

BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

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In the Matter of the Application of	)	
Rocky Mountain Power, for	)	Docket No. 10-035-124
Authority to Increase Its Retail Electric	)	
Utility Service Rates in Utah and For	)	Direct Testimony
Approval of Its Proposed Electric Service	)	of Seth Schwartz
Schedule and Electric Service	)	On behalf of the
Regulations	)	Office of Consumer Services
	)	

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May 26, 2011

REDACTED

1           **INTRODUCTION**

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

3   A.    My name is Seth Schwartz. I am the President of Energy Ventures  
4        Analysis, Inc. (“EVA”), which is located at 1901 North Moore Street,  
5        Arlington, VA 22209.

6

7   **Q.    PLEASE SUMMARIZE YOUR BACKGROUND AND QUALIFICATIONS.**

8   A.    I have been a partner at EVA since it was founded in 1981. In the last 30  
9        years, my consulting work has included:

10           1) Assisting coal-fired electric power companies (regulated and  
11            unregulated) in their coal procurement activities, such as coal  
12            contract strategies, coal purchasing, coal contract administration,  
13            and coal inventory planning;

14           2) Performing management audits of coal procurement activities of  
15            electric power companies for management, regulatory  
16            commissions and interveners. As a result of these projects, I have  
17            testified before a number of state and federal regulatory  
18            commissions;

19           3) Testifying in coal contract disputes, including litigation and  
20            arbitration;

21           4) Preparing market studies on behalf of coal producers and investors;  
22            and,

23           5) Assisting investors in the coal industry in evaluating the economics  
24           of coal mining operations.

25           In the course of this work, I was part of EVA's team which prepared a  
26           review of PacifiCorp's coal procurement policies and management  
27           practices for the PacifiCorp Inter-jurisdictional Task Force on Allocations  
28           (PITA) in 1991 and 1995.

29

30   **Q.   PLEASE DESCRIBE THE SCOPE OF YOUR WORK IN THIS CASE.**

31   A.   Energy Ventures Analysis, Inc. ("EVA") was retained by The Utah Office of  
32       Consumer Services ("OCS") to perform an independent review of the  
33       Company's coal supply plans and performance, including:

34           1) Benchmarking the Company's cost of coal for its power plants with  
35           other power plants in similar circumstances.

36           2) Review of the Company's coal supply strategy for each of its plants  
37           and the projected cost of coal in the Test Year.

38           3) Review of the Company's fuel supply organization, policies and  
39           procedures, and compliance with its policies.

40           4) Review of the Company's affiliate coal supply operations.

41           5) Review of the Company's long- and short-term coal inventory  
42           policies and projected cost of coal included in the Test Year.

43

44

45

46 **RECOMMENDATIONS**

47 **Q. BASED ON EVA'S REVIEW OF THE COMPANY'S COAL SUPPLY**  
48 **PLANS AND PERFORMANCE, PLEASE SUMMARIZE YOUR**  
49 **RECOMMENDATIONS.**

50 **A.** My recommendations include:

51 1) The Company's coal inventory targets for the Utah Plants, which  
52 were adopted September 30, 2010, should [REDACTED]. In my  
53 opinion, these targets are excessively high and are not supported  
54 by the independent study commissioned by the Company.

55 2) The Company's [REDACTED]<sup>1</sup>  
56 [REDACTED] the new targets adopted by the Company.

57 [REDACTED]  
58 [REDACTED]<sup>2</sup> [REDACTED]  
59 [REDACTED]  
60 [REDACTED] I  
61 recommend that the [REDACTED] for the [REDACTED]  
62 should be [REDACTED] of maximum burn, with a range of [REDACTED] days  
63 of maximum burn [REDACTED] of average burn).<sup>3</sup> This range is  
64 [REDACTED]

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<sup>1</sup> [REDACTED]

<sup>2</sup> According to data provided by the Company, the [REDACTED]  
[REDACTED] burn an average of [REDACTED] and a maximum of [REDACTED]

<sup>3</sup> Inventory of [REDACTED]  
[REDACTED]

65 [REDACTED]

66 [REDACTED]

67 3) The Company provided [REDACTED]

68 [REDACTED]

69 [REDACTED] EVA prepared an analysis [REDACTED]

70 [REDACTED]

71 [REDACTED]

72 [REDACTED] Based on our analysis, I recommend a [REDACTED]

73 [REDACTED]

74 [REDACTED] would be sufficient

75 [REDACTED]

76 [REDACTED] The

77 Company's [REDACTED]

78 [REDACTED] what I recommend as a

79 [REDACTED]

80 4) While the Company may have [REDACTED]

81 [REDACTED]

82 [REDACTED]

83 [REDACTED]<sup>4</sup> The Company has not prepared a plan [REDACTED]

84 [REDACTED]

85 [REDACTED] I

---

<sup>4</sup> [REDACTED]

86 recommend that the Company develop a plan [REDACTED]

87 [REDACTED]

88 5) Because of its new [REDACTED]

89 [REDACTED]

90 [REDACTED]

91 [REDACTED]

92 [REDACTED]

93 [REDACTED]

94 [REDACTED]

95 [REDACTED]

96 [REDACTED]

97 [REDACTED]

98 [REDACTED]

99 [REDACTED] I recommend that the

100 Company [REDACTED]

101 [REDACTED]

102 6) The Company has requested [REDACTED] in its total inventory value

103 for the Test Year of [REDACTED] The

104 Test Year value is determined by the average of the projected

105 values for June 30, 2011 and June 30, 2012. Most of this increase

106 is due to the projected [REDACTED] of [REDACTED]

107 Based on my analysis, I recommend that the inventory included for

108 the Test Year should include [REDACTED] for the [REDACTED]

109 [REDACTED] which would [REDACTED] the total coal inventory in the rate base  
 110 for the Test Year [REDACTED]  
 111 [REDACTED] This change would [REDACTED]  
 112 [REDACTED] from the amount of [REDACTED] requested by the  
 113 Company to [REDACTED]

114 7) The Company's internal audit department [REDACTED]  
 115 [REDACTED] Because of the large dollar expense  
 116 in coal procurement, this is an area of importance. The internal  
 117 audit department [REDACTED]  
 118 [REDACTED]. I recommend that the internal audit department  
 119 [REDACTED]  
 120 [REDACTED]  
 121 [REDACTED]

122

123 **COAL INVENTORY**

124 **Q. WHAT IS THE BACKGROUND FOR THE COMPANY'S**  
 125 **DEVELOPMENT OF NEW COAL INVENTORY TARGETS?**

126 A. In the course of the general rate case proceedings in Docket No. 09-035-  
 127 23, and as a result of the Electric Lake Settlement in February of 2008, the  
 128 Division raised the issue of the appropriate coal inventory levels that the  
 129 Company should maintain at its Utah plants.<sup>5</sup> The Division noted that a  
 130 review of the Company's coal procurement policies and practices [REDACTED]

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<sup>5</sup> Docket No. 09-035-23, Direct Testimony of Michael J. McGarry, Sr., DPU Exhibit 3, October 8, 2009.

131 [REDACTED]<sup>6</sup> As a result, the Commission  
 132 determined that the Company should have a regularly reviewed and  
 133 updated Company Coal Policy in place. In its Report and Order the  
 134 Commission stated the following:<sup>7</sup>

135 We direct the Division, beginning in 2011, to conduct  
 136 an annual audit of the Company's fuel inventory  
 137 management policies, procedures, and actual  
 138 practices and provide a summary of its audit and  
 139 associated findings to the Commission by no later  
 140 than March 31 of each year for the previous year's  
 141 activity.  
 142

143 The Company retained the consulting firm of Pincock, Allen and Holt  
 144 ("PAH") to assist the Company in determining appropriate inventory levels.  
 145 The Company adopted new policies and procedures for coal inventory  
 146 effective September 30, 2010.<sup>8</sup>

147

148 **Q. HOW DID PAH ASSIST THE COMPANY IN DETERMINING**  
 149 **APPROPRIATE INVENTORY LEVELS?**

150 A. PAH prepared a study on coal inventory policies for the Company's coal-  
 151 fired power plants [REDACTED]

152 [REDACTED] The PAH scope of work included:

153 [REDACTED]

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<sup>6</sup> [REDACTED]

<sup>7</sup> Docket No. 09-035-23, Report and Order on Revenue Requirement, Cost of Service and Spread of Rates, February 18, 2010, p. 106.

<sup>8</sup> [REDACTED]



154 [REDACTED]  
155 [REDACTED]  
156 [REDACTED]  
157 [REDACTED]  
158 [REDACTED]  
159 [REDACTED]<sup>9</sup>

160

161 **Q. WHAT WAS PAH'S APPROACH TO DETERMINING THE**  
162 **APPROPRIATE COAL INVENTORY LEVELS FOR THESE PLANTS?**

163 A. PAH developed [REDACTED] taking into account [REDACTED]  
164 [REDACTED] Based upon historical  
165 data regarding the variability [REDACTED] PAH determined [REDACTED]  
166 [REDACTED] In addition, PAH  
167 accounted for [REDACTED]  
168 [REDACTED] Using the  
169 combination of [REDACTED]  
170 [REDACTED] PAH [REDACTED]  
171 [REDACTED]

172

173 **Q. WHAT WERE THE INVENTORY LEVELS RECOMMENDED BY PAH?**

174 A. PAH made its recommendations using the number of days of maximum  
175 burn. PAH's recommended inventory targets were:

\_\_\_\_\_

<sup>9</sup> Pincock, Allen & Holt, "Coal Inventory Policies for Coal-Fired Power Plants in Utah", August 13, 2009

176

[REDACTED]

177

[REDACTED]

178

[REDACTED]

179

[REDACTED]

180

181 **Q. DID THE COMPANY ADOPT INVENTORY TARGETS CONSISTENT**  
182 **WITH THE RECOMMNDATIONS BY PAH?**

183 A. For the [REDACTED]

184 [REDACTED] For the [REDACTED]

185 [REDACTED]

186

187 **Q. GIVEN THE [REDACTED]**

188 [REDACTED] **DID THE COMPANY PERFORM ANY**

189 [REDACTED]

190 [REDACTED]

191 A. [REDACTED]

192

193 **Q. WHAT INVENTORY TARGETS DID THE COMPANY ADOPT FOR THE**

194 [REDACTED] **?**

195 A. For the [REDACTED] the Company

196 adopted [REDACTED], which

197 is equivalent to [REDACTED]

198 [REDACTED] This range is consistent [REDACTED]

199 [REDACTED]

200 [REDACTED] I believe that the new inventory targets are [REDACTED]

201 [REDACTED]

202 [REDACTED]

203

204 **Q. WHAT INVENTORY TARGETS DID THE COMPANY ADOPT FOR THE**

205 [REDACTED]?

206 A. The Company adopted a target range of [REDACTED] of average burn

207 for the [REDACTED] or [REDACTED] million tons. This is

208 equivalent to [REDACTED] of maximum burn, compared to the PAH

209 recommendation of [REDACTED] of maximum burn.

210

211 **Q. WHAT PLANTS DID THE COMPANY INCLUDE [REDACTED]**

212 [REDACTED]?

213 A. The Company included the [REDACTED] Plants

214 [REDACTED] of [REDACTED], as well as the [REDACTED] at

215 the [REDACTED]

216 [REDACTED]

217 [REDACTED]

218

219 **Q. WHY ARE THESE SITES [REDACTED] AS THE [REDACTED]**

220 [REDACTED]

221 A. The coal supplies from the [REDACTED]  
222 can be [REDACTED] Thus the  
223 purchasing and planning for the [REDACTED]  
224 [REDACTED]

225

226 **Q. PAH AND THE COMPANY PROPOSED [REDACTED]**  
227 **[REDACTED] DO YOU AGREE**  
228 **WITH [REDACTED] RECOMMENDED TARGET LEVELS?**

229 A. [REDACTED] While the approach [REDACTED]  
230 [REDACTED] I recommend that the  
231 Company should adopt a target [REDACTED]  
232 [REDACTED] Further, it should be  
233 expected that there will be [REDACTED]  
234 [REDACTED] and the target range should be [REDACTED]  
235 [REDACTED] of maximum burn. The Company's [REDACTED] of  
236 average [REDACTED]

237

238 **Q. WHAT IS THE NORMAL INVENTORY LEVELS FOR MOST ELECTRIC**  
239 **POWER COMPANIES IN THE UNITED STATES?**

240 A. Using the amount of coal inventory at the end of December 2010  
241 (175,160,000 tons) and the actual burn during calendar year 2010  
242 (961,941,918 tons), the average coal burn for electric power generators

243 was 66.5 days of average burn.<sup>10</sup> Looking at the inventory levels by state,  
244 almost all of the states averaged 40 – 90 days of average burn, [REDACTED]  
245 [REDACTED]. Only 7  
246 states had inventories above 90 days of average burn, [REDACTED]  
247 [REDACTED] My recommended  
248 inventory target [REDACTED] of maximum burn is  
249 equivalent to [REDACTED] of average burn, which is [REDACTED]  
250 [REDACTED]

251

252 **Q. DID THE COMPANY ALSO ADOPT A [REDACTED]**

253 [REDACTED]

254 A. Yes, the Company adopted a [REDACTED]  
255 [REDACTED] of average burn [REDACTED]  
256 of maximum burn).

257

258 **Q. DID THE COMPANY PROVIDE A DEFINITION OF A [REDACTED]**

259 [REDACTED]

260 A. No. The Company does not define a [REDACTED] in its  
261 new coal inventory policies and procedures. The new inventory policies  
262 and procedures manual states that:

263 [REDACTED]

264 [REDACTED]

---

<sup>10</sup>Energy Information Administration, December 2010 data for actual inventory and annual 2010 coal burn by state.

265 [REDACTED]

266 [REDACTED]<sup>11</sup>

267 I believe that the [REDACTED] are intended to quantify  
268 the level to which inventories may be [REDACTED]

269

270 **Q. DID PAH RECOMMEND A [REDACTED]**

271 A. [REDACTED] PAH recognized that there may be [REDACTED]

272 [REDACTED]

273 [REDACTED]

274 [REDACTED]

275

276 **Q. DID THE COMPANY ADOPT [REDACTED]**

277 [REDACTED]

278 A. [REDACTED]

279

280 **Q. DID THE COMPANY PROVIDE ANY [REDACTED]**

281 **SUPPORTING ITS [REDACTED]?**

282 A. [REDACTED]

283

284 **Q. WHAT BASIS DID THE COMPANY PROVIDE FOR THE [REDACTED]**

285 [REDACTED]

\_\_\_\_\_

<sup>11</sup> [REDACTED]

286 A. The Company cited the following factors as the reasons [REDACTED]

287 [REDACTED]

288 [REDACTED]

289 [REDACTED]

290 [REDACTED]

291 [REDACTED]

292 [REDACTED]

293 [REDACTED]

294 [REDACTED]

295 [REDACTED]

296 [REDACTED]

297 [REDACTED]

298 [REDACTED]

299 [REDACTED]

300 [REDACTED]

301 [REDACTED]

302 [REDACTED]

303

304 **Q. HOW DO YOU RESPOND TO THESE REASONS WHICH THE**

305 **COMPANY PROVIDED FOR THE [REDACTED]**

306 [REDACTED]

307 A. My responses to these issues are:

308 [Redacted]

309 [Redacted]

310 [Redacted]

311 [Redacted]

312 [Redacted]

313 [Redacted]

314 [Redacted]

315 [Redacted]

316 [Redacted]

317 [Redacted]

318 [Redacted]

319 [Redacted]

320 [Redacted]

321 [Redacted]

322 [Redacted]

323 [Redacted]

324 [Redacted]

325 [Redacted]

326 [Redacted]

327 [Redacted]

328 [Redacted]

329 [Redacted]

330 [Redacted]



331 [REDACTED]

332 [REDACTED]

333 [REDACTED]

334 [REDACTED]

335 [REDACTED]

336 [REDACTED]

337 [REDACTED]

338 [REDACTED]

339 [REDACTED]

340

341 **Q. HOW DID YOU ANALYZE THE APROPRIATE INVENTORY TARGET**

342 **FOR THE [REDACTED]**

343 [REDACTED]

344 **A. EVA took into account the following factors:**

345 [REDACTED]

346 [REDACTED]

347 [REDACTED]

348 [REDACTED]

349 [REDACTED]

350 [REDACTED]

351 [REDACTED]

352

353 **Q. WHAT DID YOU DETERMINE ABOUT EACH OF THESE FACTORS?**

354 A. EVA concluded the following about each of these factors:

355 1) [REDACTED]

356 [REDACTED]

357 2) The Company can [REDACTED] to [REDACTED]

358 [REDACTED] Without any [REDACTED]

359 [REDACTED] the [REDACTED] would [REDACTED]

360 [REDACTED]

361 The projected coal production from [REDACTED] in [REDACTED] is

362 about [REDACTED];

363 3) In my opinion, the Company should have [REDACTED]

364 [REDACTED] under

365 all circumstances for [REDACTED] which is [REDACTED] of

366 coal;

367 4) [REDACTED]

368 [REDACTED]

369 [REDACTED]

370 [REDACTED]

371 [REDACTED]

372 [REDACTED]

373

374 Q. ACCORDING TO YOUR ANALYSIS, HOW MUCH COAL INVENTORY

375 WOULD THE COMPANY REQUIRE?

376 A. [REDACTED]  
377 [REDACTED] the Company would have an inventory [REDACTED]  
378 [REDACTED] In order to end the year with [REDACTED] the  
379 Company would require [REDACTED]  
380 [REDACTED] This is equal to [REDACTED]  
381 [REDACTED]

382

383 **Q. HOW DOES THIS LEVEL OF INVENTORY COMPARE TO THE PAH**  
384 **RECOMMENDED RANGE?**

385 A. [REDACTED] they did [REDACTED]  
386 [REDACTED] of  
387 maximum burn for the [REDACTED]  
388

389 **Q. CAN THE COMPANY** [REDACTED]  
390 [REDACTED]  
391 [REDACTED]

392 A. [REDACTED] has [REDACTED]  
393 [REDACTED] For example,  
394 the [REDACTED]  
395 [REDACTED] Further,  
396 the Company could choose to [REDACTED]  
397 [REDACTED]

398

399 **Q. WHAT LEVEL OF INVENTORY HAS THE COMPANY INCLUDED IN ITS**  
400 **RATE BASE FOR THE TEST YEAR?**

401 A. The Company calculates the rate base for the Test Year using the  
402 average of the projected inventory in dollars for the months ending June  
403 2011 and June 2012. The total projected inventory dollars averaged  
404 [REDACTED] which includes \$ [REDACTED] for the [REDACTED]  
405 [REDACTED]  
406 [REDACTED] The increase in  
407 the amount of inventory requested by the Company for the Test Year is  
408 [REDACTED] over the amount currently included in the rate base. The  
409 inventory dollars for the [REDACTED] is based upon the projected cost of  
410 coal and projected average inventory of [REDACTED]  
411 [REDACTED] This average  
412 equates to [REDACTED] of average burn and [REDACTED] of maximum burn for  
413 the [REDACTED]

414  
415 **Q. DO YOU AGREE THAT THE COMPANY SHOULD EARN A RETURN**  
416 **ON THE AMOUNT OF INVENTORY WHICH IT HAS PROJECTED FOR**  
417 **THE TEST YEAR?**

418 A. [REDACTED]  
419 [REDACTED]  
420 [REDACTED]  
421 [REDACTED]

422

423 **Q. WHAT IS THE AMOUNT OF INVENTORY WHICH YOU RECOMMEND**  
424 **SHOULD BE INCLUDED IN THE RATE BASE FOR THE TEST YEAR?**

425 A. I recommend that the amount of average inventory [REDACTED]  
426 [REDACTED]  
427 [REDACTED]  
428 [REDACTED]  
429 [REDACTED]  
430 [REDACTED]  
431 [REDACTED]  
432 [REDACTED]

433 [REDACTED] In her Direct Testimony, OCS witness Ramas  
434 shows the revenue requirement impact of my recommended coal  
435 inventory adjustment.

436

437 **INTERNAL AUDIT**

438 **Q. WHAT IS THE ROLE OF THE COMPANY’S INTERNAL AUDIT**  
439 **DEPARTMENT WITH REGARD TO THE FUEL PROCUREMENT**  
440 **OPERATIONS?**

441 A. The Company’s policies and procedures manual states that:  
  
442 “It is the responsibility of the Internal Audit Department to conduct a  
443 thorough review of the fuel procurement function. The review shall include  
444 all aspects of the fuel procurement function from solicitations and  
445 evaluations through fuel receipts and payments. The audit shall also

446 determine adherence to and adequacy of the policies and procedures  
447 included in this Fuel/Transportation Procurement manual.”<sup>12</sup>  
448

449 **Q. IN YOUR OPINION, HAS THE INTERNAL AUDIT DEPARTMENT**  
450 **FULFILLED THIS RESPONSIBILITY?**

451 A. No. Based upon our interview of the Director of Internal Audit and our  
452 review of the audits prepared by the Internal Audit department since 2008,  
453 the Internal Audit department [REDACTED]  
454 [REDACTED] The Internal Audit department [REDACTED]  
455 [REDACTED]  
456 [REDACTED] as specified by the policies and  
457 procedures manual.  
458

459 **Q. WHAT FUNCTIONS OF THE FUEL GROUP HAS THE INTERNAL**  
460 **AUDIT DEPARTMENT AUDITED [REDACTED] ?**

461 A. The Internal Audit department has audited compliance with Sarbanes-  
462 Oxley [REDACTED]  
463

464 **Q. WHAT REASON DID THE DIRECTOR OF INTERNAL AUDIT PROVIDE**  
465 **FOR [REDACTED]**

466 [REDACTED]  
467 [REDACTED]

---

<sup>12</sup> PacifiCorp Fuel/Transportation Procurement Policies and Procedures, effective date 9/30/04, page 17.

468 A. The Director of Internal Audit stated that these functions [REDACTED]

469 [REDACTED]

470

471 **Q. DO YOU AGREE WITH THIS ASSESSMENT [REDACTED]?**

472 A. [REDACTED]

473 [REDACTED]

474 [REDACTED]

475

476 **Q. IN YOUR REVIEW OF THE COMPANY'S FUEL PROCUREMENT**

477 **FUNCTION, [REDACTED]**

478 [REDACTED]

479 [REDACTED]

480 A. Based upon our review, the Company's fuel procurement function appears

481 to be [REDACTED]

482 [REDACTED]

483 [REDACTED]

484 [REDACTED]

485 [REDACTED]

486 [REDACTED]

487 [REDACTED]

488 [REDACTED]

489 [REDACTED]

490 [REDACTED]

491 [REDACTED]

492

493 **Q. WHAT IS YOUR RECOMMENDATION?**

494 A. I recommend that the internal audit department should [REDACTED]

495 [REDACTED]

496 [REDACTED]

497 [REDACTED]

498

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

500 A. Yes.