Introduction

Q. Please state your name, business address and position with PacifiCorp or "the Company".

A. My name is Andrea L. Kelly. My business address is 825 NE Multnomah Street, Suite 2000, Portland, Oregon 97232. I am employed by PacifiCorp as Vice President of Regulation.

Q. Please summarize your education and business experience.

A. I hold a Bachelor's degree in Economics from the University of Vermont and an MBA in Environmental and Natural Resource Management from the University of Washington. After graduate school, I joined the Staff of the Washington Utilities and Transportation Commission (Commission). In 1995, I became employed by PacifiCorp as a Senior Pricing Analyst in the Regulation Department and advanced through positions of increasing responsibility. From 1999 through 2005, I led major strategic projects at PacifiCorp including the Multi-State Process (MSP) and the regulatory approvals for the Mid-American-PacifiCorp transaction. In March 2006, I was appointed Vice President of Regulation.

Q. Have you appeared as a witness in previous regulatory proceedings?

A. Yes, I have appeared as a witness on behalf of PacifiCorp in the states of Idaho, Oregon, Utah, Washington, and Wyoming. In addition, I sponsored testimony in various proceedings as a member of the Commission Staff.

Q. What is the purpose of your testimony?

A. My testimony provides an overview of PacifiCorp's request for an increase in base electric rates and the major factors driving the need for the rate increase. I describe the inter-jurisdictional cost allocation methodology pilot the Company is proposing to implement in this case and summarize the Company's proposed Power Cost Adjustment Mechanism (PCAM). Finally, I conclude my testimony with an introduction of the other witnesses providing testimony on behalf of PacifiCorp.

Summary of PacifiCorp's Rate Increase Request

Q. Please summarize PacifiCorp's rate increase request.

A. PacifiCorp is requesting to increase its base rates in Washington. Based on the evidence provided in Mr. Wrigley's testimony, PacifiCorp is currently earning a return on equity (ROE) in Washington of 4.54 percent for the test period. This return is less than the 10.2 percent ROE currently authorized by the Commission. An overall price increase of $23.2 million or 10.2 percent would be required to produce the authorized ROE.

PacifiCorp would agree to limit its overall price increase to a lower amount if the Commission adopts an expedited schedule for this proceeding. If a schedule is adopted that allows the Commission to issue a decision that would result in rates being effective no more than six months from the date of filing, the Company would voluntarily limit its overall price increase to $10 million or 4.4 percent. PacifiCorp is willing to limit its request in recognition of the value of having the base rate increase become effective sooner than the maximum period allowed under Washington law. PacifiCorp also recognizes that the development of an acceptable allocation method is a necessary pre-requisite for implementation of a PCAM.

Q. What are the primary factors driving the need for an overall rate increase?

A. The need for this increase is driven primarily by the increase in the power supply costs necessary to serve growing retail load requirements. Mr. Widmer's testimony shows that Washington's share of the Company's net power costs, primarily composed of fuel and purchased power costs net of wholesale energy sales revenue, has almost doubled as compared to the amount the Company was authorized to be recovered in rates in 2004. Mr. Widmer's testimony describes the basis for the increase in net power costs in more detail.

In addition to an increase in net power costs, the Company is experiencing significant upward cost pressures related to employee labor, pension and health insurance costs, hydroelectric generation relicensing costs, and investments in new plants. Even with the price increase proposed in this case, PacifiCorp's rates will remain very competitive when measured against other utilities within the state.

Q. How do the Company's prices compare with other utilities?

A. As demonstrated in the testimony of Mr. Griffith, PacifiCorp's average rate in Washington will remain low in a low-cost state.

Description of Inter-jurisdictional Cost Allocation Pilot

Q. Please describe PacifiCorp's approach to inter-jurisdictional cost allocations in this proceeding.

A. In response to the Commission's conclusion in PacifiCorp's last general rate case, Docket No. UE-050684 (2005 Rate Case), that the evidence did not support a finding that Washington customers benefited from all of the generation allocated to the state under the Revised Protocol, PacifiCorp, in consultation with key Washington stakeholders, created a West Control Area (WCA) method for allocating PacifiCorp's total Company costs to Washington. The WCA method includes only loads and resources contained within PacifiCorp's west control area for operational purposes. The west control area includes the California, Oregon and Washington loads and includes Company-owned generating resources such as the west hydroelectric resources, Hermiston, Colstrip, and Jim Bridger as well as wholesale contracts like the Bonneville Power Administration (BPA) Peak Purchase contract and the Mid-Columbia hydro contracts. Some of these generation facilities, such as Colstrip and Jim Bridger, are located outside Washington, Oregon and California, but there is adequate transmission from those resources to provide delivery to Washington customers. The WCA method isolates the costs associated with these assets, purchases and sales, and allocates to Washington a proportionate share of the costs based on Washington's relative contribution to the west control area's energy usage. For this filing, Washington's share of the west control area-related costs is approximately 22 percent. Mr. Widmer and Mr. Wrigley provide additional detail of the WCA method in their direct testimony.

Q. Does PacifiCorp believe that this allocation method will satisfy the Commission's concerns expressed in its rejection of the Revised Protocol method?

A. Yes. In its final order in the 2005 Rate Case, the Commission made three significant findings upon which the Company has directed its focus in designing the WCA method:

> "PacifiCorp has not met its burden of proof to show that resources allocated to Washington in the Revised Protocol are 'used and useful for service in this state' or that the Revised Protocol [met] statutory standards.... We interpret the phrase "used and useful for service in this state" to mean benefits to ratepayers in Washington either directly (e.g. flow of power from a resource to customers) and/or indirectly (e.g. reduction of cost to Washington customers through exchange contracts or other tangible or intangible benefits." (Docket No. UE-050684, Order 04, ¶ 50.)

> "In the final analysis, the Company failed to carry the burden it alone bears to prove that resources in its Eastern service territories, remote from Washington, provide tangible and quantifiable benefits to customers 'in this state' as required by RCW 80.04.250." (Docket No. UE-050684, Order 04, ¶ 62.)

> "[W]e expect the Company to include the full value of hydroelectric resources in the Western control area in any inter-jurisdictional cost allocation model it develops for Washington." (Docket No. UE-050684, Order 04, ¶ 70.)

I will address each of these in turn.

Q. **How can the Commission be satisfied that the resources allocated to Washington under the WCA method provide benefits to customers in Washington either directly and/or indirectly?**

A. For operational purposes, the resources are all either located within the Company's west control area or delivered to PacifiCorp's west system for subsequent delivery to the west control area or disposition if necessary due to normal and prudent balancing activities. Each control area operator is responsible for ensuring that reliable service is provided to the control area loads in accordance with the National Electricity Reliability Council (NERC) Minimum

Operating Reliability Code. The control area operator relies on all of the resources within the west control area to maintain reliability for PacifiCorp's Washington loads. The electric "boundary" (the west control area) was thus established on the basis of reliability considerations, as opposed to geographic boundaries that the control area concept does not recognize; PacifiCorp has designed, constructed, and operates the west control area as a whole rather than on a state-specific basis. As such, over the many years of holding a load service obligation in multiple western states, PacifiCorp has acquired resources and transmission rights on the basis of this system rather than on a state-specific nature. Because of this fact, and the fact that PacifiCorp holds a multitude of transmission rights in, out, and through Washington state for the purposes of balancing and maintaining the integrity of the west control area, it is PacifiCorp's view that all resources and assets acquired to date should be deemed to be prudent for the purposes of this docket (after considering as well Mr. Tallman's testimony on more recent resource acquisitions). There was very little controversy in the last case regarding these previously existing west control area resources.

Q. **How have you addressed the Commission's concerns regarding the lack of evidence of tangible and intangible benefits for assets located in the east control area?**

A. The WCA method eliminates all resources and loads in the east control area, thereby eliminating the significant source of controversy among parties from the 2005 Rate Case. As discussed by Mr. Widmer, the production cost dispatch model used for calculating net power costs has been re-designed to simulate the optimization of the west control area in isolation from the east control area.

Q. Does the WCA method capture the full value of hydroelectric resources in the west control area?

A. Yes. The WCA method first assigns all of the output and costs of the west hydroelectric resources to the west control area and then allocates approximately 22 percent of the costs to Washington. The 22 percent will change dynamically for each test period based on Washington's relative contribution to west control area energy usage.

Q. Please explain the pilot concept that PacifiCorp is proposing.

A. The Company is proposing to implement the new allocation method for a five year pilot period. During this period, PacifiCorp will use the WCA method to file rate cases, report its results of operations, file PCAM adjustments and make routine regulatory filings. It is important that the Company and parties recognize that this method may need to be refined over time, and the five-year pilot period would allow for this. For example, if this method is to be viable over the long-term, parties will need to work within the Company's Integrated Resource Planning (IRP) process to determine how new resource additions for the PacifiCorp system will be fairly evaluated for inclusion in rates in Washington.

Q. What other factors will need to be assessed during the pilot period?

A. The Company believes that the following factors should be monitored:

- Fairness to customers and the Company
- Impact on customer prices

- Compatibility with IRP and cost-effective resource acquisition
- Impact on other states
- Impact on actual system operations
- Consistency with cost-causation principles

The Company is also willing to provide ongoing reporting comparing the WCA method to other allocation methods such as the Revised Protocol if the Commission desires.

Q. What issues will need to be addressed in the IRP if the WCA method is to be viable long-term?

A. Under the WCA method, all new generation and transmission resources interconnected with the west control area, or delivered to PacifiCorp's west system, will be proportionately allocated to Washington, subject to a prudence review by the Commission. However, there may be future resource additions that are not directly interconnected with the west control area, or delivered to PacifiCorp's west system, that provide direct or indirect benefits to Washington customers. It is not in the best interest of Washington customers to preclude them from receiving the potential benefits of these yet unknown future resources if the standard articulated by the Commission can be met in a future Commission review.

Q. Are there other issues outside of the IRP that need further attention?

A. Yes. The applicability and interpretation of Washington rules and statutes will need to be clearly understood in light of the WCA method. For example, the Company will want confirmation that the requirement for filing a Request for

Proposals (RFP) would apply only in the case of an acquisition of a west control area resource. It should also be understood that a resource acquired outside of the west control area would not be precluded from inclusion in rates, so long as the Company can make the necessary showing that the resource provides direct or indirect benefits to Washington customers.

Request for Expedited Treatment

Q. What steps has PacifiCorp taken to facilitate an expedited schedule in this proceeding?

A. The current filing is based on a recent test period (the twelve months ended March 31, 2006), and the Company has restricted the number of pro forma adjustments included in the case. Only the adjustments that are applicable to the WCA method are included and allocated to Washington. Adjustments for major resource additions are excluded, with the exception of the power purchase agreement with Eurus Oregon Wind Power Development LLC (Eurus), the purchase of Leaning Juniper Wind Power, LLC, (Leaning Juniper), and the Grant County power purchase agreement. Adjustments for pro forma wages and benefits, as well as O&M expenses, are excluded. Given inflationary pressures on wages and salaries, the exclusion of known pro forma changes to wages and benefits implicitly incorporates a two to three percent productivity stretch target for the Company. The impact of excluding adjustments that have been included in past general rate cases is summarized in Mr. Wrigley's testimony. In addition, in the interest of minimizing the number of contested issues in this case, the Company has chosen not to re-litigate issues decided by the Commission in the

2005 Rate Case.

Q. Please identify the issues resolved by the Commission in the 2005 Rate Case that PacifiCorp is not re-litigating in this filing.

A. First, the Company has accepted the Commission-authorized cost of equity and capital structure. As described in Mr. Williams' testimony, the Company has updated its cost of capital to reflect a decrease in the cost of long-term debt and preferred equity, which reduces the Company's authorized rate of return. Second, the Company has implemented the stipulated interim methodology for temperature normalization. Third, the Company has removed all miscellaneous deferred debits that had not been authorized by the Commission. Finally, the Company has followed the Commission-ordered accounting for the Malin-Midpoint safe harbor lease.

Q. Are there any additional agreed-upon items from the 2005 Rate Case that the Company is including in this case?

A. Yes. Mr. Griffith's testimony describes the results of an updated Cost of Service study which produces similar results to the Cost of Service study filed in the 2005 Rate Case. Due to these similar results, the Company is proposing to use the rate spread methodology agreed upon by all parties from the 2005 Rate Case.

Q. How has the Company accounted for the change in ownership from ScottishPower to MidAmerican Energy Holdings Company (MEHC) in this filing?

A. The Company incorporated adjustments related to the change in ownership in two categories: (1) implementation of transaction commitments, and (2) inclusion of known and measurable transition benefits net of an amortization of transition costs. The adjustments result in a $1.8 million reduction in revenue requirement. Detailed explanations of these adjustments are discussed in Mr. Wrigley's testimony.

Power Cost Adjustment Mechanism

Q. Is the company proposing any regulatory recovery mechanisms as part of this filing?

A. Yes. PacifiCorp is proposing to implement a Power Cost Adjustment Mechanism (PCAM) to deal with volatility in power costs. Based on discussions with parties, PacifiCorp has designed its proposal to be similar to Avista's Energy Recovery Mechanism approved by the Commission. The mechanism is discussed in detail in Mr. Widmer's direct testimony.

Q. Is the company's PCAM proposal consistent with the guidance the Commission provided in the 2005 Rate Case?

A. Yes. As discussed by Mr. Widmer, the Company is proposing both a deadband and sharing bands consistent with the guidance provided by the Commission. The Company is also excluding new resource additions that exceed a specified threshold for size and term.

Q. Has the Company addressed the impact of the PCAM on PacifiCorp's cost of capital?

A. Not in this filing. Given that the Company is not re-litigating the cost of equity in this proceeding, the Company has not assessed the potential impact. Indeed, until the mechanism is approved by the Commission, it would be speculative to do so.

In addition, the potential risk-reducing aspects of a PCAM should be evaluated in concert with the potential risk-increasing aspects of a Washington-only inter-jurisdictional cost allocation method. The potential impact of these risks is best addressed in a rate case filed during or after the five-year pilot period.

Rate Increase Mitigation

Q. What action is the Company taking to mitigate the effects of the proposed rate increase for customers?

A. By limiting the amount requested in the filing, the Company is in effect minimizing the impact of the increase on customers. In addition, Mr. Griffith presents the Company's proposal regarding an increase in low-income assistance.

Introduction of Witnesses

Q. Please list the Company witnesses and provide a brief description of their testimony.

A. **Bruce N. Williams**, Treasurer, discusses changes in rates that result in reductions in PacifiCorp's cost of debt and preferred stock. Mr. Williams also presents studies that demonstrate PacifiCorp's compliance with the Company's and MEHC's commitment from Docket No. UE-051090 (Commitment 37).

Mark T. Widmer, Director, Net Power Costs, presents the net power costs for the test period, and describes the Company's production cost model including a summary of model changes necessary to implement the WCA method.

Mr. Widmer also provides a detailed description of the company's proposed PCAM.

Mark R. Tallman, Managing Director of Renewable Resource Development, describes the Company's recent supply-side resource acquisitions for the west control area since 2000. These include the power purchase agreement with Eurus, the purchase of Leaning Juniper, and the Grant County power purchase agreement.

Paul M. Wrigley, Director of Regulatory Strategy and MSP, presents the Company's overall revenue requirement based on the test period (twelve months ending March 31, 2006), with known and measurable adjustments through the rate-effective period. Mr. Wrigley presents the normalizing adjustments to actual test period results related to revenue, operation and maintenance expense, net power costs, depreciation and amortization, taxes and rate base. Mr. Wrigley also describes the WCA method that was used to allocate the revenue requirement to Washington.

William R. Griffith, Director, Pricing, Cost of Service and Regulatory Operations, presents the Company's cost of service study, proposed rate spread and changes in price design for the affected rate schedules. Mr. Griffith also presents the company's proposed rate design for the PCAM.

Conclusion

Q. Does this conclude your direct testimony?

A. Yes.