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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 POST-HEARING BRIEF OF THE DIVISION OF PUBLIC UTILITIES
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Consistent with instructions from the Public Service Commission (Commission), the Division of Public Utilities (Division) submits this post-hearing brief, and urges the Commission to adopt the energy cost adjustment mechanism (ECAM) proposed by the Division.

I. INTRODUCTION

PacifiCorp (also the Company) initiated this ECAM docket in March 2009 by filing an application and direct testimony, consisting of a total of approximately 13 narrative pages, from two witnesses.¹ The Commission then sought and received information from parties regarding the appropriate scope of issues for this docket. As a result, the Commission in its order of June 18, 2009, established a bifurcated proceeding in which Phase I would address whether an ECAM

¹ In August 2009, the Company filed additional testimony in support of its application.

was in the public interest, and Phase II would explore the design of an ECAM.² Subsequently, in August 2009, prior to the filing of additional testimony and the hearing to address Phase I issues, the Company filed its motion for Ruling on Implementation of ECAM, which addressed the relationship between this docket and the Company's general rate case in Docket No. 09-035-23. In January 2010, a hearing was held to address Phase I issues. Notably, the Company alone supported its ECAM proposal. Indeed, all the intervenors, except for the Division, urged the Commission to find that the docket need not proceed to Phase II. The Division stated that while the specific ECAM proposed by the Company was not in the public interest, an ECAM possibly could be designed that could be in the public interest, and that the matter should proceed to Phase II.

In its February 8, 2010 order (2010 Order), the Commission moved the proceeding into Phase II. In doing so, however, the Commission did not narrow the scope of the inquiry, for example, by either accepting or rejecting the Company's proposal or by ordering parties to look at specific categories of net power costs (NPC). In the 2010 Order, the Commission ordered that "[w]e give notice that we will proceed to Phase II of this docket to consider PacifiCorp's proposed ECAM and modifications or alternatives which the parties might propose."³ In addition, the Commission specifically requested that the parties address two issues raised by the Office of Consumer Services (Office): "[I]s the company's use of natural gas hedging and the level of and reliance on market energy affected by the use of an ECAM."⁴

In this brief, the Division will address the critical issues before the Commission rather than discussing every possible issue. As this brief explains, the Division's ECAM proposal satisfies the statutory requirements for an ECAM because it is in the public interest, allows

² See June 18, 2009 order.

³ 2010 Order at page 3.

⁴ 2010 Order at page 2.

recovery of prudently incurred costs, and sufficient record evidence exists to support adopting the ECAM as proposed by the Division.

II. THE DIVISION'S ECAM PROPOSAL

The Division's ECAM proposal provides a reasonable framework for an ECAM. Specific components are discussed below.

The Division proposes that its ECAM program be implemented as a four-year pilot program.⁵ After four years, the Company must file to continue or modify the ECAM.

The Division's ECAM proposal specifically relies upon a general rate case for implementation. The general rate case would establish NPC baseline, which would be used until the next general rate case. In the same rate case that determined the NPC baseline, the Commission would determine the base revenue requirement for the ECAM. The Company would be required to file a general rate case at least every three years to keep the NPC and revenue baselines current.

The Division provides specific formulae to calculate the ECAM:

$$Db = ((NPCa - NPCf) / NPCf)$$

If Absolute(Db) is less than or equal to 2.0 percent, then stop, no further action is warranted. Otherwise, proceed to next formula.

$$Ea = 98\% \times P \times [(NPCa - NPCf) - (Ra - Rf)]$$

- ✓ Db is dead band.
 - ✓ Ea is the annual ECAM adjustment.
 - ✓ 98% accounts for the dead band.
 - ✓ P is the sharing ratio approved by the Commission.
 - ✓ NPCa equals the actual annual NPC.
 - ✓ NPCf is the forecast NPC approved by the Commission in a general rate case.
 - ✓ Ra is actual annual revenues.
 - ✓ Rf is the forecast revenues over the annual ECAM period approved by the Commission in a general rate case.
- The true-up of the ECAM pass-through account be performed annually

⁵ The Company does not object to a pilot program, and has its own suggestions regarding term and continuation. See Transcript, Phase II, Volume I, Testimony of Greg Duvall, pages 140-142.

- The sharing ratio “P” has three tiers.
 - ✓ At plus and minus 2 percent from the baseline NPC, “P” equals zero (the “dead band).”
 - ✓ Between greater plus or minus 2 percent and plus or minus 30 percent, “P” initially equals 70 percent.
 - ✓ If certain conditions are met “P” in the second tier may be increased to 80 percent before the end of 2015, and raised again to 90 percent in 2020.
 - The conditions for 2015 include
 - The Commission approves a hedging program for the Company;
 - The Company complete a study of the benefits and risks of its FOT purchases; and
 - The Company meets or beats the 7 percent target for FOTs vs. system peak power.
 - The condition for 2020 is
 - The Company meets or beats the 5.5 percent target for FOTs vs. system peak power.
 - ✓ At plus or minus 30 percent or greater, “P” becomes 100 percent.⁶

Note that renewable energy credits (RECs), SO₂ credits and wheeling revenues are not included in the Division’s ECAM calculations. Their treatment should be determined outside of the ECAM.

The Division’s proposal contains sharing bands that include a dead band. The Division proposes that the sharing band outside of the dead band may be expanded if the Company meets certain criteria involving front office transactions (FTOs) and the acceptance or acknowledgment of the Company’s hedging programs by the Commission. Note that there is also an outer band outside which the Company is permitted to recover all prudently incurred NPC.

The rates adjusted pursuant to the ECAM will be set on an interim basis pending the Division’s audit. The ECAM will be implemented through a pass-through account and at the end of the annual ECAM period, the Company will request that the Commission adjust rates based upon the balance in the account. The ECAM will be trued-up on an annual basis.

⁶ Direct Testimony, Phase II, Charles Peterson, lines 412-446.

The Division proposes that the ECAM begin January 1, 2011, with a true-up filing made about a year later. The ECAM surcredits or surcharges would begin around the spring of 2012. The Company's proposal to file on or about December 15th each year is unacceptable because the time for auditing prior to the Company's planned implementation date is insufficient and the time is prejudicial to parties responding to the filing. Rather, the Division's proposal provides for an ECAM filing after the completion of a calendar year, leaving a reasonable period of time for analysis prior to the establishment of interim ECAM "true-up" rates.

III. UTAH'S ECAM STATUTE

Enacted in 2009, Utah Code Ann. § 54-7-13.5 specifically addresses energy balancing accounts. It declares that a balancing account "does not constitute impermissible retroactive ratemaking or single-issue ratemaking."⁷ The Commission may "authorize an electrical corporation to establish an energy balancing account."⁸ For an energy balancing account to become effective, the Commission must find that "the energy balancing account is: (i) in the public interest; [and] (ii) for prudently-incurred costs."⁹

Furthermore, the statute addresses other elements of an ECAM. The statute authorizing the establishment of energy balancing accounts also addresses when an energy balancing account is to be implemented, stating that it will be "implemented at the conclusion of a general rate case."¹⁰ Specific requirements concerning bill surcharges and bill surcredits are addressed in the statute.

⁷ Utah Code Ann. § 54-7-13.5(4)(c).

⁸ Utah Code Ann. § 54-7-13.5(2)(a).

⁹ Utah Code Ann. § 54-7-13.5(2)(b)(i) and (ii).

¹⁰ Utah Code Ann. § 54-7-13.5(2)(b)(iii).

IV. THE DIVISION'S ECAM PROPOSAL IS IN THE PUBLIC INTEREST AND IT IS FOR PRUDENTLY-INCURRED COSTS

An ECAM proposal can, and the Division's detailed ECAM proposal does, satisfy the public interest standard required by Utah Code Ann. § 54-7-13.5(2)(b)(i). Additionally, the Division's ECAM proposal allows for the recovery of prudently incurred costs required by Utah Code Ann. § 54-7-13.5(2)(b)(ii). The Commission should approve the adoption and implementation of the Division's ECAM proposal.

a. An ECAM Can Satisfy the Public Interest Standard

An ECAM can be in the public interest. An ECAM may improve a company's ability to earn its authorized rate of return, which may improve its stand-alone bond rating. Additionally, an ECAM can aid a company in recovering unpredictable increased costs, such as NPCs that can be outside the company's control.

"The Division believes that it is in the public interest that PacifiCorp remain a financially strong and stable utility."¹¹ Due to not earning its authorized return for several years, the Company's stand-alone bond rating has fallen to BBB or Baa from its historical A rating.¹² A continuation of the Company's inability to "earn its authorized rate of return will be detrimental to both the Company and, eventually, to ratepayers as well."¹³ Unpredictable NPCs higher than that included in rates, could have been "[p]art of the reason for this lower profitability."¹⁴ The Company does make a reasonable and plausible argument that unpredictably higher net power costs than anticipated could, "in extreme cases ... be debilitating to the financial health of the Company."¹⁵ General rate cases do not appear to the Division to be "good forums for the

¹¹ Direct Testimony, Phase I, Charles Peterson, lines 129-130.

¹² Direct Testimony, Phase I, Charles Peterson, lines 130-133.

¹³ Direct Testimony, Phase I, Charles Peterson, lines 133-135.

¹⁴ Direct Testimony, Phase I, Charles Peterson, lines 135-136.

¹⁵ Direct Testimony, Phase I, Charles Peterson, lines 141-142.

Company to recover such costs, particularly due to the bar to retroactive ratemaking.”¹⁶ Thus, given the unpredictable and uncontrollable nature of these costs, implementation of some form of ECAM is justified. In Phase I of this case, many of the parties’ concerns addressed the specific design of an ECAM rather than whether an ECAM could be in the public interest.¹⁷ For the reasons set forth above, an ECAM can be in the public interest.

b. The Division’s ECAM Proposal Satisfies the Public Interest Standard

The Division’s ECAM proposal is designed to meet the public interest standard. Company incentives are addressed, and risk shifting between the Company and ratepayers is discussed specifically. Additionally, the Division’s proposal speaks to the issues raised by the Office regarding the Company’s hedging policies and practices and market purchase activities. The Division has set forth specific conditions for an acceptable ECAM. These conditions are:¹⁸

1. That the mechanism does not reduce company incentives to provide electricity to customers at the lowest cost and least risk prudently possible.
2. That the mechanism does not reduce incentives to the Company to cover its load, and prospective load growth, with owned generation rather than through market purchases.
3. That the mechanism does not unreasonably shift risk from the Company to ratepayers.
4. That incremental power costs be offset by any incremental revenues before any additions are made to a balancing account.¹⁹

The Division’s proposal satisfies the first and third criteria set forth above by containing a dead band and sharing bands designed to provide or maintain the Company’s incentive to operate efficiently. The Division’s proposal contains a 2 percent dead band and a 70 percent sharing

¹⁶ Direct Testimony, Phase I, Charles Peterson, lines 142-144.

¹⁷ Rebuttal Testimony, Phase I, Charles Peterson, lines 30-35.

¹⁸ See Direct Testimony, Phase II, Charles Peterson, lines 74-84.

¹⁹ The Division set forth a fifth criterion, that the mechanism only covers those costs that are truly outside of Company control and cannot be anticipated and/or significantly mitigated. The Division, while still agreeing with the concept in principle, has determined that, in application, the criterion may create perverse incentives; thus the Division has “backed away” from this fifth criterion. See Direct Testimony, Phase II, Charles Peterson, lines 503-517.

percentage so that “PacifiCorp management and owners have enough self-interest at stake, or ‘skin in the game,’ that would influence them to continue to make concerted efforts to prudently lower costs and reduce risks.”²⁰ The dead band provides the Company with an “adequate interest to keep the NPC at, or a bit below, the NPC that was included in rates.”²¹ “The intent of the sharing band is to give enough incentive to management that . . . the Company has significant dollars at risk that they will maintain the mode of patience that they now have to operate as efficiently as possible, because they still are putting substantial shareholder funds at risk.”²² Moreover, the sharing band “leaves [the Company] the incentives to try to improve their control over time of ECAM costs.”²³ The Company has the incentive to search for different ways of mitigating the volatility by looking at gas storage and ways to improve its forecast.²⁴ The dead band, 2 percent above or below the NPC set in rates, provides the Company and its stockholders with some risk “to justify a relatively high authorized ROE”²⁵ and mitigates, if not eliminates, the need for ad hoc adjustments to the Company’s authorized rate of return.

Four parties in the case support a 70-30 sharing mechanism, in some instances as a secondary position to their first position that an ECAM should not be adopted now: the Division, the Office, the Utah Association of Energy Users (UAE), and Western Resource Advocates and Utah Clean Energy. The Office supports such a sharing if there is an ECAM ordered, saying “we believe that the Company needs to have an economic stake in terms of making sure that it makes reasonable decisions in terms of the way it operates, maintains, upgrades its plant . . . to promote efficient operations.”²⁶ Additionally, if an ECAM is adopted,

²⁰ Direct Testimony, Phase II, Charles Peterson, lines 459-462.

²¹ Direct Testimony, Phase II, Charles Peterson, lines 262-263 and lines 482-489.

²² Transcript, Phase II, Volume II, Testimony of Charles Peterson, page 376, lines 8-14.

²³ Transcript, Phase II, Volume II, Testimony of Charles Peterson, page 425, lines 14-16.

²⁴ Transcript, Phase II, Volume II, Testimony of Charles Peterson, page 425, lines 19-22.

²⁵ Direct Testimony, Phase II, Charles Peterson, lines 267-268.

²⁶ Transcript, Phase II, Volume II, Testimony of Daniel Gimble, page 467, lines 20-25 and page 468, line 1.

Mr. Kevin Higgins, witness for UAE, supports a 70-30 sharing band because it “establishes a reasonable threshold of materiality to ensure sufficient management incentive to control costs as well as to take into consideration the magnitude of change that is reasonable if Utah is to migrate from the status quo, in which the sharing weight is effectively 0 percent customer and 100 percent Rocky Mountain Power”²⁷ and “bears some general correspondence to the sharing provisions the Company agreed to in Wyoming in 2006.”²⁸ Ms. Nancy Kelly, witness for Western Resource Advocates and Utah Clean Energy, provides an example demonstrating how a 70-30 sharing mechanism provides a financial incentive to manage costs that is not present without it.²⁹ Ms. Kelly concludes that a sharing band is a greater incentive to manage costs than a prudence review³⁰ as does Mr. Higgins.³¹

Sharing bands are not punitive, and the Company’s attempt to discredit sharing bands is unpersuasive.³² Indeed, even with sharing bands, any ECAM provides the Company with a better opportunity to recover more of its prudently incurred NPCs than is available under the current regulatory scheme. After repeated criticisms of sharing bands, the Company admits that the Division’s proposed sharing band would provide the Company with the appropriate incentives to operate efficiently and an opportunity to recover some, but not all, excess power costs in contrast to the zero percent recovery opportunity that the Company has now.³³ When asked if “you’d just be happy about the fact that you’re going to pay a buck and only get 70

²⁷ Transcript, Phase II, Volume II, Testimony of Kevin Higgins, page 506, lines 10-17.

²⁸ Transcript, Phase II, Volume II, Testimony of Kevin Higgins, page 506, lines 18-20.

²⁹ Surrebuttal Testimony, Phase II, Nancy Kelly, lines 54-97.

³⁰ Surrebuttal Testimony, Phase II, Nancy Kelly, lines 114-117.

³¹ Transcript, Volume II, Phase II, Testimony of Kevin Higgins, page 506, lines 21-25 and page 507, lines 1-4.

³² See Rebuttal Testimony, Phase II, Greg Duvall, lines 106-132.

³³ Transcript, Phase II, Volume I, Testimony of Greg Duvall, page 41, lines 1-6.

cents,” the Division perceptively noted, “Right now you [the Company] don’t even get the 70 cents.”³⁴

The Division’s proposal meets the second criterion set forth above – that dealing with building plant – by remaining “at least neutral in this regard.”³⁵ The Division’s proposed sharing bands provide the Company an incentive to act efficiently. Additionally, by allowing the sharing bands to change in response to the Company’s resource decisions going forward,³⁶ it leaves the Company discretion over its resource choices. Note that this criterion can be met not only by building plant but also through long-term power purchase agreements³⁷

The Division’s proposal meets the fourth criterion set forth above – that incremental revenues offset incremental costs. Because at the margin the Company’s non-NPC costs “are mostly fixed, at least over a relatively short time frame,”³⁸ “incremental NPC costs above the NPC baseline are at least partially offset by incremental revenues.”³⁹ Therefore the Division proposes that any ECAM include a symmetrical revenue adjustment to account for incremental revenues due to load growth or missed forecasts.

Additionally, the Division looked at four functions of rates as described by Dr. James C. Bonbright and discussed by Mr. Peterson in his testimony. These four functions can be summarized as: (1) The Capital Attraction Function, (2) The Efficiency or Incentive Function, (3) The Consumer Rationing Function, and (4) The Income-Distribution Function.⁴⁰ The

³⁴ Transcript, Phase II, Volume II, Testimony of Charles Peterson. page 343, lines 17-21.

³⁵ Direct Testimony, Phase II, Charles Peterson, lines 476-477.

³⁶ The Division proposed that the sharing band move from 70/30 to 80/20 and eventually to 90/10 as the Company meets its integrated resource plan (IRP) targets for FOTs and gains Commission approval of its hedging plans.

³⁷ Direct Testimony, Phase II, Charles Peterson, lines 477-480.

³⁸ Direct Testimony, Phase II, Charles Peterson, lines 496-498.

³⁹ Direct Testimony, Phase II, Charles Peterson, lines 494-495.

⁴⁰ Direct Testimony, Phase II, Charles Peterson, lines 519-527. Note also that the Company noted restrictions affecting customers’ ability to decrease costs, commenting that in the short term “there’s not a whole lot you can do except turn off the lights and turn down the thermostat.” Transcript, Phase II, Volume I, Testimony of Greg Duvall,

Division's proposal serves the functions above, except possibly the consumer rationing function.⁴¹ Under the Division's proposal, the Company will have an enhanced opportunity to "improve the reliability of the Company's cash flows over the status quo"⁴² which should "enhance capital attraction."⁴³ "The Division also believes that power cost fluctuations may become large enough that the Company could be financially damaged if it were not able to reasonably recover costs from large fluctuations. Avoiding such financial damage, would, in the long run, be in the interest of ratepayers and the public, as well as the Company."⁴⁴ The Division's proposal also "maintains Company incentives to continue to pursue least cost/least risk strategies."⁴⁵ Additionally, the Division's proposal "maintains a reasonable balance between the interests of customers and the Company in distributing income from ratepayers to the Company."⁴⁶ The Division's proposal is, as previously discussed, designed to maintain the Company's incentives to operate efficiently. Additionally, the Division's proposal ensures that the Company will recovery only prudently incurred costs and, thus, strikes an appropriate balance between ratepayers and shareholders.

Although other parties object to the adoption of an ECAM as their primary position, some nonetheless offer alternative proposals concerning ECAM design. These alternative ECAM proposals contain features that are not necessary to meet the criteria set forth above, and, in some instances, impose unneeded complexity.

For example, Mr. Maurice Brubaker, witness for the Utah Industrial Energy Consumers (UIEC), proposes two features for an ECAM, neither of which meet either the Division's criteria

page 144, lines 20-21. In the long term, the customer can incorporate energy efficiency equipment and concepts. Id. at lines 22-24.

⁴¹ See Direct Testimony, Phase II, Charles Peterson, lines 529-538.

⁴² Direct Testimony, Phase II, Charles Peterson, lines 529-530.

⁴³ Direct Testimony, Phase II, Charles Peterson, line 529.

⁴⁴ Transcript, Phase II, Volume II, Testimony of Charles Peterson, page 302, lines 20-25 and page 303, line 1.

⁴⁵ Direct Testimony, Phase II, Charles Peterson, lines 530-532.

⁴⁶ Direct Testimony, Phase II, Charles Peterson, lines 537-538.

or the Bonbright criteria discussed above. He proposes performance standards for coal-fired production, Company owned coal mines, and wind resources. The proposed performance standards, as defined by Mr. Brubaker, are setting the Company up for failure: with a five year average being used, the Company would fail to meet the standards approximately one half of the time unless efficiency was continuously improved. Proposed performance standards could punish the Company.⁴⁷ Similar defects exist in Mr. Brubaker's proposal concerning wind generation performance standards because there is no substantive support for his criteria.⁴⁸ His wind proposal is not in the public interest because it lacks "quantified justification" and "would increase the burden on the Company and regulators."⁴⁹ Mr. Peterson testified:

Perhaps most problematic is the frequently repeated requirement that should the Company fail to meet the proposed standards, then PacifiCorp ha[s] a positive obligation to 'establish that it operated, maintained, and managed its resources appropriately, and to the extent that it experienced a shortfall below the performance standards[,] acquired appropriate substitute resources on a least cost basis' in order to avoid a disallowance.⁵⁰

"Second guessing" the Company and "protracted analysis and litigation"⁵¹ could result from implementation of Mr. Brubaker's proposal. Mr. Brubaker also proposes seasonal tracking and charging of classes. This concept should be proposed in a general rate case where cost of service issues are presented, not in this docket.⁵²

Mr. Higgins, of UAE, proposes a load growth adjustment factor,⁵³ something not recognized in PacifiCorp's Idaho ECAM⁵⁴ which was the result of a negotiated settlement. Ms. Kelly and Mr. Gimble also support this concept. This concept is similar to the Division's

⁴⁷ Rebuttal Testimony, Phase II, Charles Peterson, lines 95-102.

⁴⁸ Rebuttal Testimony, Phase II, Charles Peterson, lines 104-107.

⁴⁹ Rebuttal Testimony, Phase II, Charles Peterson, lines 69-70.

⁵⁰ Rebuttal Testimony, Phase II, Charles Peterson, lines 127-131, footnote omitted.

⁵¹ Rebuttal Testimony, Phase II, Charles Peterson, lines 132-134.

⁵² Surrebuttal Testimony, Phase II, Charles Peterson, lines 556-564.

⁵³ Direct Testimony, Phase II, Kevin Higgins, lines 92-104.

⁵⁴ Transcript, Phase II, Volume I, Testimony of Greg Duvall, page 116, lines 22-25 and page 117, line 1.

revenue adjustment,⁵⁵ which, among other things, insures that the Company will only recover its prudently incurred NPC. The Division has consistently recognized and advocated its revenue adjustment. Parties other than the Company recognize the clear need for something along these lines. Although Mr. Higgins' approach is somewhat different from the Division's, in essence it tries to solve the same problem the Division solves with its revenue adjustment. The Company's arguments against a revenue adjustment are wholly unpersuasive. Costs other than NPCs have been fixed in the Company's budgets. These fixed costs include such things as distribution plant, long-term debt, and employee count/wage expense.⁵⁶ Because these costs are "largely fixed at this margin . . . it's completely appropriate to offset the marginal revenue that the Company—or the marginal costs, which are almost a hundred percent net power costs, with the marginal revenue that the Company receives."⁵⁷ Indeed, if there were no adjustment, the Company would "collect, through the ECAM, the net power cost . . . and the only cost that . . . [the Company] incurred was the net power cost, so the revenue becomes just free money to the Company."⁵⁸

Unlike some parties, the Division did not include Renewable Energy Credits (RECs), in its ECAM proposal. One reason is that that RECs historically have not been included in NPCs, and there is no persuasive reason to start including them now.⁵⁹ Also, RECs should not be included in an ECAM because "they relate to revenues received for an intangible attribute of certain generation properties recently created by government action and do not represent a power

⁵⁵ Rebuttal Testimony, Phase II, Charles Peterson, lines 374-380.

⁵⁶ Transcript, Phase II, Volume II, Testimony of Charles Peterson, page 349, lines 21-25.

⁵⁷ Transcript, Phase II, Volume II, Testimony of Charles Peterson, page 350, lines 1-6.

⁵⁸ Transcript, Phase II, Testimony of Charles Peterson, page 349, lines 6-10.

⁵⁹ In essence the Company argues that since REC revenues are unpredictable and outside of the Company's control, they have the same characteristics as NPC cost items and hence should be included in the ECAM. With this logic, ultimately the Company could argue that any cost or revenue item should be in the ECAM See Supplemental Direct, Greg Duvall, lines 20-29.

‘cost’ incurred by the Company.”⁶⁰ Because the customers are paying for 100% of the turbines’ costs, the customers should get the full benefit of the RECs, rather than sharing them with the Company. The Office appears to support inclusion of RECs in an ECAM if an ECAM is adopted.⁶¹ Of note, Mr. Higgins, who originally proposed including RECs in an ECAM, ultimately “respectfully request[ed] that the Commission defer making any determination regarding the inclusion of REC revenues in the ECAM at this time.”⁶²

In contrast to the Division’s ECAM proposal, the Company’s ECAM proposal is not in the public interest. First, the Company’s ECAM proposal immediately shifts all risks associated with NPC from the Company, where those risks reside today, to ratepayers. “In the ECAM, as the Company as proposed it, the ratepayers will take upon them the risk for the forecast errors.”⁶³ Second, there is no sharing and thus the Company has no “skin in the game.” With complete recovery the Company’s incentive to act efficiently is largely undermined. To maintain the Company’s incentive, “[t]he Company must maintain at least a significant share of the responsibility for its own past and future decisions”⁶⁴ and the Company’s proposal, in essence, absolves the Company of such responsibility because it provides 100% reimbursement. Third, Company witnesses Dr. Karl McDermott’s and Mr. Gregory Duvall’s statements do not support implementing the Company’s proposal.⁶⁵ The Company’s complaints regarding its failure to

⁶⁰ Surrebuttal Testimony, Phase II, Charles Peterson, lines 450-452.

⁶¹ Transcript, Phase II, Volume II, Testimony of Dan Gimble, page 459.

⁶² Transcript, Phase II, Volume II, Testimony of Kevin Higgins, page 510, lines 6-8.

⁶³ Transcript, Phase II, Volume II, Testimony of Charles Peterson, page 328, lines 4-6.

⁶⁴ Surrebuttal Testimony, Phase I, Charles Peterson, lines 87-88.

⁶⁵ See Transcript, Phase II, Volume I, Testimony of Greg Duvall, page 23 terming the Company’s proposal “restoring the regulatory bargain” despite the fact that the Company has voluntarily entered into settlements for most of its recent rate cases in Utah. See generally, pages 21-25. Mr. Duvall did acknowledge that the Division’s proposal would allow the Company the opportunity to recover “some but not all” of greater NPCs between rate cases in contrast to the current situation where the Company does not have the chance to recover those greater NPCs between rate cases. See page 43. Note that the Division “do[es] not understand regulation to be an automatic pass through of all costs.” Transcript, Phase II, Volume II, Testimony of Charles Peterson, page 315, lines 3-5. Also, as Mr. Peterson noted, if the final accepted NPC amount is “grossly in error the Company should litigate and not settle. And the Company has stipulated a number of times in the last few years. So to the extent that there were differences

recover all net power costs ignore the fact that the Company has only had two cases in the last eight years in which revenue requirement was fully litigated and has settled the other cases.⁶⁶ Thus, “at least a significant share of responsibility” for under recovery in the past, and in the future, must lie with the Company.⁶⁷ The Company’s arguments comparing ECAMs with sharing mechanisms in other states is unpersuasive. The Commission’s decision should not be based upon what has been approved in other states, but instead upon what is in the public interest for the citizens of Utah.⁶⁸ No party, save the Company, endorses the Company’s ECAM proposal.⁶⁹ Finally, the Company’s ECAM proposal relies upon a prudence review, a process that some parties say is insufficient.⁷⁰ UAE’s witness Mr. Higgins compared and contrasted prudence reviews with sharing mechanism, saying:

A finding of imprudence essentially requires a determination that the Company acted unreasonably in its power cost management. In contrast, a risk sharing mechanism, structured such that each and every power cost action undertaken by the Company affects its bottom line, provides an incentive for the Company to get the best possible result from every action taken. In the real world, trying to get the best possible result is different from not behaving unreasonably and getting caught. Getting the best possible result is a more exacting and efficient aspiration.⁷¹

c. The Division’s ECAM Proposal Allows Recovery of Prudently Incurred Costs

The Division’s ECAM proposal provides a mechanism to allow recovery of prudently incurred costs because it combines an “all in approach” with dead bands and sharing bands.⁷² Also, the

in net power costs in those settlements, the Company tacitly agreed with those differences.” Transcript, Phase II, Volume II, Testimony of Charles Peterson, page 320, lines 18-23

⁶⁶ Surrebuttal Testimony, Phase I, Charles Peterson, lines 82-85.

⁶⁷ Surrebuttal Testimony, Phase I, Charles Peterson, line 88.

⁶⁸ Transcript, Phase II, Volume II, Testimony of Charles Peterson, page 361, lines 4-13.

⁶⁹ See Transcript, Phase II, Volume II, Testimony of Dan Gimble, page 457, lines 3-4.

⁷⁰ See, e.g., Transcript, Phase II, Volume I, Testimony of Dr. Karl McDermott, page 267, lines 9-18. See also discussion supra regarding the ineffectiveness of a prudence review as a control.

⁷¹ Transcript, Phase II, Volume II, Testimony of Kevin Higgins, page 507, lines 5-17.

⁷² Transcript, Phase II, Volume II, Testimony of Charles Peterson, page 303, lines 13-23.

Division's proposal allows recovery of prudently incurred costs because it addresses concerns about the Company's hedging practices and market purchases.⁷³

As discussed above, determining which types of NPCs should be included and which should be excluded from an ECAM presents problems. For example, including some NPCs and not others, may incent the Company to focus attention on those costs that are included in the ECAM. The Division's approach to allow the Company to recover all otherwise unrecoverable NPCs avoids the incentive that would exist if only particular costs were included in the ECAM--to focus on those particular included items "to the detriment of the more predictable and controllable items that would not be subject to the ECAM."⁷⁴ Allowing only certain NPC items in an ECAM, as advocated by the Office, would incent the Company to focus on those specific NPC items because of the prospective guarantee of recovery. The Company would have the incentive to reduce the costs that were not included in the ECAM, even though the activities associated with those costs may be more cost effective than the activities associated with the costs included in the ECAM. For example, if natural gas costs were included in the ECAM, but coal costs were not, the Company would have an incentive to move away from presumably cheaper coal resources to natural gas resources just because of the ECAM. This may not meet the prudently incurred cost standard because of potential skewing of Company practices from what they otherwise would be and, therefore, would not be in the public interest.

The Division's proposal also addresses concerns regarding hedging and market purchases. The Office raised, and the Commission directed the Parties to address, these issues. The Office asserted that "the Company's hedging practices and level of reliance on market purchases, need to be considered and acted upon in processes outside of the design phase in

⁷³ The Company acknowledged that, to its knowledge, there is not an explicit Commission order approving the Company's hedging program. Transcript, Phase II, Volume II, Testimony of Stefan Bird, page 225, lines 13-16.

⁷⁴ Transcript, Phase II, Volume II, Testimony of Charles Peterson, page 303, lines 10-12.

order for the outcome to be in the public interest.”⁷⁵ The Division’s mechanism recognizes the importance of these issues while simultaneously recognizing that an ECAM may be necessary for the Company.

The Division’s proposal addresses hedging. Although the Division “considered excluding [hedging costs] until there was a Commission approved hedging plan both in place and implemented . . . the Division has determined that excluding hedging would create a perverse incentive for the Company to stop hedging entirely (since physical costs gas costs would be passed on to ratepayers).”⁷⁶ Excluding hedging would, “in effect, mean that the volatility of gas and electricity markets would be fully flowed through to ratepayers.”⁷⁷ The Division urges that “the Commission (presumably in the existing hedging docket) provide hedging guidance and a hedging plan that will be approved by the Commission and followed by the Company.”⁷⁸ However, in recognition of the time involved in such an undertaking, “until such a plan is approved and implemented, the Division proposes a smaller cost-sharing percentage be used in the ECAM.”⁷⁹

The Division is concerned about FOTs because of “the Company’s continued reliance on front office transactions to cover much of [its] capacity deficiency.”⁸⁰ Thus, the Division’s proposal addresses FOTs, but does not ask the Company to alter its FOT practice immediately. “The Division proposes to make the target ratios of FOTs to system peak load of 7.0 percent in 2015 and 5.5 percent in 2020.”⁸¹ These were the target ratios from the Company’s 2008 IRP

⁷⁵ Direct Testimony, Phase II, Dan Gimble, lines 31-34.

⁷⁶ Direct Testimony, Phase II, Charles Peterson, lines 232-236.

⁷⁷ Direct Testimony, Phase II, Charles Peterson, lines 236-237.

⁷⁸ Direct Testimony, Phase II, Charles Peterson, lines 246-248.

⁷⁹ Direct Testimony, Phase II, Charles Peterson, lines 249-250.

⁸⁰ Direct Testimony, Phase II, Charles Peterson, lines 302-304.

⁸¹ Direct Testimony, Phase II, Charles Peterson, lines 312-313.

Update. If the IRP ratios change as the circumstances change, then the sharing ratios could change accordingly.

The Division's proposal suggests that, if warranted after proper study, the Commission approve a hedging plan for the Company. After the Commission approved hedging plan is successfully implemented and the Company also has reached established FOT goals, the Division proposes that the Company may seek an increase in the sharing percentage. If qualifying conditions are met by the Company, in 2015 the Division proposes the Company may request an increase in the sharing band from 70 to 80 percent, and in 2020 from 80 to 90 percent.⁸²

The Division believes its "plan to escalate cost sharing contingent upon the achievement of three reasonable goals should be seen as a middle ground approach for the short term that becomes more similar to the Company's proposal as time moves forward and hedging and FOT issues are resolved."⁸³ Allowing the Company to have an ECAM now, without waiting for the complete resolution of hedging and FOTs, "offers the Company a substantial degree of relief from price volatility compared to the status quo and offers it an increasingly favorable ECAM approach if it meets these goals."⁸⁴ The Office, whose primary position is that hedging and FOTs as threshold issues that must be studied before an ECAM can be approved,⁸⁵ did not have an estimate of how much time such a study would take,⁸⁶ and it seems that waiting to explore those issues fully prior to deciding whether or not an ECAM should be adopted appears untimely.

⁸² See Direct Testimony, Phase II, Charles Peterson, lines 245-253 and 307-323.

⁸³ Direct Testimony, Phase II, Charles Peterson, lines 367-369.

⁸⁴ Direct Testimony, Phase II, Charles Peterson, lines 371-373.

⁸⁵ See Transcript, Phase II, Volume II, Testimony of Dan Gimble, page 499, lines 8-25 and page 500, lines 1-9.

⁸⁶ Transcript, Phase II, Volume II, Testimony of Dan Gimble, page 466, lines 14-16.

Setting appropriate targets and allowing the Company to request increases in the sharing percentage after meeting those goals promotes and allows recovery of prudently incurred costs. By allowing the Company flexibility in its energy procurement programs, the Division's proposal encourages proper incentives, which encourage prudent behavior, which encourages prudently incurred costs.

V. COMMISSION QUESTIONS

During the hearing, the Commission identified certain legal issues that it would like addressed in this brief. Commissioner Campbell asked whether the word "component" in Utah Code Ann. § 54-7-13.5(1)(b) could permit the 70/30 sharing proposed by some of the parties.⁸⁷ He also asked the parties to brief whether "if the Questar balancing account were created under our general powers for the gas company, couldn't we do the same thing for the electric company, and then not be bound by any strict reading of statute here?"⁸⁸

To address the first question regarding balancing account "components" requires examining the statute itself. Utah Code Ann. § 54-7-13.5(1)(b) defines an "energy balancing account" as:

an electrical corporation account for one or all components of the electrical corporation's incurred actual power costs, including:

(i)(A) fuel;

(B) purchased power; and

(C) wheeling expenses; and

(ii) the sum of the power costs described in Subsection (1)(b)(i) less wholesale remedies. (emphasis added)

The word "components" could be construed as permitting sharing between an electrical corporation and its ratepayers because the balancing account itself would contain fuel, purchased

⁸⁷ See Transcript, Phase II, Volume II, Comment of Commissioner Campbell, page 537, lines 6-24.

⁸⁸ Transcript, Phase II, Volume II, Comment of Commissioner Campbell, page 538, lines 11-15.

power, and wheeling expenses, less wholesale remedies, and the act of sharing does not alter what costs and revenues go into the balancing account. Moreover, as discussed above, a balancing accounting incorporating a sharing band is in the public interest because it encourages prudent behavior by the company, and a balancing account must be found to be in the public interest as a condition of approval. Admittedly, however, the statute does not address the sharing issue explicitly. Subsections (2)(g) and (h) and (4), which more specifically address disposition of the balancing account, should not be read as precluding sharing because such a reading could be seen as unduly restrictive on the public interest that can be, and must be, conferred by a balancing account. In particular, subsections (2)(g) and (h) seem to provide direction as to how balances are to be distributed, or collected rather than precluding sharing. Also, subsection (4), which does talk about all revenues, seems to be addressing segregating balancing account funds from a company's general funds, preventing the company from moving the balancing account funds into another account as well as addressing, and prohibiting, the Commission from, through imputation, adding, or subtracting, the money in the revenue account from the company's general revenues. However, if one were to take a narrow interpretation – that 100% recovery is required by the statute, then the Division believes that an ECAM would fail the “public interest” requirement.

As to the second question about the precedential effect of the existing Questar Gas balancing account, not only must the new balancing account statute be examined but also past case law. The Utah Supreme Court presumed the validity of the Commission's power to establish Questar Gas' balancing account, and did not engage in an analysis of whether or not the Commission's general power did indeed allow the Commission to establish Questar Gas'

balancing account.⁸⁹ Moreover, because there is now a specific Utah statute addressing balancing accounts, under the rules of statutory construction, the balancing account statute shall be given precedence over the general powers statute.⁹⁰ Thus, it seems that the existence of Questar Gas' balancing account does not provide support for the Commission to establish a balancing account for the Company through the Commission's general powers rather than the energy balancing account statute.

VI. CONCLUSION

The Division urges the Commission to adopt the ECAM mechanism proposed by the Division. The Division's proposal complies with the applicable energy balancing account statute because incenting the Company to make proper decisions, and tying recovery of NPCs thereto, is in the public interest. Additionally, the Division's proposal is in the public interest because it has safeguards to limit recovery to prudently incurred costs. Finally, the Division's proposal recognizes the importance and impact of the Company's hedging and FOTs, and provides a means to encourage the Company to meet targets by providing the opportunity for increased sharing bands as the Company achieves certain targets.

Respectfully submitted this _____ day of December 2010.

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⁸⁹ See Questar Gas Company v. Public Service Commission, 34 P.3d 218, 222-223 (Utah 2001).

⁹⁰ See Dairyland Insurance Company v. State Farm Mutual Auto Insurance Company, 882 P.2d 1143, 1146 (Utah 1994).

CERTIFICATE OF SERVICE

I hereby certify that on this 16th day of December, 2010, I caused to be e-mailed, a true and correct copy of the **POST HEARING BRIEF OF THE DIVISION OF PUBLIC UTILITIES** of Docket No. 09-035-15 to:

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