Exhibit No.___(APB-2)
Docket No. UE-032065
Witness: Alan P. Buckley

WUTC Staff Review of Protocol

- All generating resources will be assigned to one of four categories: 1) Seasonal resources, 2) Regional Resources, 3) State Resources, and 4) System Resources. A general description for each of these categories is contained in Exhibit No.___(ALK-1T), pages 8 though 16. More details of the actual resources in each category is provided in Mr. Duvall's testimony.

- Seasonal Resources are simply defined as: 1) any simple-cycle combustion turbine owned or leased by the Company, 2) seasonal contracts, and 3) the combination of Cholla Unit IV and the APS Exchange.

- Unlike other resources, the simple-cycle turbines are classified as 100 percent demand related. The fixed costs will be allocated using a generation-weighted coincident peak method. This method adjusts the monthly coincident peak measurements by the monthly portion of the total annual energy generated by the particular Season Resource being allocated. In this manner monthly weighted generation demand related costs of a Seasonal Resource is then allocated among the States based on each States contribution to monthly coincident peaks. The specific methodology to calculate the allocation factor is described on page 10 and 11 of Exhibit No.___(DLT-1T). The Company claims this method captures the cost causation aspect of Seasonal Resources being used at certain times of the year.

- Fuel and energy related costs are allocated using weighted monthly energy use, where similar so demand related costs, each State's energy use is weighted by that month's portion of annual energy for the particular resource.

- ASeason Contracts are to be classified as being 75 percent demand and 25 percent energy related and allocated to the States on a weighted month basis according to their monthly delivered megawatt hours.

- The Cholla Unit IV plant is considered a Seasonal Resource. In spite the plant operating all year, the Company is proposing to treat it as a winter Seasonal Resource due to a substantial portion of the summer output being delivered to Arizona Public Service Company. An equivalent amount of capacity and energy is returned to Pacificorp during the winter months.

- The Company recognizes that the Cholla plant is actually a baseload plant and classifies the fixed costs as being 75 percent demand- and 25 percent energy-related. A weighting method, similar to that used for simple-cycle turbines, is used for both the demand and energy components of plant costs with an adjustment for the megawatt hours delivered to and received from APS. The demand and energy costs are assigned to months based on monthly megawatt hours dispatched from Cholla plus megawatts received from APS less MegaWatts hours delivered to APS.

The result is that the majority of Cholla costs get allocated to the winter months.

- Other resources are categorized as Seasonal Resources in the Protocol
- The Company owns or leases eight simple cycle turbines – three as the Gadsby site and five at West Valley. The Company has three existing long-term seasonal contracts (for heavy load hours, June through September), with a fourth contract identified in the latest IRP.

- Both of the simple-cycle turbine site locations are in the Company's Eastern Control Area. The energy from the three existing contracts, as well as the specifically identified planned contract is or is to be delivered to points within the Company's Eastern Control Area. The energy from Cholla is delivered into the Eastern Control Area.

- Washington will be allocated a share of both the demand and energy related costs associated with each of these resources and contracts.

- The Company has identified three types of what the Protocol calls Regional Resources. These are the Hydro Endowment, the Coal Endowment, and what is called the First Major New Coal Resource. The Company claims that this classification of resources is driven by state or regional energy policy preferences and is for allocation purposes only.

- The costs are to be assigned to two or more states based on policy preferences and then allocated between those states on a dynamic basis. The dynamic allocation to the assigned states uses the same methods that apply to System Resources – using a 75 percent demand classification and 25 percent energy. The demand related portion of the costs is allocated is calculated using a 12 CP methodology, but only based on the loads of those jurisdictions assigned the resource. The same holds true for the energy related portion of the allocator.

- In describing the basis for the Hydro Endowment, the Company claims that the endowment derives from individual State policy initiatives recognizing the location of the generation and fish mitigation issues, as well as a belief by the former Pacific Power jurisdictions that an entitlement to these low cost resources exists.

- The Hydro Endowment, as defined in the Protocol, includes what is called the "Hydro-Electric Resources" or 1) the Company-owned hydro-electric plants located in Oregon, Washington, or California, 2) the existing Mid-Columbia Hydro Contracts, and 3) Contracts entered into by Pacificorp to directly amend or replace the Mid-Columbia Hydro Contracts. The later item recognizes that several of the Mid-Columbia contracts will expire in the coming years and that extensions or successor contracts are expected. Also, as a point of clarification, the Hydro-Electric Resources do not include the various smaller hydro-electric facilities in the other States.

- The treatment of a hydro endowment in the Protocol is different than under the Modified Accord" method. In the Modified Accord methodology the Mid-Columbia contracts were not included as part of any hydro-endowment. Also, under the Modified Accord all States were allocated a portion of the fixed-costs associated with the Hydro-Electric Resources and the Northwest states receives a credit to their allocation of fuel costs. The Protocol directly assigns all costs of the Hydro-Electric Resources to the Hydro Endowment participants.

- The basis of the Coal Endowment is simply a tool to "balance" the assignment of pre-merger resources on both a capacity and energy basis. The Company claims that the Hydro-Endowment requires an economic offset to the other States in order to avoid what it calls "unreasonable cost shifts". According to the Company this adjustment can be carried out by either decreasing the assignment of all other resources to the Hydro-Endowment participants or by directly assigning like amount of pre-merger resources to the other jurisdictions. The Company chose the later method because the use of a Hydro-Endowment alone would result in a smaller share of <u>future</u> resource costs being assigned to the Hydro-Endowment participants.

- The Huntington Generating Station, which is a low-cost resource in Utah that pre-dates the 1989 PacificPower/Utah Power merger, has been identified for inclusion in the Coal Endowment. This resource will be allocated in the same manner as the Hydro-Endowment Resources, except that they will initially be assigned to the former Utah Power jurisdictions.

- First Major New Coal Resource" as identified in the Protocol, is simply defined as new first resource to be acquired by the Company (either Company-owned or third-party contract) subsequent to January 1, 2004 that is over 300 megaWatts in size, has a life of at least 25 years, and whose primary source is coal. This carve-out apparently only applies to Oregon.

- This carve-out appears to be solely based on expressed concerns of Oregon policy makers and customer groups about supporting a major new coal plant. This Protocol feature attempts to provide some certainty to the Company as to the recoverability or not of costs associated with a new coal plant by Oregon. The Company claims that it is fair to customers in the other States and to the Company for Oregon to face a decision before the resource is committed to and before its actual costs are known. Ms. Kelly describes the process and forum for resolving the issue of whether Oregon will participate in Exhibit No.___(ALK-1T), page 13.

- Protocol does not provide for an explicit opportunity for the other States to opt out of participating in a major new coal plant in the same manner as Oregon.

- State Resources consist of demand side management program and resource acquisitions resulting from portfolio standards adopted by a particular jurisdiction.

- Demand side management costs will be assigned on a situs basis to the State in which the investment is made. Benefits will ultimately be reflected in the load-based dynamic allocation factors. Any costs associated with the implementation of portfolio standards are treated slightly different. Only the costs that may be disallowed by the other jurisdictions, will be assigned situs to the state initiating the acquisitions.

- System Resources are defined as all resources not included in the other classifications. The Protocol does not identify the specific treatment for costs or benefits associated with non-generating resources such as firm purchase power or sales contracts, exchanges, or other arrangements, other than say that all fixed and variable costs and revenues associated with System Resources will be allocated as described below.

- Both costs and revenues associated with System Resources will be allocated dynamically based on each States contribution to system peak and energy requirements. Fixed costs of System Resources are classified as being 75 percent demand- and 25 percent energy-related and will be allocated using the allocation factor based on that classification. The variable and fuel costs will be allocated based on an annual energy allocation factor.

- The Company claims that certain Special Contracts with large industrial customers enable the Company to lower the total cost of operating the system. Savings are claimed from the availability of curtailment rights that support operating reserves and the delay of firm resource additions.

The Protocol addresses the issue of potential over-compensation for the claimed benefits received. The individual States may have concerns regarding the subsidization of industrial customers for economic development purposes by another State.

- Recognizing that States should be free to use electric rates as a means of subsidizing local economic development, the Protocol attempts to insure that the costs of that decision are not borne by customers in other States. Unfortunately, this treatment is not easily understood. The Protocol begins by treating the costs of serving contract customer loads and their revenues the same manner as any other retail customer. It is then proposed that any payments made, or discounts received, for special attributes will be treated a System resource acquisition and included in the purchased power costs allocated among all States. Finally, if a buy-through option is provided with economic curtailment, the associated cost and revenues will be assigned situs to the host jurisdiction.

- In regards to Special Contracts the Protocol states that: "The Commission with jurisdiction over a Special Contract will make a determination of the fair market value of any Customer Ancillary Service Contract attributes of a Special Contract." (Exhibit No.___(ALK-2), p. 7) Company witness Mr. Taylor appears to equate the pricing of Customer Ancillary Service Contract attributes with the establishment of retail tariff prices, claiming that Commissions can consider other public policy preferences, in addition to costs, when setting retail prices.

- The Protocol assumes that the host jurisdiction has sole authority to determine a fair market value for any service and that the other jurisdictions are obligated to pay those costs. Per the Protocol, no opportunity, outside the proposed MSP Standing Committee, exists for States to challenge the over-compensation of services obtained through Special Contracts.

- As with System Resources, transmission assets and firm wheeling expenses are first classified as 75 percent demand- and 25 percent energy-related and then allocated to the jurisdictions based on the system generation allocator. Non-firm wheeling expense and revenues are 100 percent classified as energy-related and allocated among the States based on energy use.

- The Protocol provides that charges from the RTO would be allocated among the States based on billing determines relied upon by the FERC in setting RTO rates. The Protocol addresses the potential refunctionalization of transmission, generation, or distribution assets, presumably through FERC action related to RTO approval. Under the Protocol, the allocation of costs will then be consistent with the new function of those assets.

- Distribution costs are all directly assigned to individual States. This represents no change from existing methodologies that have been used by the Company.

- The Protocol addresses the allocation of gains or losses from the sale of resources or transmission assets, the implementation of direct access programs, and the loss or increase in load. Gains or losses generally will be allocated among the States based on the factors used to allocate the fixed costs of the asset at the time of its sale. Resources that are "freed-up" due to direct access programs are treated differently. Individual States are left to decide how a State's share of any gain or loss will be allocated to customers and shareholders.

- Without having to specifically define potential restructuring processes in each State, the Protocol attempts to address two broad issues: 1) the inter-jurisdictional entitlement and responsibility associated with resources freed up by direct access programs, and 2) the evaluation of these resources for assessing stranded costs or benefits. The Protocol treatment is, however, in large part responding to Direct Access in Oregon and the administrative rules implementing SB 1149. This entire issue is the subject of extensive testimony by Ms. Kelly in Exhibit No.___(ALK-1T), p. 18 through 25.

- The Company claims that a key element underlying direct access in Oregon is the idea that direct access customers should receive the benefits of or bear the costs associated with resources made unnecessary the result of implementing direct access. Benefits are claimed to exist if the resource is cheaper than market prices. Stranded costs would exist if the resources are more expensive than market prices. The Protocol actually defines "Freed-up Resources" as a category of resources. This policy becomes an

issue because, in a multi-state utility such as Pacificorp, there may arise different claims as to the treatment of such resources. The Company's proposal attempts "wall-off" the actions of one State against the others.

- Protocol provides that any load associated with direct access customers will continue to be treated as retail load in the respective State for purposes of calculating all load-based dynamic allocators related to resource costs. Second, the Protocol provides that the sale of "Freed-up Resources" will be separately tracked and treated as a State Resource, which is then assigned situs to the appropriate State. Thirdly, losses or gains on wholesale market purchases made by the Company on behalf of direct access customers will also be treated as a Sate Resource and assigned on a situs basis. These provisions are designed to insure that other States will not benefit or be burdened by direct access programs of another state.

- The Company has determined that three pieces of information are necessary to determine the benefits or stranded costs associated with "Freed-Up Resources," beginning with: 1) what resources have been freed-up by direct access customers, 2) the embedded costs of those resources, and 3) the market value of the resources. The actual acquisition or calculation of this information is, however, entirely based on Oregon SB 1149 administrative rules, that contemplate the measurement of benefits or stranded costs on an ongoing valuation.

- Under "on-going evaluation," it is assumed that Oregon direct access customers were previously served from a uniform "slice" of system resources allocated to Oregon. A "Freed-Up Resource" is not, therefore, a single resource, but a proportion of the total embedded generation costs allocated to Oregon. Under "ongoing valuation", power freed-up from direct access is sold into short-term wholesale markets and the revenues compared to the embedded costs of "Freed-Up Resources" to determine benefits or stranded costs to be paid or recovered.

- The recovery of resource costs by Oregon, or any State implementing such a program, must follow the resources that being used in the ongoing valuation process. The Company states that without agreement on allocations there can be no consensus regarding the calculation of embedded costs in that process. In addition, the ongoing valuation process required the "color-coding" of short-term market sales revenues associated with the sale of power from "Freed-Up Resources". The situs assignment of these revenues is a change from the traditional treatment of such amounts.

- According to the Company, many parties believed that the ongoing valuation method was flawed and needs to be replaced by a "one-time" evaluation method. Fundamental to a one-time valuation method is the preparation, by the Company, of a "resource plan", subject to Oregon Commission approval. In that resource plan, the Company would describe all of its allocated resources and propose the following: 1) which free-up Oregon resources should be dedicated to serving residential and

small commercial customers who do not chose direct access, and 2) which freed-up Oregon resources should be sold or administratively valued and deregulated. This process would occur once, resulting in a permanent determination of benefits or stranded costs the responsibility of direct access customers. The benefits or costs associated with those freed-up resources dedicated to serving the remaining cost-of-service customers would follow those customers, while the benefits or costs associated with the sold or deregulated free-up resources would be the responsibility of Pacificorp shareholders.

- Several issues arise out of this proposal. The one-time evaluation assumed there is the ability to specifically identify a fixed share of Company resources required to serve Oregon to the degree necessary to value and perhaps sell the resources. This is not only counter to the Protocols dynamic allocation principle, but any sale would also most likely require the approval of the other states. It is also difficult to envision how a particular resource could operate in both a deregulated manner at the same time being part of cost-of-service resources for other States.

- The Company does not believe the use of a one-time valuation is imminent. Although still allowed in SB 1149 administrative rules, there has been no customers volunteering to permanently, irrevocably leaving the system, which is a necessary action for direct access customers under the one-time valuation process.

- The Protocol addresses the possibility of a one-time valuation only to the extent that Oregon's ratification of the Protocol would acknowledge that it is not entitled to a fixed share of the Company's resources, without specific concurrence of the other States. Although it appears that some form of one-time valuation may be possible using estimated dynamic quantities of freed-up resources, the most problematic issue is the ability to sell an asset without the approval of the other States.

- The Protocol specifically identifies losses or increases in loads arising from the condemnation or municipalization of Company service territory, the sale or acquisition of new service territory (less than 5 percent of system load), realignment of service territories, changes in economic conditions, or the gain or loss of large customers. To the extent that any of these events occur the Protocol calls for the gain or loss to be reflected in changes in the load-based dynamic allocation factors. For large acquisitions or mergers with another utility, the Protocol provides that allocation issues will be dealt with on a case-by-case basis as part of Commission approval process.

- The Protocol contains provisions related to sustainability and the process for amending the Protocol. Regarding sustainability, the Protocol provides that if issues of interpretation arise, there will first be an attempt to resolve them with reference to testimony offered in proceedings associated with the ratification of the Protocol and related Commission orders. The Company expresses the desire to have a full record in the proceedings explaining what the Protocol provisions intend. The Protocol also

provides for the establishment of an MSP Standing Committee consisting of one member of each Commission. Annual meetings of the MSP Standing Committee will be held together with other interested parties for the purpose of discussing inter-jurisdictional issues and to consider possible amendments to the Protocol. The MSP Standing Committee may also initiate additional studies, sub-committee, or other actions to encourage consensus among states. Amendments to the Protocol can be made if approved by all of the Commissions who originally ratified the Protocol. Interested parties will be given six months notice of intent prior to seeking amendment approval.