1 **Q. Mr. Wrigley, have you previously filed testimony in this proceeding?**
2 A. Yes, I filed direct testimony in this proceeding.
3 **Q. Please describe the purpose of your rebuttal testimony.**
4 A. The purpose of my rebuttal testimony is twofold. First, I update the revenue
5 requirement that the Company is presenting in its rebuttal testimony. This update
6 incorporates adjustments to which the Company is agreeing in its rebuttal
7 testimony (in either my testimony or that of other Company witnesses), and the
8 impact of a stipulation the Company has reached with the Industrial Customers of
9 Northwest Utilities (ICNU) regarding Net Power Costs.
10 Second, I address certain adjustments in the testimony of Staff witnesses
11 Schooley, Ward, Kermode and Mariam; Public Counsel witness Effron; and
12 ICNU witnesses Selecky and Falkenberg.
13 **Updated Revenue Requirement**
14 **Q. What is the revised revenue requirement being sought by the Company in**
15 **this proceeding?**
16 A. The Company's updated revenue requirement increase is $32,599,613. While this
17 represents an increase of 14.9 percent over current rates, it is a reduction of
18 $6,654,000 from the amount requested by the Company in its original filing.
19 **Q. Why has the Company updated its revenue requirement request since its**
20 **original filing?**
21 A. The Company has updated its request to take account of information developed
22 during the discovery process in this proceeding, and in response to a number of
23 the points raised in the opposing testimony. In addition, the Company's initial

1 filing included forecasted data. With the passage of time, these numbers have
2 become more certain or refined. Finally, the Company reached an agreement
3 with ICNU regarding Net Power Costs in this proceeding. Based on all of these
4 developments, the Company revised its request as appropriate.

5 **Uncontested Adjustments**

6 **Q. Please describe the adjustments in the opposing testimony that the Company**
7 **is accepting in their entirety.**

8 A. The following table lists those adjustments and their individual impact on revenue
9 requirement. These adjustments are accepted in their entirety by the Company.
10 As explained on page 7 of Mr. Schooley's testimony, however, there may be a
11 variance between the adjustment as calculated by the Company and as calculated
12 by Staff (or other intervening parties) for various reasons, but these differences
13 are not due to a dispute regarding the substance of the adjustment. Rather, they
14 are due to different recommendations on rate of return, the inclusion of revenue
15 related expenses and/or the use of a different conversion factor. In addition, the
16 settlement with ICNU regarding Net Power Costs impacts the Embedded Cost
17 Differential calculation (per the Revised Protocol) and costs are reallocated
18 between the states.

1 Uncontested Adjustments

Adj. No.	Description	Revenue Requirement Impact
3.8	Out of Period Revenue Adjustment	($1,713,782)
4.2	Remove Naches O&M	($11,900)
4.13	ScottishPower Cross Charge	($372,292)
5.1a	NPC Settlement	($2,514,961)
7.3a	Renewable Energy Credit	($15,202)
8.5a	Reverse Company Environmental Adjustment (8.5)	$201,043
8.10	Production Factored Rate Base	($3,413,288)
8.11	Remove Naches Rate Base	($17,448)
8.11a	Remove Skookumchuck	($62,796)
8.12	Remove Trail Mountain	($195,814)
8.13	Remove Environmental Remediation	($238,250)
8.14	Remove Transition Regulatory Asset	($1,805,004)
	Total Uncontested Adjustments	**($10,159,694)**

2 **Q. Please describe each of these uncontested adjustments in more detail.**

3 A. Mr. Effron has proposed an adjustment – Out of Period Revenue Adjustment
4 (Adjustment No 3.8) – updating the Company's present revenues. As discussed
5 in the testimony of Mr. Griffith, the Company has accepted a refined version of
6 Mr. Effron's adjustment resulting in a larger change in revenue requirement than
7 that proposed by Mr. Effron.

8 The Company accepts the following adjustments of Mr. Schooley:

9 - 4.13 – ScottishPower Cross Charge
10 - 8.10 – Production Factored Rate Base
11 - 8.11 – Remove Naches and Skookumchuck (modeled by the Company
12 as Adjustments 4.20, 8.11 & 8.11a)
13 - 8.12 – Remove Trail Mountain
14 - 8.13 – Remove Environmental Remediation

1 In addition, the Company incorporated into its original filing, as
2 Adjustment 8.5 – Environmental Settlement, the Company's proposed procedure
3 dealing with environmental expenses. This procedure, however, was rejected by
4 the Commission in Docket No. UE-031658. Concurrent with the Staff
5 Adjustment 8.13, the Company's Adjustment 8.5 should be reversed and is
6 modeled above as Adjustment 8.5a.
7 Finally, the Company agrees in principle with Mr. Schooley's adjustment
8 8.14 – Remove Transition Regulatory Asset. However, Mr. Schooley has
9 incorrectly calculated taxes and thus overstated the revenue requirement impact.
10 (See Exhibit No.___(TES-3), column 8.14, line 63 where operating revenue is
11 incorrectly set to zero).
12 The Company accepts Mr. Kermode's Renewable Energy Tax Credit
13 update (included above as Adjustment 7.3a) and includes the revenue requirement
14 impact of the Company's settlement with ICNU as Adjustment 5.1a.
15 **Q. Does this conclude the adjustments that the Company accepts in their**
16 **entirety?**
17 A. Yes. In addition, there are certain adjustments proposed by Staff with which the
18 Company is in partial agreement. I will now describe those in more detail.
19 **Partially Contested Adjustments**
20 **Q. Please describe the following table.**
21 A. The following table shows all the changes to the Company's original revenue
22 requirement and also lists those of the adjustments that the Company is accepting
23 in part.

1 Revised Revenue Requirement

Adj. No.	Description	Revenue Requirement Impact
	Original Revenue Requirement Increase	**$39,204,568**
	Total Uncontested Adjustments	**($10,159,694)**
Partially Contested Adjustments		
4.10a	Wages and Benefits	($41,818)
4.10b	Pension Update	($41,109)
4.18	Miscellaneous A&G	($25,078)
5.8	Hydro Deferral Recovery	$3,089,831
	Partially Contested Adjustments	$2,981,825
	Updated Factors, uncollectibles, net to gross	$572,915
	Revised Revenue Requirement	**$32,599,613**

2 **Q. What is the Company's response to Mr. Schooley's Adjustment 4.10a –**
3 **Wages and Benefits?**
4 A. Mr. Wilson and Mr. Rosborough provide the Company's response to the portion
5 regarding Incentive Pay Adjustments and Pension and Benefits Adjustments. The
6 Company accepts Mr. Schooley's adjustments for non-union salary increases and
7 severe winter storms, which reduce the Company's revenue requirement. In
8 addition, that portion of Pension Adjustment which updates the actual FAS 87 and
9 FAS 106 expense is accepted by Mr. Rosborough in his testimony, and I have
10 incorporated this above as Adjustment 4.10b.
11 **Q. Please respond to Mr. Ward's Adjustment 4.18 – Miscellaneous**
12 **Administrative and General Expenses.**

1 A. I have prepared a four page exhibit, Exhibit No.___(PMW-6), comparable to Mr.
2 Ward's Exhibit No.___(CJW-2) to assist in this discussion.
3 As can be seen on the schedules, Mr. Ward made no adjustments to
4 Accounts 910, 912, and 913. The Company accepts his adjustments to Accounts
5 901, 904, and 920 and the disallowance of the rate base account.
6 With regard to Account 921 (see page 2 of my Exhibit), further analysis
7 by the Company reveals that the $44,328 of expenses related to EEI, shown on
8 page 1 of Exhibit No.___(CJW-2), were incurred for various EEI sponsored
9 conferences and training activities attended by Company employees. Thus these
10 expenses should be allowed at 100 percent, rather than disallowed at 43.6 percent
11 as proposed by Staff. With this small change, the Company accepts the rest of
12 Mr. Ward's adjustment.
13 With regard to Account 923 (see page 3 of the Exhibit), the Company
14 disagrees on a policy level with the reallocation of expenses, related to rate case
15 activity in states other than Washington, away from Washington and the
16 reallocation of Washington rate case costs on a situs basis. In addition, Mr.
17 Ward's calculation does not mirror his testimony, which would disallow $2.25
18 million on a Total Company basis ($169,000 Washington allocated) and then
19 allocate $336,000 directly to Washington, the net result of which is to increase
20 Washington expense by $148,000. The Company does not agree with the
21 methodology which produces such an approach. If implemented, however, this is
22 the correct calculation, which has been accepted by the Company in calculating

1 the revenue requirement in its rebuttal testimony. In light of this turn of events,
2 the Company would not oppose the withdrawal of this adjustment by Staff.
3 With regard to Account 930 (see page 4 of my Exhibit), Staff has three
4 specific disallowances:
5 - a nature conservancy disallowance;
6 - Membership, Civic and Political Activities; and
7 - EEI Activities.
8 The Company agrees to the first disallowance. The third disallowance –
9 EEI Activities – is double counted, as this amount is also included in
10 Membership, Civic and Political Activities.
11 Further analysis by the Company of account 930 shows the WECC
12 membership dues were $734,027 (Total Company). Since the Company operates
13 two control areas within the Western Interconnection, WECC membership is
14 required. Thus, these membership costs should be allowed.
15 Mr. Ward identifies $847,428 membership dues paid to EEI but includes
16 $15,000 charged to account 426.4, which is a below-the-line account and is not
17 included in the results. In addition, according to the invoices sent to the Company
18 by EEI, only 25 percent of fees are for legislative activities. The Company would
19 agree to a disallowance at this level rather than the 43.6 percent recommended by
20 Mr. Ward.
21 **Q. Mr. Buckley proposes to amortize the Hydro Deferral Recovery costs over**
22 **three years with a return on the unamortized balance. Does the Company**
23 **agree with that approach?**

1 A. Yes. However the Company proposes the estimated balance of $7.5 million as
2 described in Mr. Widmer's testimony rather than the amount proposed by Mr.
3 Buckley.

4 **Q. Does this conclude the adjustments that the Company has partially**
5 **accepted?**

6 A. Yes. In addition I have prepared Exhibit No.___(PMW-7), a three page exhibit
7 which provides the detail of each of the adjustments accepted either in part or
8 total by the Company.

9 **Q. Please describe Exhibit No.___(PMW-8).**

10 A. This exhibit revises Tabs 1 & 2 of Exhibit No.___(PMW-3), provided as an
11 exhibit to my direct testimony, to reflect the adjustments contained in Exhibit
12 No.___(PMW-7).

13 This concludes the first part of my testimony. In the second part, I address
14 certain adjustments opposed by the Company.

15 **Weather Normalization**

16 **Q. In addition to the issues addressed in Mr. Klein's testimony, do you have any**
17 **issues with respect to Dr. Mariam's calculation of the weather normalization**
18 **adjustment?**

19 A. Yes. Mr. Klein's testimony addresses the problem with Dr. Mariam's weather
20 normalization methodology. I will address the serious problem of Dr. Mariam's
21 failure to model the change in cost allocation accurately.

22 The methodology approved by this Commission allocates costs among the
23 states based upon their percentage of energy and peak demand. Dr. Mariam's

1 adjustment increases Washington retail sales – and thus Washington energy and
2 peak demand – but his adjustment fails to reallocate costs correctly.
3 **Q. How should Dr. Mariam have modeled this change in retail sales?**
4 A. As described in the Company's response to Staff Data Request 260, Dr. Mariam's
5 change in Washington retail sales of 94,710 MWh would increase Total Company
6 power costs by $1.48 million, of which $121,000 would be allocated to
7 Washington. In addition, increasing Washington sales increases Washington
8 energy and peak loads. Under the dynamic cost causation methodology approved
9 in this jurisdiction, this increases the expense and rate base charged to
10 Washington. In the Company's response to the Data Request, we indicated that
11 this change in sales would increase Washington revenue requirement by $3.87
12 million. The effect of these adjustments is to decrease Dr. Mariam's proposed
13 $4.9 million adjustment to $920,000. In addition, an increase in the test year load
14 would reduce the Production Factor adjustments proposed by the Company in its
15 original filing and discussed by Mr. Schooley in his testimony.
16 **Q. Mr. Klein's testimony identifies a major problem with Dr. Mariam's**
17 **methodology. What effect would this have on the above analysis?**
18 A. Mr. Klein's testimony indicates that the 43,629 MWh adjustment proposed by
19 Dr. Mariam should be reduced to 29,517 MWh, which reduces the $4.9 million
20 discussed above to $4.186 million. In addition, the Net Power Costs allocated to
21 Washington would decrease from $121,000 to $102,700. The change in
22 allocation factors would reduce the revenue requirement increase by $3,421,000,
23 thereby further reducing Dr. Mariam's recommended adjustment to $663,000. As

1 described above, a further reduction should also be made to account for the
2 change in the Production Factor.
3 **Q. What is your recommendation regarding Dr. Mariam's weather**
4 **normalization adjustment?**
5 A. It should be rejected by the Commission for the reasons set forth above and in Mr.
6 Klein's testimony.
7 **Cash Working Capital**
8 **Q. Does the Company agree with Mr. Schooley's proposed adjustment to Cash**
9 **Working Capital?**
10 A. No. The balance-sheet based, Investor Supplied Working Capital (ISWC)
11 methodology used by Mr. Schooley is a less accurate, short-cut method that is
12 inferior to that used by the Company. In fact, it is unreliable and Mr. Schooley
13 demonstrates that by the differences in how he calculated ISWC in the
14 Company's last Washington general rate case (Docket No. UE-032065) and in
15 this case. In doing so, he demonstrates that no consistent approach is being used.
16 In contrast to the capricious ISWC methodology, the Company uses a Lead Lag
17 study for calculating cash working capital that is recognized by FERC and
18 industry experts as the most accurate, thorough, and preferred method.
19 In addition, even if the Commission chooses to adopt the inferior method
20 proposed by Mr. Schooley, he has made a number of errors that lead to erroneous
21 results.
22 **Q. Why does the Company use a Lead Lag study?**

1 A. The use of a Lead Lag study is recognized by FERC and other regulatory utility
2 experts as the preferred method to calculate cash working capital requirements.
3 FERC, for its part, states that "[w]here a fully developed and reliable lead-lag
4 study is available in the record, we will utilize that study to determine the
5 working capital allowance." *Docket No. RM84-9-001*. FERC in its NOPR on
6 "Calculation of Cash Working Capital Allowance for Electric Utilities" stated that
7 "a fully-developed and reliable lead lag study is the most accurate method of
8 determining the working cash needs of a particular utility." *Docket No. RM84-9-*
9 *000*.

10 **Q. Please explain the Lead Lag study approach and why it is superior to the**
11 **ISWC method for calculating cash working capital.**

12 A. The purpose of a working capital adjustment for regulated purposes is to calculate
13 the Cash Working Capital required to cover the time between payment for
14 services and receipt of revenue. If, on average, the time difference between
15 providing the service and collecting the associated revenue exceeds the time
16 difference between providing the service and paying the associated expenses, the
17 utility is experiencing a "net revenue receipt lag." This necessitates maintaining a
18 working cash balance that must be funded. Cash working capital based on a Lead
19 Lag study is calculated by taking total operation and maintenance expense
20 allocated to the jurisdiction (excluding depreciation and amortization) and adding
21 its share of allocated taxes, including state and federal income taxes and taxes
22 other than income. This total is divided by the number of days in the year to
23 determine the Company's adjusted daily cost of service. The daily cost of service

1 is multiplied by net lag days to produce the adjusted cash working capital balance.

2 Because of the thoroughness and data and resource intensity of this

3 approach, the Company acknowledges that it is not universally feasible for all

4 utilities. The cost and effort to complete a Lead Lag study is reasonable for

5 PacifiCorp because it is accepted in five of the Company's jurisdictions. In the

6 Company's direct case, Cash Working Capital is based on its 2003 Lead Lag

7 study.

8 The balance sheet-based ISWC method, on the other hand, is flawed as it

9 is usually applied in that it "assumes that all non-utility or non-jurisdictional

10 assets are investor supplied…[which] represents a *fatal flaw* in the typical

11 application of this approach," according to Robert Hahne in *Accounting for*

12 *Public Utilities.* Additionally, this method provides a snapshot of the current

13 liquidity of a company at a point in time, while determination of cash working

14 capital requirements is a moving picture over time of cash flows into and out of

15 the Company's treasury.

16 Another shortcoming of this approach described in Mr. Hahne's text is

17 that if unbilled revenues are not recorded, which is typically the case using this

18 method, the cash working capital requirement may be substantially understated as

19 it "does not recognize the working capital requirement from the time service is

20 provided until revenues are recognized for financial reporting purposes."

21 **Q. Methodological inferiority aside, has Mr. Schooley correctly carried out his**

22 **ISWC analysis?**

23 A. If the Commission were to consider the ISWC method, then certain aspects of

1 Mr. Schooley's Exhibit No.___(TES-7) must be corrected. I have outlined the
2 needed corrections in my Exhibit No.___(PMW-9). The corrections identified are
3 as follows:

4 o The balance for Account 216 included in Line 2, Common Equity,
5 is different by $24 million.

6 o Line 5, Mr. Schooley should include Accounts Receivable offset
7 146 and Accounts Payable to Associated Companies 234. The net
8 result is that Line 5 is understated by $12.5 million.

9 o Impacts associated with certain Federal Accounting Standards
10 rules should be excluded from the calculation of cash working
11 capital. Specifically, any impacts from FAS 87/88, FAS 109, and
12 FAS 133 should be excluded. Mr. Schooley missed an additional
13 $11.6 million in FAS 87/88 (line 38) and mistakenly included $2.2
14 million related to BPA balancing activity as part of FAS 133 (line
15 40). Mr. Schooley then adds these items as part of Total Operating
16 Investment including the effects of 175 and 244 which are non-
17 cash FAS 133 mark-to-market measurements and should not be
18 included. The net result is that line 41, Total Other Regulatory
19 Assets, is understated by $9.6 million.

20 o Mr. Schooley departs from his ISWC methodology as previously
21 presented in Docket No. UE-032065 by including accounts in that
22 calculation that he did not include before and presenting no reason
23 for their inclusion in this case. These accounts include 182.2

1 Unrecovered Plant / Regulatory Study Costs (line 70), 183
2 Preliminary Survey & Investigations (line 78), 136 Temporary
3 Cash Investments (line 87), and 132-134 Other Investments &
4 Special Funds (line 89). These items together result in average
5 operating investment being overstated by $100.2 million.

6 - Lastly, there is a sign error on line 91, Account 252, in which the
7 $6,000 total should be negative so that it is appropriately offset by
8 the $6,000 in the Operating Investment section (line 54). This
9 results in average operating investment being overstated by
10 $6,000.

11 The net effect of correcting his calculation is to convert the ISWC from a
12 net negative $16.1 million to a net positive $84.9 million investor supplied
13 working capital.

14 **Q. Does the Company agree with the other Working Capital adjustments**
15 **proposed by Mr. Schooley?**

16 A. No. Based on the errors highlighted above, Mr. Schooley erroneously concluded
17 that because the Company's ISWC was negative, there was no need to include
18 prepayments, fuel stock, material and supplies, and working capital. Based on my
19 Exhibit No.___(PMW-9) and the net positive balance of Investor Supplied
20 Working Capital, the amounts he is contesting are part of total working capital
21 and are properly included in rate base. As stated by Mr. Hahne in *Accounting for*
22 *Public Utilities:*

23 "[V]arious other requirements for cash must be added and amounts not
24 supplied by investors… must be deducted. These additions include cash

1 balances, prepayments, materials and supplies, and fuel stock. Deductions
2 include customer advances and contributions in aid of construction."
3
4 Mr. Hahne further explains that:

5 "For rate making purposes, working capital is not a measure of liquidity at
6 a point in time, but the *average* amount of investment required of
7 investors on a *continuing* basis over and above that invested in plant and
8 other specified rate base items. In general the components are: 1) fuel
9 inventory, 2) materials and supplies inventories, 3) prepayments, and 4)
10 cash working capital."
11
12 The Company has included these additions and deductions in its rate base,
13 including the cash working capital balance, consistent with its approach in Docket
14 No. UE-032065 and the definition of working capital.

15 **Q. Please summarize your position.**

16 A. A Lead Lag study is widely recognized as the most accurate method of
17 calculating Cash Working Capital. The Company stands behind its use of its
18 most recent Lead Lag study. If the Commission were to consider adopting Staff's
19 recommendation, certain assumptions and conclusions in Staff's calculation must
20 be corrected as shown in my exhibit.

21 **Major Plant Additions**

22 **Q. Please respond to Mr. Effron's Adjustment to adjust forward the**
23 **accumulated depreciation.**

24 A. This adjustment is not necessary and is inconsistent with the Production Factor
25 methodology utilized by the Commission. With the Company's acceptance of
26 Mr. Schooley's Production Factor on Rate Base Adjustment, the Company is
27 accurately modeling the Production as it relates to Net Power Costs and
28 Production Rate Base and Expense. In that adjustment, production-related rate

1 base and expenses are adjusted forward to the rate effective period and then
2 scaled back in the same manner as variable power costs. This is the proper way to
3 model changes to production costs after the test year. Mr. Effron's methodology
4 would produce a mismatch between production-related rate base expenses, on the
5 one hand, and variable power costs, on the other.

6 **Miscellaneous Deferred Debits**

7 **Q. How do you respond to Mr. Effron's proposal to eliminate all miscellaneous**
8 **deferred debits from rate base?**

9 A. Mr. Effron proposes reducing the Company's revenue requirement by
10 approximately $2.7 million. The Company agrees with the major part of this
11 adjustment, in which Mr. Effron proposes a similar adjustment to Mr. Schooley's
12 removal of the regulatory asset and expense related to the transition plan. This
13 reduces revenue requirement by approximately $2 million.

14 In addition, Mr. Effron would remove the Deferred Environmental
15 Remediation costs, also as recommended by Mr. Schooley. As described
16 previously, Mr. Schooley's adjustment is offset when combined with the
17 elimination of the Company's Environmental Settlement adjustment and has a
18 negligible effect on the Company's revenue requirement.

19 In addition, Mr. Effron proposes eliminating the deferred costs associated
20 with the Trail Mountain Mine. Mr. Schooley has proposed an adjustment larger
21 than that of Mr. Effron's, which reduces revenue requirement by $192,000. The
22 Company agrees with Mr. Schooley's methodology.

23 The Company does not agree with Mr. Effron's rationale for excluding the

1 rest of the deferred debits. Mr. Effron excludes them because he claims that prior
2 authorization from the Commission is necessary to include them in rates. In
3 doing so, he refers to the Company's response to Public Counsel Data Request
4 No. 37. However as the Company responded in response to WUTC Staff Data
5 Request 227:

6 "With regard to Miscellaneous Deferred Debits, no specific
7 deferred accounting authorization exists or is needed. The items
8 included in them are "unusual or extraordinary expenses, not
9 included in other accounts, which are in the process of
10 amortization" as approved by FERC."
11

12 **Acquisition Adjustments**

13 **Q. Please discuss the Electric Plant Acquisition Adjustments included in Mr.**
14 **Schooley's and Mr. Effron's testimony.**

15 A. Three Acquisition Adjustments are included in this case. Mr. Effron recommends
16 that all three should be disallowed. The vast majority of the total adjustment
17 (92%) is the Yampa Adjustment. Mr. Schooley recommends inclusion of this
18 adjustment in rate base since the Company received accounting treatment for the
19 acquisition adjustment in 1992. In addition, the Joint Report filed in compliance
20 with the Third Supplemental Order in Docket No. UE-991832 found that the
21 acquisition of the Craig and Hayden plants – to which this adjustment relates –
22 was prudent. Since that time, the Commission has not had the chance to
23 explicitly allow ratemaking treatment on this issue because both of the
24 Company's last two rate cases were resolved through settlement without
25 discussion of this issue. However, in neither case was the Yampa Acquisition
26 Adjustment disallowed. The Company asks for explicit recognition of the Yampa

1 Acquisition Adjustment in this case because, as determined in the Joint Report,
2 the acquisition of these resources was prudent and payment of the acquisition
3 adjustment was warranted.
4 The two other Acquisition Adjustments are relatively minor. The first is
5 related to the Wyodak Steam plant and the second is for a transmission line. The
6 rate base related to these adjustments is $530,000 and $101,000, respectively, and
7 the Company asks for ratemaking treatment of these Acquisition Adjustments in
8 this proceeding.
9 **Property Tax Expense**
10 **Q. Which of the adjustments of Mr. Kermode do you address?**
11 A. I address Mr. Kermode's adjustment, Adjustment 7.2, Property Taxes, which
12 disallows a portion of property taxes because they are "based upon management's
13 judgment." Although the $1,215,888 figure identified in support of Adjustment
14 7.2-Property Taxes is influenced by professional judgment, an upward adjustment
15 to the Company's property tax expense is warranted when proper consideration is
16 given to the increase in utility property that occurred between tax years 2004 and
17 2005.
18 A utility's property tax burden is a function of two factors: 1)
19 jurisdictionally specific property tax rates and 2) assessed values established on a
20 centralized basis by state taxing authorities. The central assessment process has
21 been adopted by nearly all states as a way to avoid the conflict and inequity that
22 would arise if local county assessors were left to independently value utility
23 property which spans multiple counties or states.

1 State appraisers typically employ two methods when valuing utility
2 property: a cost approach, which focuses on the original cost of utility plant
3 less book depreciation and amortization reserves (net utility plant), and an
4 income approach, which produces an estimate of market value by capitalizing
5 each company's net utility operating income. Each year's assessed value
6 results from assigning weight, often by use of percentages, to the value
7 estimate derived from each approach. Many states assign 50 percent or more
8 weight to the cost approach.
9 As indicated above, the cost approach focuses on the Company's
10 investment in net utility plant on January 1st of each tax year. The relevant
11 amounts, as shown below for tax years beginning January 1, 2004 and 2005,
12 are reported on Line 6, page 110 of PacifiCorp's 2004 FERC Form 1.
13

Net Utility Plant at 12/31/03	$ 8,120,324,805
Net Utility Plant at 12/31/04	$ 8,450,786,258

14 The $67,666,699 in property tax expense accrued during the twelve
15 months ending September 30, 2004 is largely a function of the December 31,
16 2003 utility plant balance of $8,120,234,805. Given the $330,551,453
17 (8,450,786,258 - 8,120,324,805) increase between December 31, 2003 and
18 December 31, 2004 in the level of reportable and thus taxable property,
19 property tax expense would, absent other considerations, be expected to rise
20 by $3,966,617 (330,551,453 times a 1.2% composite property tax rate).
21 While there is little question that the cost approach for the 2005 tax
22 year will capture the $330 million increase in utility plant, the Company

1 believes that the cost approach will receive no more that 50 percent weight.
2 This assumption produces an increase in property tax of $1,983,308
3 (330,551,453 x 1.2% composite property tax rate x 50%). The Company's
4 more conservative increase of $1,215,888 is well below that figure and should
5 therefore be allowed.

6 **Income Tax**

7 **Q. Please address Mr. Effron's two proposed adjustments to Income Taxes.**

8 A. His first adjustment relates to "Interests & Dividends AFUDC-Equity." The
9 Company explained in responses to a Public Counsel data request that this item
10 had no effect on Washington taxable income. This is because the amount of
11 $611,689 shown as part of the current state and federal income tax calculation
12 section of the results shown on Line 1375 on Page 2.22 of Tab 2 in Exhibit
13 No.___(PMW-3) is accompanied by a Schedule M deduction of $679,000 (shown
14 on page 3 of Tab B6 of the same Exhibit). These two amounts offset each other
15 and must be considered in tandem. Mr. Effron's adjustment would remove only
16 the first of these amounts without considering the second amount, and should be
17 rejected.

18 **Q. Is Mr. Effron correct to use the 4.54 percent combined effective tax rate to**
19 **calculate Washington's share of state income tax expense?**

20 A. No. The 4.54 percent combined effective rate is a rate that is used to estimate
21 total state income tax expense when the individual state taxable income is not
22 measurable and is used when calculating taxes on individual adjustments. The
23 Company's methodology uses a more direct approach.

1 To calculate state income taxes for regulatory purposes, each state's
2 statutory rate is first applied to the state's income amount to generate a Total
3 Company state income tax number. This Total Company number is then
4 allocated among the states based upon each state's respective "Income before
5 Taxes." In the same fashion, Washington Revenue tax rate is applied to the
6 Washington Revenue only and then shared with the other jurisdictions.

7 **ScottishPower UK (SPUK) Cross-Charge**

8 **Q. Do you agree with Mr. Selecky's proposal to disallow a portion of the SPUK**
9 **cross-charge?**

10 A. No, we believe the methodology sponsored by Mr. Schooley is more appropriate,
11 and we have accepted that adjustment, which makes consideration of Mr.
12 Selecky's adjustment unnecessary.

13 **Capital Stock Expense**

14 **Q. Please respond to Mr. Ward's & Mr. Effron's proposal to remove Capital**
15 **Stock Expense from the revenue requirement.**

16 A. The Company does not agree with their proposed adjustments to remove capital
17 stock expense from the revenue requirement. Staff witness Ward does not say the
18 cost should be disallowed; rather, he says this cost category should not be
19 included in revenue requirement as an operating expense. Public Counsel witness
20 Effron, for his part, acknowledges that certain additional capital stock expenses
21 associated with the issuance of common equity will be incurred. These additional
22 costs, such as legal, accounting, and underwriting fees are elements of flotation
23 costs which should be recovered as a legitimate part of the cost of issuing

1 common equity such that the actual proceeds of the issuer of the common stock
2 will be whole with the price of the stock to the public.

3 **Q. How have flotation costs typically been recovered?**

4 A. Capital stock expense in FERC account 214 represents the cost of acquiring
5 equity capital. The common treatment is to add flotation cost to the allowed
6 return on common equity. In Docket No. UE-991606, for example, the
7 Commission said "…a 25 basis point markup for flotation costs should be made"
8 to the allowed return on common equity.

9 **Q. Please explain why the Company prefers its proposed method of amortizing**
10 **the capital stock expense.**

11 A. The Company proposes that the capital stock expense be amortized over 20 years.
12 The amount that has been accumulating in account 214 is $41,281,084, as shown
13 in FERC Form 1. Amortizing this balance over 20 years is a reasonable method
14 to recover the costs and has a lower revenue requirement than including the cost
15 as part of the return on equity in perpetuity. Just as paying off a home mortgage
16 in twenty years is less expensive than repaying a mortgage over thirty years,
17 amortizing capital stock expense over a specified period is less expensive than
18 allowing recovery in perpetuity.

19 On the other hand, if the Commission prefers to include capital stock
20 expense with the return on common equity, that would result in adding 13 basis
21 points to the 11.125% requested return on equity, producing an updated return on
22 equity of 11.255%.

1 **Q. Do you agree with Mr. Ward's claim that permitting recovery of capital**
2 **stock expenses constitutes retroactive ratemaking?**
3 A. No. Capital stock expense is akin to bond issuance expense. Both represent the
4 cost of obtaining funds to finance the utility rate base. Bond issuance expenses,
5 even though they were incurred many years ago, are amortized over the life of the
6 bond. The amortization of bond issuance expenses is routinely included as part of
7 the utility revenue requirement, without raising false claims of retroactive
8 ratemaking.
9 **Q. Please summarize your position on this adjustment.**
10 A. Capital stock expense in FERC account 214 represents the cost of acquiring
11 equity capital. A twenty year amortization period for the recovery of capital stock
12 expense is reasonable.
13 **RTO-Related costs**
14 **Q. Please describe the issue with respect to recovery of RTO-related costs.**
15 A. Mr. Ward recommends that the Washington-allocated amount of the Company's
16 total expenditures related to development of an RTO included in this proceeding
17 be removed for retail ratemaking purposes. Mr. Selecky also testified that
18 expenses related to the RTO development should be excluded.
19 **Q. What reasons did Mr. Ward and Mr. Selecky give for their**
20 **recommendations?**
21 A. Mr. Ward stated the RTO-related expenses should be disallowed because "the
22 Company has not demonstrated that Washington retail customers have benefited
23 from these efforts, or that the expenses are in the best interest of Washington

1 ratepayers." Mr. Selecky makes a slightly different point, stating that the
2 expenses should be excluded because they are "neither used nor useful during the
3 test year."

4 **Q. Do you agree with Mr. Ward's characterization of the benefits of RTO**
5 **project expenses?**

6 A. No. Because we have been engaged since the early 1990s in various forms of
7 joint planning or restructuring of the transmission grid, and anticipate continued
8 efforts, I do not agree with Mr. Ward that Washington retail customers have not
9 benefited from these efforts. Retail electric customers could not be served
10 without transmission services. Not only is transmission necessary to deliver
11 power from generating resources to the Company's distribution system; it is also
12 used to market surplus energy for the benefit of retail customers, to acquire
13 alternative supplies during outages, and to displace expensive resources when
14 market conditions allow. Our retail customers directly benefit from the
15 Company's transmission services and, consequently, from the ordinary,
16 necessary, and reasonable expenditures that are associated with the provision of
17 such services. RTO-specific development efforts have been ongoing since late
18 1999 in response to FERC's guidance in Order 2000. This Commission has
19 previously recognized the diligence and good faith with which the Company has
20 pursued these efforts.

21 **Q. Do you expect RTO expenses to continue into the foreseeable future at a level**
22 **comparable to the test year expense?**

23 A. Yes. We remain optimistic that the region will support some form of regional

1 transmission organization, so the level of the Company's expenses in the future
2 should be comparable. Even if Grid West ultimately fails to receive the support
3 of the region, the Pacific Northwest must continue to work jointly to plan a
4 transmission system to accommodate the growing importance of renewables,
5 continued load growth (including our Washington service territory), and
6 increasing congestion on the grid. That work will be done, and is being done, by
7 the same people and resources currently deployed in support of an RTO.

8 **Q. What is your response to Mr. Selecky's statement that the expenses should**
9 **be excluded because the RTO is not yet operating and the expenses are**
10 **"neither used nor useful" during the test year?**

11 A. I disagree that the expenditures are not useful. In order to continue operations as
12 a transmission provider, the Company needs to comply with current FERC
13 requirements. And again, as explained in my answer to the previous question, we
14 must commit to this type of work and this level of resources if the region is to
15 maintain the high reliability and flexibility that are the hallmarks of the Northwest
16 system.

17 **Q. Mr. Selecky also recommends that the Company's operating expenses**
18 **relevant to RTO development should be deferred and reviewed for prudence**
19 **by the Commission at a later time. Do you agree?**

20 A. No. As ongoing regulatory expenses, the Company's operating expenses for its
21 RTO project are properly subject to review and inclusion in rates now because
22 they are ordinary, necessary, and reasonable.

1 **WAPA Contract**

2 **Q. What is the issue regarding WAPA wheeling in this case?**

3 A. Mr. Falkenberg proposes to impute revenue to a contract under which PacifiCorp
4 provides wheeling to Western Area Power Administration (WAPA) customers.

5 **Q. Does the WAPA wheeling contract provide benefits to Washington**
6 **customers?**

7 A. Yes. The WAPA contract currently provides a revenue source greater than the
8 cost of owning and operating a pro-rated share of the specific facilities used as
9 they were contemplated in 1962. Total actual wheeling revenues from the WAPA
10 contract far exceed the operating and maintenance cost attributable to the WAPA
11 wheel.

12 **Q. How does the service available to WAPA under the contract differ from the**
13 **service provided to PacifiCorp's transmission customers paying for service**
14 **based on average embedded transmission pricing?**

15 A. WAPA is limited to the use of only those points of interconnection and points of
16 delivery listed in the contract. WAPA may not substitute alternate resources or
17 deliver its energy to alternate points of delivery. WAPA may not re-market any
18 of its transmission rights to any party. Also, PacifiCorp has no planning or
19 construction requirements resulting from load growth occurring within the load
20 serving systems of WAPA's customers served from PacifiCorp under the WAPA
21 contract. These circumstances need to be taken into account in determining
22 whether PacifiCorp's charges to WAPA under the WAPA contract are just and
23 reasonable.

1 **Q. Does the WAPA contract provide any other benefits to Washington**
2 **customers?**
3 A. Yes. The lack of flexibility afforded to WAPA under the WAPA contract results
4 in short term transmission marketing opportunities for PacifiCorp. PacifiCorp
5 Transmission Systems actively markets available transmission scheduling rights
6 over its Open Access Same-time Information System (OASIS). These available
7 transmission rights can be from un-committed transmission capacity or from
8 transmission capacity committed to others that remains un-scheduled (as is the
9 WAPA contract transmission capacity throughout the year). These short-term
10 transmission sales appear as revenue credits against the total system cost of
11 service allocation to Washington retail customers, thus reducing rates. The total
12 amount of short-term transmission revenue credits allocated to Washington in this
13 proceeding is $950,741 based on the product of total short-term revenues
14 ($11,272,851) and Washington's allocation factor (8.4339%).
15 **Q. Do you agree that revenue should be imputed for this 43-year old contract at**
16 **the FERC Open Access Transmission Tariff rate for firm transmission**
17 **across the entire PacifiCorp system, as Mr. Falkenberg proposes?**
18 A. No. It is not appropriate to impute revenue additions or deductions for any
19 contract 43 years after it was signed. It is not appropriate to impute higher
20 revenue for a contract just because it might be perceived by some to have prices
21 that are currently less than market price. Second, no utility regulator took
22 exception with the contract during the first 21 years. Lastly, 42 years ago
23 transmission was not marketed in a manner that provided the level of scheduling

1 and re-marketing flexibility to the customer as is the case today for those
2 transmission agreements returning an average embedded revenue. The limited
3 rights provided to the customer under the WAPA Contract would make pricing
4 and cost allocation using an average embedded method unjust and unreasonable.

5 **Q. Do you agree with Mr. Falkenberg's calculation of imputed revenue?**

6 A. No. Mr. Falkenberg's calculation is based on the assumption that the only benefit
7 Washington customers receive from the facilities used to provide firm
8 transmission service under the WAPA Contract is the level of revenue received
9 from WAPA. In fact, in addition to these revenues, a portion of the short-term
10 revenues used as credits in this proceeding would be a result of WAPA's
11 unscheduled transmission rights. Mr. Falkenberg fails to recognize the value of
12 the credit for short-term transmission service sold.

13 **Q. Is there an alternative adjustment for WAPA that could be considered?**

14 A. If the Commission determines that an adjustment is warranted, it should be
15 similar to the Colstrip #3 adjustment adopted by the Commission in Cause No. U-
16 83-57. Such an adjustment removes from revenue requirement all revenue,
17 operating expenses, and rate base associated with the plant dedicated to the
18 contract, and PacifiCorp in exchange would retain the revenues it receives. Such
19 an adjustment would likely increase revenue requirement to retail customers in
20 Washington. PacifiCorp is not currently proposing an adjustment for WAPA,
21 however. The adjustment proposed by Mr. Falkenberg is without support, and
22 should be rejected.

1 **Currant Creek**

2 **Q. Mr. Falkenberg proposes to remove Currant Creek from this filing because**
3 **it is not operational during the historic test year. Is he correct in doing this?**

4 A. No, this is not the appropriate decision point. Under the Production Factor
5 methodology, the relevant information is whether Currant Creek will be used and
6 useful during the rate effective period. Since the final phase of Currant Creek
7 will go into service in February 2006, it is appropriately modeled in the rate
8 effective period and, in common with all production-related costs in that period, is
9 then scaled back to the historic test period using the Production Factor. As for the
10 legal requirement of "used and useful," the plant will be in service at the time
11 rates in this case become effective, and thus the requirements of Washington's
12 rate base statute are fulfilled.

13 **Q. Does this conclude your rebuttal testimony?**

14 A. Yes.