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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 Response of the Division of Public Utilities to Rocky Mountain Power's Request for Clarification and Reconsideration or Rehearing
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Pursuant to Utah Code Ann. § 54-7-15 and Utah Administrative Code R746-100-11.F, the Utah Division of Public Utilities (Division) responds to certain issues raised by Rocky Mountain Power's Request for Clarification and Reconsideration or Rehearing (Request) concerning the Utah Public Service Commission's (Commission) Corrected Report and Order dated March 3, 2011, as amended on March 16, 2011 (Order). As explained in more detail and for the reasons set forth below, the Division (1) supports the request for reconsideration of the Commission's decision to exclude swaps from base and net power costs included in the Energy Balancing Account and urges the Commission to include swaps in those net power costs; (2) opposes the request for reconsideration of the Commission's decision to implement a 70% - 30% sharing of the difference between customers and shareholders of the difference between those forecasted and actual net power costs which are included in the Energy Balancing Account

(Sharing Feature) because no change is needed; and (3) supports the request for clarification that the term of the Energy Balancing Account pilot program runs from the first day of the month following the Commission's decision in Docket No. 10-035-124 through December 31, 2015 and provide guidance as to in which years the Division must file its report.

I. Swaps Should Be Included in Base and Net Power Costs Pertaining to the Energy Balancing Account

The Energy Balancing Account should include all net power costs, including swaps. Including swaps will facilitate the determination, and examination and auditing of, net power costs. Moreover, excluding swaps could result in perverse incentives for the Company concerning its decisions to pursue swaps or lead to unintended consequences with the EBA balances and amortizations. Finally, including swaps is consistent both with Utah Code Ann. § 56-7-13.5 and the Commission's treatment of gas costs for Questar Gas Company (Questar Gas).

An Energy Balancing Account incorporating all components of net power costs, including swaps, with sharing bands is appropriate.¹ Excluding swaps unnecessarily complicates defining net power costs. As the Division argued earlier in this docket, the Company's hedging program seems not to be precisely defined² and it is sometimes difficult to determine what constitutes hedging activities.³ While the Company is now identifying swaps as two separate line items in its filings of net power costs in rate cases, what the Company considers to be included in its total hedging program has been difficult for the Division to identify in the filings the Company usually provides. The Company has made it clear, however, that swaps are part of

¹ The Division characterized this approach, along with the inclusion of dead bands, as an "all in approach." See Transcript, Phase II, Volume II, Testimony of Charles Peterson, p. 303, lines 10-12.

² The Company's hedging program is very broad and difficult to monitor. See, generally, the Division's Post-Hearing Brief at pp. 16-19, filed December 16, 2010 in this docket.

³ See, e.g. Direct Testimony of Charles Peterson, Phase II – Part 1, August 4, 2010, lines 165-168.

its larger hedging program.⁴ Auditing the Energy Balancing Account largely will fall to the Division, and steps that will streamline the auditing process will allow the Division to do more with its limited resources, resulting in better analyses.

Including some net power costs and not others such as swaps may incent the Company to focus attention on those costs that are included in the Energy Balancing Account, possibly causing perverse incentives. Excluding swaps could lead the Company to abandon, or lessen, its interest in swaps as a method to control net power costs. Such action could expose customers, and the Company, to higher net power costs than otherwise would be incurred. Possibly, excluding swaps from the Energy Balancing Account could result in the Company incurring other than prudent net power costs.⁵ Excluding swaps may also lead to unintended consequences. The Division, for example, is concerned that excluding swaps from the EBA may lead to a situation where the Company's actual net power costs may decline or remain relatively flat, while the ratepayer liabilities through account accruals may increase, or vice versa.

Additionally, including swaps in the Energy Balancing Account is consistent with the Energy Balancing Statute, Utah Code Ann. § 54-7-13.5(1)(b), and the Commission's treatment of Questar Gas' gas costs. The statute calls for the inclusion of "some 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 net power costs described in Subsection (1)(b)(i) less wholesale revenues." Note that the statute does not restrict eligible expenses to only the listed items, as evidenced by the statute's use of the word "including" and the lack of the use of words such as "exclusively," and "limited to." Moreover, a plain reading of the statute accommodates the view that swaps are fuel because they are a financial mechanism used to

⁴ In this docket, the Division suggested that the Commission address the Company's hedging program, and believes that such attention would be helpful still. See, e.g., the Surrebuttal Testimony of Douglas D. Wheelwright.

⁵ See Direct Testimony of Charles Peterson, Phase II – Part 1, August 4, 2010, lines 207-240.

purchase, on a forward basis, fuel. Although there are different facts applicable to Questar Gas, it is appropriate to note that the Commission has allowed all of Questar Gas' gas costs, including swaps, to be included in its pass through account and to treat the Company's swaps the same.⁶

Substantial evidence in the record supports including swaps in net power costs. Division witness Mr. Charles Peterson, and Company witnesses Mr. Steven McDermott and Mr. Stefan Bird testified concerning the appropriate inclusion of swaps. The argument against including swaps, raised only by Utah Industrial Energy Consumers (UIEC), is unpersuasive when compared to the testimony and arguments discussed above, because UIEC's argument is overly restrictive, and inappropriately interprets § 54-7-13.5 as excluding swaps.

II. Establishing a 70% - 30% Sharing Feature is Appropriate, and its Elimination is Unwarranted

The Company's claims that the Sharing Feature is inappropriate are without merit. The Commission's decision to incorporate the Sharing Feature in the Energy Balancing Account mechanism is appropriate, and is supported by substantial evidence in the record. The Division believes that an interpretation that § 54-7-13.5 prohibits sharing renders an ECAM not in the public interest.

The Company ineffectively claims that the Sharing Feature "is a different and separate objective from what the Commission found to be the 'primary objective. . . [of the Energy Balancing Account];' that primary objective being to ensure sufficient incentive to make prudent resource decisions" ⁷ For the reasons stated below, the Sharing Feature, particularly when compared to the Company's current lack of a recovery mechanism for unforecasted net power costs, facilitates the Commission's "primary goal" of providing incentives for the Company to make prudent resource decisions.

⁶ See Division's Post-Hearing Brief, at pp. 19-21.

⁷ Request at p. 20, quoting the Order at p. 67.

The Company inaccurately argues that the Sharing Mechanism contradicts Utah Code Ann. § 54-7-13.5. Applying the well accepted rules of statutory construction such as looking to the plain language of the statute, giving effect to each word, and construing the provisions as a whole, gives rise to the conclusion that the Sharing Mechanism is allowed. Note that the statute addresses “some or all components of the electrical corporation’s incurred actual power cost” and “all allowed costs and revenues associated with an energy balancing account.” One must not overlook the use of “some or all” and “all allowed” when evaluating the appropriateness of the Sharing Mechanism under this statute; “some or all” means all or less than everything, and “all allowed” means that costs must be included by permission of the Commission under the proper interpretation and application of the statute. As stated in the Division’s Post Hearing Brief:⁸

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 power, and wheeling expenses, less wholesale remedies [revenues], 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.⁹

⁸ Division’s Post-Hearing Brief, at pp.19-20.

⁹ See the Division’s Post-Hearing Brief at pp. 19-20.

Critically, if one were to take the narrow interpretation advocated by the Company – that 100% recovery is required by the statute – “the Division believes an ECAM would fail the ‘public interest’ requirement.”¹⁰ The Division believes that “there may be a case for providing some sort of ECAM but not at the expense of removing incentives for the Company to prudently manage its business, or at the expense of removing business risks for which the Company is being compensated.”¹¹

By incorporating the Sharing Feature, the Commission creates a mechanism to share risk between customers and the Company – properly providing an incentive for the Company to make prudent resource decisions. “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 patience¹² that they now have to operate as efficiently as possible, because they still are putting substantial shareholder funds at risk.”¹³ Moreover, the sharing band “leaves [the Company] the incentives to try to improve their control over time of ECAM costs.”¹⁴

The Sharing Features also provides an incentive for the Company to improve the accuracy of its forecasts, which will improve the Company’s ability to make prudent resource decisions. 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.

Importantly, the Sharing Feature provides the Company with a mechanism to recover unanticipated net power costs – an opportunity that the Company otherwise does not have. 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

¹⁰ Id. at p. 20.

¹¹ Surrebuttal Testimony, Phase II – Part 2, of Charles Peterson at lines 64-67.

¹² Most likely the word “patience” is a transcription error and the word actually should be “practice.”

¹³ Transcript, Phase II, Volume II, Testimony of Charles Peterson, p. 376, lines 8-14.

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

opportunity to recover some, but not all, excess power costs in contrast to the zero percent recovery opportunity that the Company has now.¹⁵ When asked if “you’d just be happy about the fact that you’re going to pay a buck and only get 70 cents,” the Division perceptively noted, “Right now you [the Company] don’t even get the 70 cents.”¹⁶

Substantial evidence in the record supports implementation of the Sharing Feature. Four parties support the Sharing Feature.

Four parties in this case support a 70-30 sharing mechanism, in some instances as a secondary position to their first position that an Energy Cost Adjustment Mechanism (ECAM)¹⁷ should not be adopted now: the Division, the Office of Consumer Services (Office), the Utah Association of Energy Users (UAE), and, together, Western Resource Advocates and, Utah Clean Energy.¹⁸

Specifically:

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.”¹⁹ Additionally, if an ECAM is adopted, 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”²⁰ and “bears some general correspondence to the sharing provisions the Company agreed to in Wyoming in 2006.”²¹ 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.²²

¹⁵ Transcript, Phase II, Volume I, Testimony of Greg Duvall, p. 41, lines 1-6.

¹⁶ Transcript, Phase II, Volume II, Testimony of Charles Peterson, p. 343, lines 17-21.

¹⁷ For all practical purposes, the terms ECAM and Energy Balancing Account can be used interchangeably here.

¹⁸ See Division’s Post-Hearing Brief at pp. 8-9.

¹⁹ Transcript, Phase II, Volume II, Testimony of Daniel Gimble, p. 467, lines 20-25 and page 468, line 1.

²⁰ Transcript, Phase II, Volume II, Testimony of Kevin Higgins, p. 506, lines 10-17.

²¹ Transcript, Phase II, Volume II, Testimony of Kevin Higgins, p. 506, lines 18-20.

²² Surrebuttal Testimony, Phase II, Nancy Kelly, lines 54-97.

Ms. Kelly concludes that a sharing band is a greater incentive to manage costs than a prudence review²³ as does Mr. Higgins.²⁴

When measured against this evidence supporting the Sharing Feature, the Company's evidence proves inadequate, and the Sharing Feature should remain unchanged.

III. The Term of the Pilot Needs Clarification

The Commission's order arguably leaves open the term of the pilot program because there are no explicit instructions concerning the effect of the "stub period," consisting of the months between implementation of the Energy Balancing Account and the end of the first year, on the pilot's four year term. The Division requests that the Commission define the term of the pilot program as beginning on the first day of the month following the Commission's decision in Docket No. 10-035-124 and ending on December 31, 2015. This term will provide certainty to the parties and allow the Division to file its required reports within four months of specified years, while allowing collection of four years, and three months, of data to be used in evaluating the effect of the pilot program. The Commission's order is also unclear as to in which years the Division is to file its reports. Further clarification on this matter would be helpful.

IV. Conclusion

The Division respectfully requests that the Commission reconsider its decision to exclude swaps from base and net power costs included in the Energy Balancing Account, and instead include swaps; (2) deny the Company's request for reconsideration of the Commission's decision to implement a 70% - 30% sharing of the difference between customers and shareholders of the difference between those forecasted and actual net power costs included in the Energy Balancing Account (Sharing Feature); and (3) clarify that the term of the Energy Balancing Account pilot

²³ Surrebuttal Testimony, Phase II, Nancy Kelly, lines 114-117.

²⁴ Transcript, Volume II, Phase II, Testimony of Kevin Higgins, p. 506, lines 21-25 and p. 507, lines 1-4.

program runs from the first day of the month following the Commission's decision in Docket No. 10-035-124 through December 31, 2015 and when the Division must file its report.

Respectfully submitted this _____ day of May, 2011.

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CERTIFICATE OF SERVICE

I hereby certify that I caused a true and correct copy of the foregoing Response of the Division of Public Utilities to Rocky Mountain Power's Request for Clarification and Reconsideration or Rehearing to be served upon the following by electronic mail to the addresses shown below on May 2, 2011:

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