 I believe that the MPA II proceeding is the appropriate venue for
101 addressing on its merit the ratemaking treatment of the revenues identified and
102 issues raised by UAE's application. In my opinion, the incremental REC
103 revenues that have been deferred starting February 22, 2010 should be recognized
104 as a credit to customers to be applied against any new revenue requirement
105 determined in the MPA II proceeding.

106 **Q. Why do you believe the MPA II docket is the appropriate venue for**
107 **addressing on its merit the ratemaking treatment of the incremental REC**
108 **revenues addressed in UAE's application?**

109 A. First, as I understand it, UAE's application for a deferred accounting order
110 for incremental REC revenues preceded the proposal of any party in this docket to

111 include REC revenues in an ECAM. It would thus be appropriate to allow UAE
112 to make its case for, and for the Commission to have an opportunity to consider,
113 the most appropriate method for recognizing the deferred incremental REC
114 revenues in rates.

115 Second, as proposed by RMP, the rate increase for MPA II, and recovery
116 of deferred costs from the first MPA case, would be implemented January 1,
117 2011, which will be prior to any rate change associated with implementation of an
118 ECAM. Because the incremental REC revenues identified in UAE's application
119 are not currently reflected in rates, but properly should be credited to customers,
120 current rates are, in my opinion, too high. Assessing a further rate increase on
121 January 1, 2011, without simultaneously recognizing the value of the deferred
122 RECs as a credit to customers would cause rates to diverge even further from
123 reasonable levels, an outcome that plainly would be inequitable for customers.
124 Simply put, there is a strong public interest basis for recognizing the deferred
125 RECs in rates sooner rather than later.

126 **Q. In your direct testimony you recommended that a 70/30 sharing mechanism**
127 **should be implemented if an ECAM is adopted. Are you opposed to the**
128 **sharing between customers and RMP of the incremental REC revenues**
129 **addressed in UAE's Application?**

130 A. Yes. In my opinion, 100 percent of the REC revenues currently being
131 deferred should be credited to customers; this is the most reasonable action that
132 can be taken in response to the extraordinary and unforeseeable orders-of-

133 magnitude increase in REC revenues that RMP experienced at the time the most
134 recent general rate case was being concluded. The crediting to customers of 100
135 percent of the incremental REC revenues (above the level of RECs reflected in
136 rates) should continue until the start of the rate-effective period associated with
137 the next general rate case. This credit can properly expire upon the start of the
138 rate-effective period following the next general rate case, because at that time,
139 new base rates will reflect a revised going-forward level of REC revenues.

140 **Q. What if the Commission ultimately determines that REC revenues are**
141 **appropriately included in an ECAM?**

142 A. If the Commission determines that it is appropriate to include REC
143 revenues in an ECAM, then I recommend that such inclusion be initiated
144 following the next general rate case, after the action I am recommending above
145 has run its course.

146

147 **Response to Mr. Peterson**

148 **Q. Please respond to the sharing proposal put forward by the Division.**

149 A. As explained in Mr. Peterson's direct testimony, the Division is proposing
150 a sharing mechanism that is comprised of a deadband of plus or minus two
151 percent of the NPC that are in rates (comparable to plus or minus two percent of
152 Base NPC). For NPC deviations outside the deadband, but within 30 percent of
153 NPC in rates, the Division is proposing a sharing arrangement in which 70 percent

154 of the responsibility is assigned to customers and 30 percent is assigned to RMP.

155 I have no disagreement with these two aspects of the Division's proposal.

156 However, the Division is also proposing that the sharing percentage
157 assigned to customers may be increased to 80 percent by 2015 if RMP meets
158 certain conditions pertaining to front-office transactions and the Commission
159 approves the Company's hedging program, and increased again to 90 percent in
160 2020 if RMP meets additional conditions pertaining to front-office transactions.

161 Further, the Division is proposing that NPC deviations that exceed 30 percent of
162 the NPC in rates be allocated 100 percent to customers. I disagree with these
163 aspects of the Division's proposal.

164 **Q. Please explain the basis of your disagreement with these aspects of the**
165 **Division's proposal.**

166 A. I appreciate that the Division and other parties have concerns with RMP's
167 reliance on front-office transactions to cover much of the Company's projected
168 capacity deficiency in its Integrated Resource Plan ("IRP"). These concerns are
169 properly addressed in the IRP process and, if necessary, in a general rate case.
170 And if a party objects to the prudence of the level of front-office transactions, this
171 issue can also be addressed in an ECAM docket. However, I do not agree that the
172 fundamental design of the ECAM sharing percentage should be modified to
173 increase customer risk if RMP meets certain front-office transaction benchmarks,
174 as the Division has proposed. In my view, the sharing percentage should reflect
175 the need for RMP to have strong incentives to perform efficiently and to minimize

176 fuel and purchase power expenses, subject to reliability constraints and risk
177 management objectives. I believe this objective can be reasonably accomplished
178 with a 70/30 sharing mechanism, but that increasing the customer responsibility
179 beyond this apportionment is excessive and unnecessary.

180 Moreover, the Division's front-office transaction proposal, which involves
181 potential adjustments in 2015 and 2020, appears fundamentally incompatible with
182 the Division's core proposal that any ECAM be structured as a four-year pilot
183 program. By its nature, a time-limited pilot program should be structured using a
184 basic set of parameters throughout its term and should not contain provisions that
185 call for basic parameter adjustments and the end of, or even beyond, its term, as
186 the Division is proposing. If the ECAM is adopted, and if there are compelling
187 reasons to continue it beyond the term of the pilot, the basic design parameters of
188 the ECAM can be addressed at that time.

189 I also oppose the Division's proposal to include an additional tier in which
190 100 percent of cost responsibility would be allocated to customers. While I
191 recognize that the Division's proposal is intended to address large deviations from
192 Base NPC, I do not agree that absolving the Company of sharing cost
193 responsibility within that tier is appropriate. Allocating 70 percent of the
194 deviation to customers (as occurs in my recommended design) is already a
195 significant reduction in risk for the Company (and increase in risk to customers)
196 relative to the status quo.

197 **Q. In your direct testimony you proposed that a load growth adjustment be**
198 **included as part of any ECAM design, and support for this concept was also**
199 **offered by Office of Consumer Services witness Daniel E. Gimble and**
200 **Western Resource Advocates witness Nancy L. Kelly in their respective**
201 **direct testimonies. Can you comment on the apparent absence of an explicit**
202 **load growth adjustment in the Division’s proposal?**

203 A. An explicit load growth adjustment is not necessary in the Division’s proposal
204 because the mechanics of the Division’s proposal already incorporate the effects
205 of load growth. That is, the Division proposes to use NPC benchmarks that are
206 based on total dollar values of NPC and revenues, in contrast to the “per MWH”
207 measurements proposed by RMP. If Base NPC and Actual NPC are measured on
208 a “per MWH” basis, then an explicit load growth adjustment is needed for
209 incorporating the value of incremental margins earned on any increase in retail
210 sales, as discussed in my direct testimony.

211 However, because the Division not using a “per MWH” measurement of
212 NPC as basis of the ECAM, but instead is proposing to calculate the ECAM by
213 measuring the difference between actual total NPC and forecasted total NPC,
214 adjusted for the difference between actual total revenue and forecasted total
215 revenue, the effects of any incremental margins from load growth will already be
216 included in the Division’s calculation; i.e., incremental margins are captured in
217 the measurement of actual total revenue. Indeed, the Division’s approach is more
218 inclusive of incremental margins than my proposal, because the Division’s

219 approach includes as a credit in the ECAM the incremental margins associated
220 with the distribution function, whereas my recommended load growth adjustment
221 factor is limited to crediting to customers the incremental margins associated with
222 the generation and transmission functions.

223 The upshot is that there is no conceptual inconsistency between the
224 Division's treatment of load growth and my recommended treatment, although the
225 Division's measurement of incremental revenues from load growth is broader
226 because it includes incremental margins from distribution.

227 Finally, I note that the Division's proposal would credit (or charge)
228 customers for the incremental (or decremental) margins associated with the
229 difference between actual and forecasted load within the test period used for
230 setting base rates (as well as for the subsequent period), whereas my load growth
231 adjustment would only apply to ECAM measurement periods that occur after the
232 close of the test period used to set rates in the last general rate case. I believe the
233 latter approach is preferable. As I stated in my direct testimony, the purpose of
234 the adjustment factor is to account for the effects of load growth over time; thus, it
235 is appropriate to begin applying it in the first month following the close of the test
236 period used to set Base NPC in a general rate case. In my opinion, the adjustment
237 should not be used to correct or true up the test period load forecast. In my view,
238 this would be an overly-broad application of the adjustment.

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

240 **A.** Yes, it does.