

**BEFORE THE UTAH PUBLIC SERVICE COMMISSION**

Application of Rocky Mountain Power  
To Establish a Balancing Account for  
Pension Settlement Losses

DOCKET NO. 21-035-14

**DIRECT TESTIMONY**

**AND EXHIBITS**

**OF**

**KEVIN C. HIGGINS**

**On Behalf of**

**Utah Association of Energy Users**

**June 22, 2021**

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UAE Exhibit 1.1	Illustrative Utah Pension Settlement Adjustments Balancing Account
UAE Exhibit 1.2	RMP Response to UAE Data Request 2.6

1           **I.       INTRODUCTION AND SUMMARY**

2           **Q.       PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

3           A.       My name is Kevin C. Higgins. My business address is 111 East Broadway, Suite 1200,  
4               Salt Lake City, Utah, 84111.

5           **Q.       BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?**

6           A.       I am a Principal in the firm of Energy Strategies, LLC, a private consulting firm that  
7               specializes in economic and policy analysis applicable to energy production,  
8               transportation, and consumption.

9           **Q.       ON WHOSE BEHALF ARE YOU TESTIFYING IN THIS PROCEEDING?**

10          A.       My testimony is being sponsored by the Utah Association of Energy Users (“UAE”).

11          **Q.       PLEASE SUMMARIZE YOUR QUALIFICATIONS.**

12          A.       My academic background is in economics, and I have completed all coursework and field  
13               examinations toward a Ph.D. in Economics at the University of Utah. In addition, I have  
14               served on the adjunct faculties of both the University of Utah and Westminster College,  
15               where I taught undergraduate and graduate courses in economics. I joined Energy  
16               Strategies in 1995, where I assist private and public sector clients in the areas of energy-  
17               related economic and policy analysis, including evaluation of electric and gas utility rate  
18               matters.

19               Prior to joining Energy Strategies, I held policy positions in state and local  
20               government. From 1983 to 1990, I was economist, then assistant director, for the Utah  
21               Energy Office, where I helped develop and implement state energy policy. From 1991 to  
22               1994, I was chief of staff to the chairman of the Salt Lake County Commission, where I

23 was responsible for development and implementation of a broad spectrum of public  
24 policy at the local government level.

25 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE UTAH PUBLIC**  
26 **SERVICE COMMISSION (“PSC” OR “THE COMMISSION”)?**

27 A. Yes. Since 1984, I have testified in forty-four dockets before the Commission on  
28 electricity and natural gas matters.

29 **Q. HAVE YOU TESTIFIED PREVIOUSLY BEFORE ANY OTHER STATE**  
30 **UTILITY REGULATORY COMMISSIONS?**

31 A. In addition to these Utah proceedings, I have testified in approximately 220 other  
32 proceedings on the subjects of utility rates and regulatory policy before state utility  
33 regulators in Alaska, Arizona, Arkansas, Colorado, Georgia, Idaho, Illinois, Indiana,  
34 Kansas, Kentucky, Michigan, Minnesota, Missouri, Montana, Nevada, New Mexico,  
35 New York, North Carolina, Ohio, Oklahoma, Oregon, North Carolina, Pennsylvania,  
36 South Carolina, Texas, Virginia, Washington, West Virginia, and Wyoming. I have also  
37 filed affidavits in proceedings before the Federal Energy Regulatory Commission and  
38 prepared expert reports in state and federal court proceedings involving utility matters.

39 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

40 A. My testimony addresses the proposal by Rocky Mountain Power (“RMP” or “the  
41 Company”) to implement the Pension Settlement Adjustments Balancing Account  
42 (“PSABA”) that is being established in response to the Commission’s order in the most  
43 recent general rate case filed by RMP in Docket No. 20-035-04.

44 **Q. PLEASE SUMMARIZE YOUR PRIMARY CONCLUSIONS AND**  
45 **RECOMMENDATIONS.**

46 A. I offer the following conclusions and recommendations:

47 (1) I do not object to the general mechanics of the PSABA proposed by RMP.  
48 However, I oppose RMP's attempt in this case to use the PSABA as a vehicle to correct a  
49 filing error made by the Company in its last general rate case.

50 (2) In the last general rate case, RMP proposed an adjustment to pension cost  
51 to include a projected 2021 settlement loss of \$11.9 million (Total Company)<sup>1</sup> in the test  
52 period. To implement this cost recovery, RMP included \$7.9 million of the forecasted  
53 settlement loss in pension expense and implicitly capitalized the remaining balance.  
54 However, under current accounting guidance, the Company is no longer permitted to  
55 capitalize its pension settlement losses. To correct this error in its rate case filing, RMP  
56 proposes that the initial PSABA baseline be set equal to Utah's share of the \$7.9 million  
57 as the amount of pension settlement losses included in rates, while allowing the Company  
58 to immediately begin deferring for later recovery through the PSABA the Utah-allocated  
59 portion of the remaining \$4.0 million (subject to true-up) that was originally deemed to  
60 have been capitalized in the rate case.

61 (3) I recommend that the Commission reject RMP's proposal to use the  
62 PSABA to correct its rate case error. Instead, for purposes of the PSABA, the  
63 Commission should deem 33.35% of the pension settlement loss to have been capitalized  
64 for ratemaking purposes. The PSABA baseline can be set at Utah's share of the \$7.9

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<sup>1</sup> Unless otherwise specified, all of the references in my testimony to the amount of the settlement loss are on a Total Company basis. Of course, the deferral in the PSABA will be limited to Utah's allocated share of the Total Company amount.

65 million as proposed by RMP, but any measurement of actual settlement losses in 2021  
66 should be assigned a 33.35% capitalization factor, consistent with the ratemaking  
67 treatment in the general rate case.

68 (4) This same approach should continue to be used in subsequent years, *i.e.*,  
69 33.35% of any future settlement losses in 2022 and thereafter should be deemed to be  
70 capitalized, until new rates are established in a subsequent rate case. This treatment will  
71 ensure consistency between any future deferral amounts and the baseline used for  
72 recovering settlement losses in the revenue requirement approved in the last rate case.

73

74 **II. PENSION SETTLEMENT ADJUSTMENTS BALANCING ACCOUNT**

75 **Q. PLEASE DESCRIBE RMP'S PSABA PROPOSAL.**

76 A. RMP's PSABA proposal is being made in response to the Commission's order in the  
77 Company's last general rate case directing that such a balancing account be established.  
78 The Company's proposal is presented in the direct testimony of Nicholas Highsmith. As  
79 described by Mr. Highsmith, RMP will calculate, on an annual basis, the difference  
80 between the amount of Utah-allocated pension settlement loss collected in rates versus  
81 the Utah-allocated amount expensed. Any differences will be deferred to a regulatory  
82 asset or regulatory liability with an annual carrying charge at the Commission-approved  
83 customer deposit rate under Schedule No. 300. The Company will continue to defer any  
84 differences booked into the regulatory asset or regulatory liability until the rate treatment  
85 is determined via a separate proceeding or general rate case. If a material balance is  
86 reached in either the regulatory asset or regulatory liability, the Company would initiate a  
87 proceeding to present its proposal for regulatory treatment, which may include a new

88 tariff to amortize the balance. Otherwise, the balance will be addressed in the next  
89 general rate case.<sup>2</sup>

90 **Q. DO YOU HAVE ANY OBJECTIONS TO THE GENERAL MECHANICS OF THE**  
91 **PSABA AS JUST DESCRIBED?**

92 A. Generally, no; although, as I will explain below, I object to RMP's application of these  
93 mechanics to the specific facts of this case. I also note for the record that UAE remains  
94 opposed to the use of an adjustment mechanism for these costs and, in particular, opposes  
95 setting the annual revenue requirement for pension settlement losses – which is a *non-*  
96 *cash* item – at the annual accounting cost rather than amortizing this expense over the life  
97 of the pension plan. But UAE recognizes that these latter two issues are not up for  
98 consideration in this case.

99

100 **III. SETTLEMENT LOSSES**

101 **Q. BY WAY OF BACKGROUND, WHAT ARE PENSION SETTLEMENT LOSSES?**

102 A. Under certain circumstances, settlements are recognized in ASC 715 pension cost, which  
103 is the basis for setting RMP's pension expense in a general rate case. A settlement is an  
104 irrevocable action that relieves the employer of primary responsibility for a benefit  
105 obligation, and eliminates significant risks related to the obligation and the assets used to  
106 effect the settlement. For example, a settlement occurs when the employer provides plan  
107 participants with lump-sum cash payments in exchange for their rights to receive  
108 specified benefits.

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<sup>2</sup> Direct Testimony of Nicholas L. Highsmith, lines 86-98.



109 **Q. WHEN MUST AN EMPLOYER RECOGNIZE GAINS OR LOSSES IN**  
110 **EARNINGS AS THE RESULT OF SETTLEMENTS?**

111 A. According to ASC 715-30-35-82, if the cost of all settlements in a year exceeds the sum  
112 of the service cost and interest cost components of net periodic pension cost (the  
113 threshold amount), the employer must recognize a pro rata portion of previously  
114 unrecognized gains or losses in earnings. In the last general rate case, RMP offered  
115 testimony that it anticipates such an event in the test year (2021) and projected that it will  
116 result in a settlement loss of \$11.9 million.

117 **Q. WHAT ARE UNRECOGNIZED GAINS AND LOSSES?**

118 A. Unrecognized gains and losses represent the cumulative adjustments to the value of  
119 pension plan assets and liabilities that have not yet been reflected in earnings through the  
120 net periodic pension cost. In any given year, actual experience will generally differ from  
121 the long-term assumptions used to set the net periodic pension cost. For example, the  
122 actual return on plan assets may be lower than the expected long-term return included in  
123 the net periodic pension cost, resulting in a loss. Changes to the actuarial assumptions  
124 used to value the pension assets and obligations can also result in gains or losses.

125       Employers, including utilities, are not required to immediately recognize these  
126 changes to the value of the pension plan assets or liabilities in net periodic pension cost.  
127 Instead, such gains or losses can be reflected as increases or decreases to “other  
128 comprehensive income,” which is excluded from the company’s net income. It is  
129 possible that, over time, gains and losses may offset each other, but a portion of the net  
130 gain or loss is required to be amortized (*i.e.* recognized in earnings) if a “corridor” of

131 materiality is exceeded.<sup>3</sup> The annual amortization of such losses is included in net  
132 periodic pension cost. In the context of Utah ratemaking, in the ordinary course of  
133 determining the revenue requirement in general rate cases, RMP ratepayers pay down  
134 RMP's pension plan's previously unrecognized losses over time, since the amortization  
135 of these prior losses is a component of the accounting pension cost that is included in  
136 rates.

137 When there is a settlement loss, this means that a portion of previously  
138 unrecognized losses must be recognized in earnings in a single year rather than amortized  
139 to pension cost over a longer period. Note, however, that this single-year charge is not a  
140 cash expense to the Company.<sup>4</sup> It is simply a change to the timing of when these costs  
141 are recognized for accounting purposes.

142

143 **IV. THE PROPOSED PSABA IN RELATION TO THE RATEMAKING**  
144 **TREATMENT OF SETTLEMENT LOSSES IN THE LAST GENERAL**  
145 **RATE CASE**

146 **Q. YOU STATED THAT YOU OBJECT TO RMP'S APPLICATION OF ITS**  
147 **PROPOSED PSABA MECHANICS TO THE SPECIFIC FACTS OF THIS CASE.**  
148 **PLEASE EXPLAIN.**

149 **A.** This inaugural case to implement the PSABA is complicated by an apparent error that  
150 RMP made in its general rate case filing with regard to its pension settlement loss. As a

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<sup>3</sup> The corridor rule was first established in Financial Accounting Standards Board ("FASB") Statement of Financial Accounting Standards No. 87 (Dec. 1985).

<sup>4</sup> See RMP response to UAE Data Request 2.6, included in UAE Exhibit 1.2.

151 result, one of the threshold issues before the Commission in this case is whether the  
152 newly-created PSABA can be used as a vehicle to correct a filing error made by the  
153 Company in a general rate case that has already been concluded. I recommend that the  
154 PSABA not be used for that purpose.

155 **Q. PLEASE DESCRIBE THE FILING ERROR AT ISSUE IN THIS CASE.**

156 A. As I explained in my direct testimony in the rate case, RMP proposed an adjustment to  
157 pension cost to include a projected 2021 settlement loss of \$11.9 million in the test  
158 period.<sup>5</sup> To implement this cost recovery, RMP included \$7.9 million of the forecasted  
159 settlement loss in pension expense and implicitly capitalized the remaining balance.<sup>6</sup> The  
160 problem is that under current accounting guidance, the Company is no longer permitted  
161 to capitalize its pension settlement losses. To correct this error in its rate case filing,  
162 RMP proposes that the pension settlement loss amount recognized in rates (“baseline  
163 amount”) should be set equal to Utah’s share of the \$7.9 million settlement loss that was  
164 expensed,<sup>7</sup> while permitting the Company to immediately begin deferring for later  
165 recovery through the PSABA the Utah-allocated portion of the remaining \$4.0 million<sup>8</sup>  
166 (subject to true-up) that was originally deemed to have been capitalized in the rate case.

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<sup>5</sup> The Utah-allocated portion of the \$11.9 million is \$5,184,769, shown on line 3 of Exhibit RMP\_\_(NLH-1).

<sup>6</sup> Docket No. 20-035-04, Direct Testimony of Kevin C. Higgins, lines 705-710.

<sup>7</sup> On lines 73-74 of his direct testimony, Mr. Highsmith refers to the \$7.9 million as the “starting balance for the pension balancing account,” but his use of the term “starting balance” in this context is somewhat confusing. It is clear that Mr. Highsmith is referring here to the pension settlement loss recognized in rates. For that reason I will refer to this as the “baseline amount.” It is also clear that Mr. Highsmith intends the “starting balance” in the deferral account to equal Utah’s share of the \$4.0 million in settlement loss that was deemed to be capitalized.

<sup>8</sup> The Utah-allocated portion of the \$7.9 million is \$3,455,809 and the Utah-allocated portion of the \$4.0 million capitalized amount is \$1,728,960, as shown on lines 8 and 10, respectively, of Exhibit RMP\_\_(NLH-1).

167 **Q. WHAT DOES IT MEAN TO “CAPITALIZE” A LABOR COST SUCH AS A**  
168 **PENSION SETTLEMENT LOSS?**

169 A. RMP has had a long-term practice of capitalizing a portion of its labor costs, including  
170 pension-related costs. When a portion of labor cost is capitalized, the capitalized portion  
171 is not included in operating expense, but rather is rolled into rate base, where it earns the  
172 Company’s authorized return and is depreciated over time, just like plant-in-service.

173 Consistent with this long-term practice, in the last general rate case, RMP  
174 separated its pension cost adjustment into two components: a portion that was expensed  
175 (66.65%) and a portion that was capitalized (33.35%), at least implicitly. As RMP’s  
176 forecasted pension settlement loss of \$11.9 million was included in its pension cost  
177 adjustment, it was treated in a like manner; that is, \$7.9 million of the settlement loss was  
178 added to expense and the \$4.0 million balance was assumed to be capitalized.

179 However, as explained in Mr. Highsmith’s direct testimony, RMP’s pension  
180 settlement losses are no longer eligible to be capitalized according to current accounting  
181 practices.<sup>9</sup> Therefore, RMP’s implicit capitalization of \$4.0 million of its pension  
182 settlement loss was done in error.

183 **Q. WHY DO YOU USE THE TERM “IMPLICIT CAPITALIZATION”?**

184 A. I describe RMP’s capitalization of the settlement loss as “implicit” because RMP applies  
185 the historical capitalization factor of 33.35% to its total wage and employee benefit cost  
186 adjustment in its rate case workpapers.<sup>10</sup> As I discussed above, this adjustment results in

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<sup>9</sup> Direct Testimony of Nicholas L. Highsmith, lines 63-80.

<sup>10</sup> See Docket No. 20-035-04, Exhibit RMP\_\_ (SRM-3), page 4.2.2. RMP’s Direct Total Labor adjustment of \$72.1 million was divided into the Non-Utility and Capitalized Labor portion of \$24.0 million (33.35%) and the Total Utility Labor (i.e., expense) portion of \$48.0 million (66.65%). The \$11.9 million pension settlement loss was included in the Pro Forma 2021 pension cost of \$14.5 million.

187 \$7.9 million of settlement loss being included as an expense in the revenue requirement.  
188 However, there is no explicit adjustment in the rate case filing in which the remaining  
189 \$4.0 million is separately added to rate base. Rather it is “deemed” to be included in rate  
190 base along with other labor costs that have been capitalized on the Company’s books.  
191 This approach would have been followed irrespective of whether the capitalization of the  
192 settlement loss was permissible or not. That is, even if the capitalization of the settlement  
193 loss were permissible (as it was in the past), the inclusion of the capitalized settlement  
194 loss in rate base would have been implicit insofar as any rate case adjustments were  
195 concerned. However, as the capitalization of the settlement loss is no longer permissible,  
196 and RMP no longer actually capitalizes settlement losses on its books (as I understand it),  
197 RMP is now trying to correct the error in its rate case filing in which the Company  
198 deemed a portion of its settlement loss to be capitalized.

199 **Q. DO YOU BELIEVE IT WOULD BE REASONABLE FOR THE PSABA TO BE**  
200 **USED AS A VEHICLE TO CORRECT A RATE CASE FILING ERROR?**

201 A. No. I recommended against adoption of this single-issue ratemaking mechanism in the  
202 first place. However, having adopted it, the Commission should not permit it to be used  
203 as a vehicle to correct the Company’s filing error in the last rate case. RMP did not  
204 identify this error during the pendency of that case, and it is my understanding that there  
205 would normally be no remedy available to the Company to retroactively correct its error  
206 absent the opportunity presented by the adoption of the PSABA. As the PSABA  
207 provides a going-forward benefit to the Company to defer and likely recover future  
208 settlement losses in between rate cases, this new benefit should not be expanded to allow

209 RMP to also reach backward to correct a rate case filing error that otherwise would not be  
210 permissible.

211 **Q. ARE THERE ADDITIONAL REASONS WHY THE PSABA SHOULD NOT BE**  
212 **USED AS A VEHICLE TO CORRECT RMP'S RATE CASE FILING ERROR?**

213 A. Yes. The Commission should also consider RMP's Response in Opposition to Petitions  
214 for Review, Reconsideration, or Rehearing ("Response in Opposition") filed in the last  
215 general rate case, Docket 20-035-04. In response to UAE's legitimate concerns that the  
216 initial amount included in the PSABA required clarification, RMP replied:

217 First, UAE's argument that the initial amount to be included in the balancing  
218 account is unclear is disingenuous. The Company presented undisputed evidence  
219 that \$11.9 million in actuarially-projected pension settlement losses are forecast in  
220 the test period, and *its rate request included that amount*.<sup>11</sup>

221 RMP concluded this argument by declaring: "It could not be more clear that the initial  
222 amount in the balancing account is \$11.9 million."<sup>12</sup>

223 This last statement stands in contrast to Mr. Highsmith's testimony in this case:

224 [O]nly \$7.9 million of the \$11.9 million projected settlement loss was included in  
225 base rates. Therefore, the starting balance for the pension balancing account  
226 should be \$7.9 million.<sup>13</sup>

227 Mr. Highsmith's explanation is offered in this docket, but the "last word" from RMP in  
228 the rate case docket is that its "rate request" included \$11.9 million in pension settlement  
229 losses.

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<sup>11</sup> Docket 20-035-04, RMP's Response in Opposition to Petitions for Review, Reconsideration, or Rehearing at 12. Footnote omitted. Emphasis added.

<sup>12</sup> *Id.* at 13.

<sup>13</sup> Direct Testimony of Nicholas L. Highsmith, lines 72-74.

230 **Q. DID THE COMMISSION’S FINAL ORDER IN THE GENERAL RATE CASE**  
231 **ALTER RMP’S TEST PERIOD REVENUE REQUIREMENT AS IT PERTAINS**  
232 **TO THE PENSION SETTLEMENT LOSS?**

233 A. No. The Company got exactly the revenue requirement it requested in its prepared case  
234 for this item, consistent with the Company’s exhibits and work papers as filed.<sup>14</sup>

235 **Q. IN LIGHT OF RMP’S CONTRADICTIONARY REPRESENTATIONS, HOW**  
236 **SHOULD THE PSABA BE IMPLEMENTED AS IT PERTAINS TO THE**  
237 **STARTING BALANCE AND ANY GOING-FORWARD DEFERRALS?**

238 A. The Commission should consider Mr. Highsmith’s recommendation that  
239 the “starting balance” (or baseline amount) for the pension balancing account should be  
240 \$7.9 million *in tandem* with RMP’s prior representation that its “rate request” included  
241 \$11.9 million in pension settlement losses. Indeed, as I explained earlier in my  
242 testimony, the Company’s “rate request” did include \$11.9 million in pension settlement  
243 losses: \$7.9 million was included in expense and \$4.0 million was deemed to be  
244 capitalized. The Commission should hold RMP to its final depiction of this issue in the  
245 general rate case and, for purposes of the PSABA, deem 33.35% of the pension  
246 settlement loss to have been capitalized for ratemaking purposes. The baseline amount  
247 can be set at \$7.9 million as proposed by Mr. Highsmith, but any measurement of actual  
248 settlement losses in 2021 should be assigned a 33.35% capitalization factor consistent  
249 with the ratemaking treatment in the general rate case, with only the remaining 66.65%  
250 expense portion eligible for inclusion in the PSABA.

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<sup>14</sup> The UT-allocated revenue requirement for this item may differ slightly from RMP’s Direct filing due to minor changes in jurisdictional allocation factors that are internally calculated.

251 **Q. UNDER YOUR PROPOSED TREATMENT, WHAT WOULD HAPPEN, FOR**  
252 **EXAMPLE, IF THE ACTUAL SETTLEMENT LOSS FOR 2021 TURNS OUT TO**  
253 **BE \$11.9 MILLION, AS FORECASTED IN THE RATE CASE?**

254 A. Under my proposal, if the actual settlement loss for 2021 turns out to be \$11.9 million as  
255 forecasted in the rate case, then there would be no 2021 deferral, because 33.35% (\$4.0  
256 million) will be deemed to be capitalized and the balance (\$7.9 million) will be equal to  
257 the amount that was included as an expense item in the rate case revenue requirement.

258 **Q. HOW SHOULD THE DEFERRAL BE CALCULATED AFTER 2021?**

259 A. This same approach should continue to be used after 2021. That is, 33.35% of any actual  
260 settlement losses should be deemed to be capitalized, until new rates are established in a  
261 subsequent rate case. Between now and then, this treatment will ensure consistency  
262 between any future deferral amounts and the baseline used for recovering settlement  
263 losses in the revenue requirement approved in the last rate case.

264 **Q. CAN YOU PROVIDE A FURTHER ILLUSTRATION OF HOW YOUR**  
265 **PROPOSAL WOULD WORK USING THE EXAMPLE PROVIDED IN MR.**  
266 **HIGHSMITH'S TESTIMONY?**

267 A. Yes. I provide such an illustration in UAE Exhibit 1.1. This exhibit reflects the  
268 illustrative pension settlement losses for 2021 to 2025 as shown in Mr. Highsmith's  
269 Exhibit RMP\_\_(NLH-1).



270 **Q. WHAT ABOUT USING \$11.9 MILLION AS THE “STARTING BALANCE” (OR**  
271 **BASELINE AMOUNT) AS ARGUED BY RMP IN ITS RESPONSE IN**  
272 **OPPOSITION?**

273 A. If the baseline amount were set at \$11.9 million and the actual settlement loss for 2021  
274 turns out to be \$11.9 million, then there would be no 2021 deferral, just as under my  
275 proposal. However, if the 2022 pension settlement loss turns out to be zero, under my  
276 proposal, the deferred credit to customers in 2022 would be Utah’s share of \$7.9 million  
277 (the same amount Mr. Highsmith would credit), whereas if the baseline amount were set  
278 at \$11.9 million, the 2022 credit to customers would be Utah’s share of \$11.9 million.  
279 Although this would be a good outcome for customers, it would not be reasonable  
280 because it would be \$4.0 million more than was included as an *expense* in the general rate  
281 case revenue requirement (RMP’s assertions in its Response in Opposition to Petitions  
282 for Review notwithstanding).

283 **Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?**

284 A. Yes, it does.