

Exhibit T-__ (RCM-1T)
Docket No. UE-020417
Witness: Roland C. Martin

**BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION
COMMISSION**

In re the Petition of

**PACIFICORP d/b/a PACIFIC POWER
& LIGHT COMPANY,**

**For an Accounting Order Authorizing
Deferral of Excess Net Power Costs.**

DOCKET NO. UE-020417

**DIRECT TESTIMONY OF
ROLAND C. MARTIN**

**STAFF OF
WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION**

February 5, 2003

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

2 A. My name is Roland C. Martin. My business address is 1300 South Evergreen Park
3 Drive SW, Olympia, Washington, 98504.

4
5 **Q. By whom are you employed and in what capacity?**

6 A. I am employed by the Washington Utilities and Transportation Commission as a
7 Regulatory Consultant in the Energy Section.

8
9 **Q. Would you please describe your educational background and professional
10 experience?**

11 A. I received a Bachelor of Science degree in Business Administration, majoring in
12 marketing management, from the University of the Philippines in April 1975. I
13 am also a graduate of the University of Pangasinan where I received a Bachelor
14 of Science degree in Commerce, majoring in accounting, in March 1980. On an
15 ongoing basis, I attend educational seminars on regulation and ratemaking.

16 I have been employed by the Washington Utilities and Transportation
17 Commission since May 1982. I have performed various phases of accounting
18 and financial analysis of regulated utility and transportation companies both
19 independently and jointly with other analysts, either as a lead or member of a
20 team. During the course of my employment, I have been a Commission Staff
21 witness in numerous formal contested proceedings before this Commission. I
22 was a Staff witness in consolidated Docket Nos. UE-991255, UE-991262, and UE-
23 991409 regarding the applications by Avista Corporation (Avista), Pacific Power
24 & Light Company (PacifiCorp), and Puget Sound Energy (PSE) to transfer their
25 respective interests in the Centralia facilities. I was also a Staff witness in Docket
26 No. UE-990267 regarding PSE's application to transfer its Colstrip facilities. I
27 also presented testimony in Cause Nos. U-84-28, U-88-2380-T, and UG-900190

1 concerning The Washington Water Power Company's (now Avista) filings for
2 general rate increases. I also testified in Cause No. U-85-32 concerning the
3 general rate increase filing of Continental Telephone Company of the Northwest,
4 Inc. and in Cause No. U-86-02 regarding PacifiCorp's filing for a general rate
5 increase. I have participated in a number of rate proceedings involving Puget
6 Sound Power & Light Company (Puget) including the past energy cost
7 adjustment clause (ECAC) filings, the general rate increase filing in Docket No.
8 U-89-2688-T, the proceeding that dealt with Puget's cost recovery proposals in
9 Docket Nos. UE-901183-T, UE-901184-P, and the Periodic Rate Adjustment
10 Mechanism (PRAM) implementation proceedings in Docket Nos. UE-910626,
11 UE-920630, UE-940728, and UE-950618. I was the lead revenue requirement
12 specialist in Puget's consolidated filings including a petition for
13 accounting of residential exchange benefits, rate design case, and general rate
14 change (Docket Nos. UE-920433, UE-920499, and UE-921262) and Puget's filing
15 to transfer revenues from PRAM rates to general rates (Docket No. UE-951270). I
16 was a member of the Staff team in the proceeding regarding the merger of Puget
17 and Washington Natural Gas Company into PSE in Docket No. UE-960195.

18
19 **Q. What issues do you address in your testimony?**

20 A. PacifiCorp operates in six states: Washington, Utah, Oregon, Idaho, California
21 and Wyoming. My testimony addresses the issue of allocating power costs and
22 other costs among these states, in the context of the Company's deferred cost
23 proposal in this case.

24
25 **Q. Please summarize your testimony on that subject.**

1 A. PacifiCorp’s analysis uses the “Modified Accord” method to allocate current and
2 prospective power and transmission costs and other common costs among the
3 various states in which it operates. The Modified Accord allocation method
4 contains inherent flaws such as allocating a disproportionate share of the cost of
5 new generation to states, like Washington, with load growth that does not
6 require those resources. The Modified Accord allocation method also has not
7 previously been accepted by this Commission nor by Staff for ratemaking
8 purposes. Therefore, Staff recommends that the Commission reject any
9 Washington results of operations portrayals and analyses that are based on the
10 Modified Accord.

11

12 **Q. Do you sponsor any exhibits in support of your testimony?**

13 A. Yes, I sponsor Exhibit No. ____ (RCM-2) and Exhibit No. ____ (RCM-3):

14 RCM-2: Load Growth Data 1989 - 2001

15 RCM-3: Changes in generation allocators

16

17 **Q. Please provide a brief history of the interjurisdictional cost allocation process.**

18 A. PacifiCorp, as it exists today, is the result of the acquisition of Utah Power &
19 Light Company by PacifiCorp in 1989. Following the acquisition, PacifiCorp
20 convened a group of representatives from the Company and from the
21 jurisdictions served by the Company to study interjurisdictional cost allocation
22 issues. The group became known as the “PacifiCorp Interjurisdictional Task
23 Force on Allocations” (PITA). I participated in most PITA meetings as one of the
24 representatives of the Commission staff. A main purpose of the group was to
25 create an allocation method that satisfied the objectives of fairness and cost
26 causation. Meeting the fairness objective meant that the lower cost PacifiCorp

1 jurisdictions, which included Washington, should not receive overall cost
2 increases as a result of acquiring the higher cost Utah division. It also meant that
3 the benefits from the consolidation should be fairly and reasonably shared
4 among all PacifiCorp jurisdictions. To satisfy the cost causation objective,
5 jurisdictions were to assume responsibility for direct costs each particular
6 jurisdiction imposed on the system, and for those total system costs which
7 cannot be directly assigned. The total system power costs were to be allocated
8 based on power requirements.
9

10 **Q. What were the results of those PITA meetings?**

11 A. After the PacifiCorp acquisition became effective in January, 1989, numerous
12 working meetings were immediately held to study interjurisdictional allocations
13 of system plant and expenses. The PITA developed a “Consensus Allocation
14 Method” which served as the basis for PacifiCorp’s jurisdictional allocations
15 from March 1990 through December 31, 1992. This method evolved from the
16 various allocation methods previously studied by the group. Some major
17 features of this method included divisional assignment of pre-acquisition plant,
18 recognition of hydro and transmission endowments or benefits that were
19 brought to the acquisition by each division, and direct assignment of pre-
20 acquisition firm off-system sales and purchases . The Pacific division included
21 California, Washington, Oregon, Wyoming-East and Montana. The Montana
22 service territory was sold in 1998. The Utah division includes Utah, Idaho and
23 Wyoming-West. The Consensus Allocation Method was used for a limited
24 period of time because PITA recognized that that allocation method would
25 begin to produce undesirable results after 1992 such as disproportionate sharing
26 of merger benefits among jurisdictions. PITA continued to study alternative

1 allocation methods to correct the shortcomings of the Consensus Allocation
2 Method. The group eventually developed another allocation method called the
3 “PITA Accord Method”. The group maintained that an appropriate target was
4 an approximate “50%/50%” sharing of merger benefits between the Pacific and
5 Utah divisions.

6 The PITA Accord Method eliminated the divisional assignment of certain
7 costs and revenues, but retained the divisional assignment of pre-acquisition
8 plant and the hydro and transmission endowments. The PITA Accord Method
9 became the method used by PacifiCorp in its post 1992 regulatory filings until
10 the development of the Modified Accord method in 1997. The Modified Accord
11 method eliminated the transmission endowment and reflected a revised method
12 for valuing the hydro endowment. In subsequent meetings of PITA, various
13 proposals to further amend the Modified Accord method were discussed. It is
14 important to note that Washington consistently advocated recognition of the old
15 Pacific operations, with its low cost resource portfolio, as an element of any
16 allocation methodology to meet the merger objectives.

17
18 **Q. Was the Modified Accord method adopted in all of PacifiCorp's jurisdictions?**

19 A. No. The Utah Public Service Commission in 1998 adopted a “Rolled-In”
20 allocation method that allocates common costs, including power costs, system-
21 wide to all jurisdictions. (PSC of Utah Docket No. 97-035-04.) Nevertheless, PITA
22 continued to meet on two occasions in 1999 to discuss cost allocation issues.
23 PITA ceased to exist after its last meeting in April 2000.

24
25 **Q. What ensued after PITA’s demise?**

1 A. In late 2000, PacifiCorp pursued a different path to solve the problems that arise
2 from operating in many jurisdictions. Some of the problems include the lack of
3 clarity on responsibility for future resources and the absence of consensus on
4 each state's entitlement to existing generating resources. The Company
5 developed the "Structural Realignment Proposal" (SRP) – a comprehensive
6 restructuring of PacifiCorp into six separate electric companies, a generation
7 company and a service company. The SRP was filed with this Commission on
8 December 1, 2000 in Docket No. UE-001878. However, the SRP was withdrawn
9 in 2002 so that the Company could pursue the current multi-state process (MSP)
10 to investigate and clarify cost allocation of generation resources and other issues.
11 The MSP is still on-going. Staff is an active participant in the MSP on behalf of
12 the Commission.

13
14 **Q. Please describe the allocation method used by the Company in Docket No. UE-**
15 **991832, the 1999 Rate Case.**

16 A. In Docket No. UE-991832, PacifiCorp's general rate case, the Company proposed
17 the use of the Modified Accord allocation method to determine Washington
18 revenue requirements. This was the last method discussed prior to the breakup
19 of PITA. Modified Accord maintains the pre-acquisition plant in the respective
20 Utah and Pacific divisions. The facilities are allocated to the jurisdictions as it
21 was prior to the acquisition, based on the premise that the Company's costs were
22 the result of prior decisions to meet the demands of the former companies. New
23 plant, that is, plant added since about 1989, including hydro plant, is allocated
24 system-wide.

25 Modified Accord attempts to maintain the value of the hydro-based system
26 within the Pacific division by calculating a value for the hydro-generation and

1 crediting that value to the Pacific division states. However, as I will discuss in
2 more detail, there were problems with Modified Accord.

3
4 **Q. Could you please give a brief explanation of how the primary allocation**
5 **factors are calculated by the Modified Accord method?**

6 A. Yes. The Modified Accord method primary allocation factors are based on
7 demand and power consumption in each state. Generation plant and power
8 purchases are allocated by three different, but related, allocation factors.

9 The System Capacity factor (SC) is based on the twelve monthly
10 coincidental peak loads at the time of system peak. Each state's megawatts
11 contribution to those 12 peaks is determined and each state's percentage of the
12 total is calculated.

13 The System Energy factor (SE) is based on each state's annual
14 consumption in megawatt-hours and the percentage each state is of the total.

15 The System Generation factor (SG) is composed of 75% of the SC and 25%
16 of the SE.

17
18 **Q. In the 1999 Rate Case, did Staff contest the Modified Accord allocation**
19 **method?**

20 A. The case was settled before Staff filed testimony on revenue requirements or
21 allocations. Thus, Staff neither supported nor opposed the Modified Accord
22 method.

23
24 **Q. Did the Commission accept a specific allocation method in Docket No. UE-**
25 **991832?**

1 A. No. The 1999 general rate case was PacifiCorp's first opportunity since the
2 acquisition of the Utah properties in 1989 to satisfy its burden to prove that the
3 allocation method it used produced fair results for its Washington operations.
4 This was also PacifiCorp's opportunity to show that its proposal for cost
5 allocations was consistent with the Commission's order approving the
6 acquisition in 1989 and that Washington's customers were not harmed by the
7 acquisition. The Merger Order states, "The Commission continues to be
8 concerned about the effects on Pacific's ratepayers of merging with a higher cost
9 system, and believes the integration of the power supply function for the two
10 companies should be done in a manner consistent with Pacific's least-cost
11 planning process, now getting underway. In the meantime, the Commission
12 views Pacific's current average system costs as the appropriate basis for rates."
13 (Docket No. U-87-1338-AT, Second Supplemental Order Approving Merger With
14 Requirements at 14). However, the Company and other interested parties in the
15 1999 Rate Case entered into a Stipulation establishing a Rate Plan that provided
16 the Company rate relief over the initial three years of a five-year period. The
17 revenue requirement increases were not based on Modified Accord to calculate
18 Washington's rate base, operating expenses, or net operating income. They were
19 the result of the Rate Plan as discussed by Staff witness Mr. Elgin.

20

21 **Q. Earlier you stated that you would discuss flaws in the Modified Accord cost**
22 **allocation method. Please elaborate on the problems and issues you see with**
23 **that allocation method?**

24 A. The key flaw which renders Modified Accord unreasonable for purposes of
25 assigning costs to Washington is that it fails to recognize costs caused by
26 consistently disparate load growth in the jurisdictions the Company serves. The

1 system-wide allocation of new generation built to serve significant load
2 increases, particularly in Utah, results in an unfair distribution of power costs to
3 other states.

4 The simplicity of dividing new power costs on a usage-based allocation
5 scheme has appeal, but for it to remain fair, the various jurisdictions must grow
6 at similar rates. Reality contradicts this assumption. Growth in Utah is
7 substantially greater than in other states. Yet, only a portion of the generation
8 built to serve the load growth in Utah is allocated to Utah under the Modified
9 Accord method.

10
11 **Q. Are there other flaws with the Modified Accord allocation methodology?**

12 A. Yes. State commissions may approve special contracts with industrial customers
13 to achieve economic development or other purposes specific to that state.
14 Modified Accord inappropriately allocates on a system-wide basis these special
15 contracts with industrial customers, in violation of the cost-causation principle.
16 Modified Accord also allocates almost all state taxes among all the jurisdictions.
17 System-wide allocation of some taxes, such as state income taxes and revenue
18 based taxes, again contradicts the cost-causation principle.

19
20 **Q. Can you illustrate the key flaw of the Modified Accord you mentioned earlier
21 with respect to disparate load growth among the states?**

22 A. Yes. Of PacifiCorp's six states, Utah is growing the fastest. Exhibit ____ (RCM-2)
23 shows the load growth and the peak loads on PacifiCorp's system from 1989 to
24 2001. The data shows that total load for PacifiCorp grew 22%. Of the six states
25 now served by PacifiCorp, Washington's load grew by 23% while Utah's load
26 increased 57%.

1 Peak loads, as measured by the sum of the twelve coincidental peaks for
2 each month, grew 22% for the total system, 60% in Utah and only 18% in
3 Washington. A closer examination shows that July peak load in Utah grew 78%
4 from 1989 through 2001. The system July peak grew 34% with Washington's July
5 peak increasing only 27%. This data is graphically portrayed by Staff witness
6 Mr. Buckley in his testimony.

7
8 **Q. How does this data affect the primary Modified Accord allocation factors?**

9 A. Using the data in Exhibit ____ (RCM-2), we can calculate the System Energy,
10 System Capacity, and System Generation factors. Exhibit ____ (RCM-3) presents
11 this information. These numbers are not equal to those applied in regulatory
12 filings since I removed the sales to northern Idaho and Montana. Those two
13 areas have been sold since 1989. The data presented is for illustrative purposes
14 only.

15 Washington's System Generation allocation factor has declined slightly to
16 9.2% from 9.4% since 1989. Over the same time period, however, Utah's SG
17 factor increased to 38.1% from 29.1%.

18
19 **Q. Doesn't this indicate that Utah is allocated a higher percent of the power costs
20 under Modified Accord?**

21 A. Yes. But, as Mr. Buckley points out, two new generation plants, West Valley and
22 Gatsby II, were constructed for the purpose of meeting the summer peak load in
23 Utah. Utah will only be allocated about 38.1% of the cost of those plants under
24 the Modified Accord method. Washington will pick up 9.2% of the cost of those
25 plants even though the need for those peaking resources is driven by growth in
26 Utah's summer peak load. The Company has not made a demonstration that

1 these resources are needed for, or would provide benefits to, Washington. The
2 appropriate forum for determining the need and benefits from new resource
3 additions is a general rate case.
4

5 **Q. Can you demonstrate why the Washington results of operations and financial**
6 **data presented by Mr. McDougal can not be used as dependable indicators of**
7 **the Company's performance in this state?**

8 A. Yes. The Modified Accord results of operations used by the Company to support
9 its deferral petition is not the only portrayal of results of operations that could be
10 presented. For instance, based on the Modified Accord method, the Washington
11 adjusted results of operations for the period ending March 2002 show a return on
12 rate base of 6.717 % and a return on equity of 6.892 %. (See Exhibit__ (SRM-2.)

13 Staff requested the Company to measure these indicators using the PITA
14 Accord Method, the allocation method used during the mid-1990s. The result is
15 significantly different. The return on rate base improved to 7.274 %, while the
16 return on equity increased to 8.11 %. This clearly illustrates that Washington
17 results of operations cannot be reliably depicted and are inherently influenced by
18 the chosen allocation method.

19 Neither the Modified Accord method, nor any other post-merger
20 allocation methods, were ever approved in Washington for ratemaking purposes.
21 It is unlikely that the Modified Accord, or other historical methods developed by
22 PITA, will be used in the future because none of these methods solve the flaws
23 and shortcomings discussed earlier. Nor is any party to the MSP discussions
24 actively advocating any of the historical methods or the Modified Accord. New
25 paths have been proposed.
26

1 **Q. You mentioned earlier that Modified Accord reserves the benefits of the**
2 **hydro-based system to the Pacific division states. Is that correct?**

3 A. Yes. Modified Accord explicitly reserved, for the most part, the benefit of low-
4 cost hydro-power generation facilities to the customers within the pre-merger
5 Pacific Power & Light Company jurisdictions. Under Modified Accord, these
6 Pacific jurisdictions, where most of the hydro facilities are located, get the
7 majority of the benefits of the lower cost hydro outputs through a fuel expense
8 credit. However, this feature of Modified Accord has been rendered meaningless
9 because Utah decided to disregard the hydro benefit assignment and use a
10 rolled-in allocation method that drastically differs from other states. As a result,
11 the collective claims to the hydro benefits do not equal 100 per cent and the sum
12 of all jurisdictional costs and benefits does not mirror the Company's total cost of
13 providing service. The consequence of Utah's action is the development of
14 different versions of results of operations, rates of return, returns on equity, etc.
15 In combination with Modified Accord's deficiency regarding cost responsibility
16 for new generating resources, and other issues that impact allocation of costs
17 (such as, direct access mandates and the sale of a service territory), the results of
18 operations for PacifiCorp's various states are inconsistent and meaningless on a
19 collective basis. This situation gives the Company an opportunity to over or
20 under recover its total cost of providing service in all of its jurisdictions.

21
22 **Q. Is the situation you discussed true not only with the Modified Accord method,**
23 **but also when the different jurisdictions do not agree on a single method of**
24 **allocation?**

25 A. Yes.

1 **Q. Is this a continuing problem and how is the Company addressing it?**

2 A. Yes, it is a problem for PacifiCorp, and a risk PacifiCorp accepted when it
3 requested the acquisition in 1987. The differing allocation methods in use by the
4 various states do not allow the Company the potential to recover all of its costs.
5 The SRP proposed in 2000 was PacifiCorp's attempt to solve the "hole" left in the
6 jurisdictional allocations and to resolve problems arising from legislation in
7 Oregon. PacifiCorp's SRP proposal did not address key jurisdictional or other
8 issues of every state commission. In response, PacifiCorp proposed the current
9 MSP to include commissions and stakeholders in the solution to PacifiCorp's
10 problem. Those meetings are underway and progress is being made.

11
12 **Q. Does Staff support a particular alternative to Modified Accord?**

13 A. Staff is working on this issue by participating in the MSP and there is a method
14 Staff believes to be potentially acceptable. This method, originally proposed by
15 Idaho Staff, basically allocates costs according to control areas. A control area is
16 an electrical system bounded by interconnection, metering, and telemetry. It
17 controls generation directly to maintain its interchange schedule with other
18 control areas and contributes to frequency regulation of the interconnection.
19 However, it is premature to draw conclusions at this time about the outcome of
20 the MSP.

21
22 **Q. Given the discussion above, is the Company's request to defer certain power
23 expenses reasonable?**

24 A. No. Mr. McDougal's exhibits showing past, current, and future results of
25 operations are based on allocation assumptions known to be faulty. Power costs
26 and other common costs allocated to Washington based on Modified Accord will

1 not be comparable to future costs based on another method. Before
2 Washington's costs can be reasonably determined, a more equitable allocation
3 plan must be agreed upon by PacifiCorp states, and approved by the
4 Washington Commission.

5

6 **Q. Does this conclude your testimony?**

7 A. Yes.