Exhibit ___T (TES-8T)
Dockets UE-061546/UE-060817
Witness: Thomas E. Schooley

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION Complainant, vs. PACIFICORP dba Pacific Power & Light Company, Respondent.	DOCKET UE-061546
In the Matter of the Petition of PACIFIC POWER & LIGHT COMPANY For an Accounting Order Approving Deferral of Certain Costs Related to the MidAmerican Energy Holdings Company Transition.	DOCKET UE-060817

CROSS-ANSWERING TESTIMONY OF

Thomas E. Schooley

STAFF OF WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

March 5, 2007

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I. INTRODUCTION AND SCOPE OF TESTIMONY

Q. Please state your name and for whom you are testifying.

A. My name is Thomas E. Schooley. I am testifying for Commission Staff.

Q. Are you the same Thomas E. Schooley who presented direct testimony in this docket?

A. Yes.

Q. On what issues do you offer cross-answering testimony?

A. I respond to the testimony of ICNU witness Ms. Iverson regarding the following ICNU adjustments: a) MEHC Transition Costs; b) Pension Expense; c) Incentive Compensation; and d) Health Care.[1]

I also explain the small difference between Staff's calculation and ICNU's calculation of what Staff calls Adjustment 5.5, Revised CAGW & SO Allocators.

Finally, I correct Adjustment 4.9. This correction increases Staff's proposed revenue requirement deficiency to $12,744,727 (+5.6%) from $12,251,343 (+5.4%).

[1] These adjustment names are taken from the table on page 3 of Ms. Iverson's direct testimony.

II. DISCUSSION

A. MEHC Transition Costs

1. *ICNU's Adjustment for Transition Costs*

Q. What does ICNU propose for the ratemaking treatment of transition costs?

A. ICNU proposes to disallow all the transition costs PacifiCorp incurred. This includes the severance expense PacifiCorp booked in the test year, the severance package expenses PacifiCorp will incur going forward, and the expense the Company incurred to change its fiscal year.

Q. How does ICNU treat the wage savings of the dismissed employees?

A. ICNU proposes to remove the test year loaded wages of the dismissed employees. The dollar amount ICNU removes is the amount presented in the Company's Response to ICNU Data Request 6.4. *Direct Testimony of Kathryn E. Iverson, Exhibit ___ (KEI-1CT) at 5.* This data request response contains more current data than was available to PacifiCorp when it filed its direct case.

Q. What is the effect of ICNU's proposed ratemaking treatment of transition costs?

A. ICNU gives ratepayers 100 percent of the cost savings of PacifiCorp's employee layoffs, but makes the Company absorb 100 percent of the costs it incurred to achieve those savings.

Q. Is ICNU's proposed ratemaking treatment appropriate?

A. No. ICNU's proposal is an extreme example of taking all the benefits of a utility's cost cutting efforts, but none of the costs incurred to achieve those reduced cost levels. This violates the matching principle of accounting.

Q. Please compare the adjustments proposed by ICNU, Staff and PacifiCorp.

A. The Company and Staff both include the recovery of deferred severance expenses, though at different amounts. ICNU denies recovery of all severance expenses.

Staff and ICNU agree on the following revisions to the Company's proposal: The Commission should use updated data as of December 2006, per the Company's response to ICNU Data Request 6.4; the wage savings going forward is \$35.9 million (system); and the Commission should not allow PacifiCorp to defer expenses related to the change in fiscal years.

The Company's proposal is based on August 2006 data, which contains a lower estimate of going-forward savings, and the Company proposes to defer upwards of one million dollars (system) in fiscal-year conversion expenses.

The Company and Staff similarly exclude the test year severance expenses of $11.9 million. ICNU revises this amount to $15.3 million.

ICNU's adjustment reduces revenue requirements nearly $3 million more than the Company's filing, and about $1 million more than Staff's adjustment.

Q. You just indicated that ICNU excludes $15.3 million in transition costs. What is ICNU's basis for using the $15.3 million figure?

A. ICNU asserts that the $15.3 million figure is the correct figure, citing a PacifiCorp data request response. *Direct Testimony of Kathryn E. Iverson, Exhibit ___ (KEI-1CT) at 4, line 15, citing PacifiCorp's responses to ICNU Data Requests 3.2 and 3.4, which are in Ms. Iverson's Exhibit ___ (KEI-4).*

Q. Assuming ICNU's proposed ratemaking treatment is appropriate in theory, is $15.3 million the correct figure?

A. No. $11.9 million is the test year figure for the severance expense related to the MEHC acquisition. *Exhibit ___ (PMW-4) at Tab 8, page 8.13.1.* ICNU is wrong to assume the $15.3 million figure is the correct figure for severance costs.

Staff understands that the $15.3 million figure contains severance expenses not related to the MEHC acquisition. PacifiCorp is not requesting deferral of such expenses. Therefore, if the Commission accepts the theory of ICNU's adjustment, it should use the $11.9 million figure to calculate the adjustment.

Q. How does ICNU recommend the Commission treat PacifiCorp's accounting petition in Docket UE-060817?

A. ICNU recommends the Commission deny the petition. *Direct Testimony of Kathryn E. Iverson, Exhibit ___ (KEI-1CT) at 8.*

Q. How does ICNU justify this recommendation?

A. ICNU justifies this recommendation by comparing the one-time severance expense of $42.1 million to an annual savings of $35.9 million and concluding there is no net gain. *Id.*

Q. Is ICNU correct in comparing the $42.1 million expense figure to the $35.9 savings figure, and concluding there is no net gain?

A. No. ICNU's comparison of a one-time cost to <u>annual</u> savings is poor analysis at best or simply self-serving.

Q. Does ICNU recommend any conditions if the Commission decides to grant the accounting petition?

A. Yes. ICNU recommends the following conditions, if the Commission decides to grant the accounting petition. Staff's response follows each condition.

1. "Only severance-related costs booked by March 31, 2007, would be eligible for recovery. Computer upgrade and other non-severance costs would be excluded."

Response: Staff agrees with this condition and Staff's adjustment satisfies it.

2. "The costs will be amortized over five years beginning April 1, 2007."

Response: Staff recommends a three-year amortization period. The benefits of the reduced wage expense occasioned by the severance program exceed the amortization expense within the first three years. A five-year amortization period produces a $1.86 million revenue requirement in total, while a three-year amortization period produces a $1.61 million revenue requirement.

While the annual revenue requirement may be less per year with longer amortization periods, the revenue requirement over time is greater. Therefore, a three-year amortization is better from a ratepayer perspective.

3. "Pacific will provide a cost-benefit study in its next rate case demonstrating that its total test year labor expense plus the total unamortized balance of the transition costs is less than the labor costs and management fees prior to the MEHC acquisition.."

Response: This recommendation is unnecessary because for Washington, this docket is the "next rate case." The data in the record in this docket show the benefits of the severance programs exceed the costs over the three year amortization period.[2]

4. "Transition costs are recoverable only to the extent that customers have already received the full benefit of the $6 million in A&G savings that PacifiCorp and MEHC agreed to in the MEHC acquisition proceeding."

[2] On a Washington basis, compare Staff's proposed annual amortization expense of $637,000 to the annual savings of $2,648,000. The annual benefit is apparent. *See my Exhibit ___ (TES-5) at 1, lines 19 and 44.*

Response: This condition appears to be satisfied by the Company's Adjustment 4.9, A&G Expense Commitment, which includes the $6 million A&G savings. *See Mr. Wrigley's Exhibit ___ (PMW-4), tab 4, page 4.9.1, line entitled "MEHC Transition A&G Cap Adj."* The Commission should accept the actual, immediate reduction in revenue requirements presented in Staff's Adjustment 8.13, rather than wait for the possibility of potential future savings.

2. *Effects on Staff Adjustment 4.9, A&G Expense Commitment*

Q. Does Staff's adjustment for the MEHC Transition Savings affect Adjustment 4.9, A&G Expense Commitment?

A. Yes. In my direct testimony, I should have included the effect of certain of Staff's adjustments on Adjustment 4.9, A&G Expense Commitment. This includes the effect of Staffs' Adjustment 4.4, Out-of-Period Expenses; Adjustment 4.10, Pro forma Wages; and Adjustment 8.13, MEHC Transition Savings.

Taken together, these adjustments bring the total Company A&G expenses below the Company's commitment threshold of $222.8 million from the MEHC acquisition stipulation. Therefore, Adjustment 4.9 is unnecessary and it should be "zeroed out." This increases Staff's proposed revenue requirement deficiency to $12,744,727 (+5.6%) from $12,251,343 (+5.4%).

B. Pension Expense

Q. What does ICNU propose for the ratemaking treatment of pension costs?

A. Based on Ms. Iverson's understanding that PacifiCorp's defined benefit pension plan is changing, ICNU proposes to impute the average of the last two years' pension costs as a substitute for the test year level. *Direct Testimony of Kathryn E. Iverson, Exhibit ___ (KEI-1CT) at 9.*

Q. Is ICNU's pension adjustment an appropriate pro forma adjustment?

A. No. ICNU's adjustment is not based on any known and measurable change to the plan. While the Company's pension plan may change, there is no evidence of what the changes will be. Consequently, ICNU's adjustment is speculative, and violates the "known and measurable" test for a proper pro forma adjustment.

C. Incentive Compensation

Q. What does ICNU propose for the ratemaking treatment of incentive pay?

A. ICNU excludes 100 percent of test year executive incentive pay and 50 percent of non-executive incentive pay. *Direct Testimony of Kathryn E. Iverson, Exhibit ___ (KEI-1CT) at 10.*

Q. What rationale does ICNU offer for eliminating all executive incentive pay?

A. ICNU does not provide a rationale. ICNU simply states: "it is inappropriate to include additional compensation for PacifiCorp's top nine executives." *Direct Testimony of Kathryn E. Iverson, Exhibit ___ (KEI-1CT) at 10.*

Q. Did ICNU offer any evidence in support of this statement?

A. No.

Q. Does ICNU offer a basis for eliminating 50 percent of all non-executive incentive pay?

A. ICNU provides no firm basis for a disallowance. ICNU concludes it is not "entirely clear" that a portion of the incentives are tied to business performance. From this hazy background, ICNU conjures up an equally hazy proclamation that "it is likely that both shareholders and ratepayers may benefit from the program." *Direct Testimony of Kathryn E. Iverson, Exhibit ___ (KEI-1CT) at10-11.*

Q. Did ICNU offer any evidence in support of this rationale?

A. No.

Q. Did Staff propose an adjustment for incentive compensation in the 2005 Rate Case?

A. Yes. In the 2005 Rate Case, Staff provided detailed analysis of PacifiCorp's incentive compensation plans and proposed a disallowance based on specific aspects of those plans.

Q. Did the Commission accept Staff's adjustment in the 2005 Rate Case?

A. No. The Commission rejected Staff's adjustment, stating: "The ultimate issue is whether total compensation is reasonable and provides benefits to ratepayers…" *Docket UE-050684, Order 04 at ¶128.*

Q. Does ICNU provide any evidence that PacifiCorp's total compensation is unreasonable or provides no benefits to ratepayers?

A. No. Therefore, the Commission should reject ICNU's incentive compensation adjustment.

D. Health Care

Q. What does ICNU propose for the ratemaking treatment of medical benefits?

A. ICNU's adjustment restates the level of employee contributions to the Company's medical plan. ICNU claims the Company contributes "roughly 85 percent" of the cost of medical insurance for its employees, and thus the employees contribute 15 percent. ICNU then compares this 15 percent figure to figures contained in two surveys that suggests that employees in firms across the country contribute an average 22 percent. Therefore, ICNU concludes that PacifiCorp employees are not contributing enough. ICNU reduces the Company's medical benefits expense to reflect an employee contribution at the 22 percent level. *Direct Testimony of Kathryn E. Iverson, Exhibit ___ (KEI-1CT) at 11-12, and Exhibit ___ (KEI-13).*[3]

Q. Is ICNU's comparison valid?

A. No. ICNU should have calculated the employee contribution based on an analysis of the actual dollars employees contributed. ICNU provides no such analysis. Therefore, because ICNU has not shown that the 15 percent figure is valid, ICNU has not shown its adjustment is valid.

Q. Is the structure of the Company's medical plan inappropriate?

A. No. If anything, PacifiCorp's medical plan appears progressive because in general, lower-paid employees contribute lesser amounts, and higher-paid employees pay greater amounts. *See ICNU's Exhibit ___ (KEI-12), the Company's response to ICNU Data Request 6.3.*

Q. In sum, does Staff recommend the Commission accept any of ICNU witness Ms. Iverson's adjustments?

A. No.

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[3] ICNU does not explain all the details of the calculation in Exhibit ___ (KEI-13). The adjustment takes the current $43,851,108 figure for medical health benefits (which ICNU assumes reflects an 85 percent Company contribution - thus ICNU's assumed 15 percent employee contribution) and multiplies it by the ratio .78/.85, to derive the Company's contribution at the 78 percent level - thus reflecting ICNU's proposed 22 percent employee contribution.

E. Adjustment 5.5, Revised CAGW & SO Allocators

Q. Do ICNU and Public Counsel propose a change to the allocation of production plant fixed costs?

A. Yes. ICNU and Public Counsel witness Mr. Falkenberg presents a change to the allocation of production plant fixed costs based on a control area generation factor, CAGW. He calls this adjustment either "CAGW Allocation Factor" or "Jurisdictional Allocation Factor." *Direct Testimony of Randall J. Falkenberg, Exhibit ___ (RJF-1T) at 5, Line Item 4, and at 26.*

Q. Does Staff offer the same adjustment?

A. Yes. Staff presents the same adjustment in Staff Adjustment 5.5, Revised CAGW & SO Allocators. *Exhibit ___ (TES-1T) at 11-12.*

Q. Is Mr. Falkenberg's adjustment the same amount as Staff's?

A. Not exactly. I cannot replicate Mr. Falkenberg's figure of $2,192,439, as shown in the table in his direct testimony on page 5, Line Item 4. In his testimony, he references PacifiCorp's response to ICNU Data Request 1.39, but that response does not quantify the adjustment.

Staff's adjustment is based on PacifiCorp's response to Staff Data Request 59. The difference in revenue requirement between the Company's filed case and the amount in its response to Staff Data Request 59 is $2,193,439, exactly $1,000 higher than Mr. Falkenberg's figure.

Q. How did Staff quantify its adjustment?

A. As I described in my direct testimony, Exhibit ___ (TES-1T) at 12, Staff calculated the difference between the net operating income and rate base PacifiCorp used in the adjusted results of operations of the Company's direct case and the corresponding data from the Company's response to Staff Data Request 59. The result is $2,193,439 using the Company's filed conversion factor and rate of return. This is the figure I compared to ICNU's adjustment. However, Staff applied the corrected conversion factor and its revised return on rate base to arrive at a revenue requirement reduction of $2,182,127.

Q. Does this conclude your cross-answering testimony?

A. Yes.