

Exhibit 600T (LW-T)

**BEFORE THE WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION**

Docket Nos. UE-991255, UE-991262, and UE-991409

DIRECT TESTIMONY OF LINCOLN WOLVERTON

On Behalf Of

INDUSTRIAL CUSTOMERS OF NORTHWEST UTILITIES

December 8, 1999

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December 8, 1999

Q. PLEASE STATE YOUR NAME, AFFILIATION AND BUSINESS ADDRESS.

A. My name is Lincoln Wolverton. My business address is East Fork Economics, P.O. Box 620, La Center, Washington 98629. I am an economist, and through East Fork Economics, I am a consultant for Industrial Customers of Northwest Utilities (“ICNU”). My qualifications are summarized in Exhibit 601 (LW-1).

Q. PLEASE DESCRIBE ICNU.

A. ICNU is a non-profit trade organization comprised of forty-one industrial electric users in the Pacific Northwest. Many ICNU members purchase electric service in Washington from Avista Corporation (“Avista”), PacifiCorp, and Puget Sound Energy, Inc. (“PSE”). ICNU represents the common interests of its members in regulatory proceedings throughout the Pacific Northwest.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. My testimony responds to the Applications and Direct Testimony filed by Avista, PacifiCorp and PSE (collectively “the Companies”) in these consolidated proceedings. The Companies are requesting approval from the Washington Utilities and Transportation Commission (“WUTC” or “Commission”) to sell their respective interests in the Centralia Power Plant (“Centralia”) to TECWA, a wholly owned-subsiidiary of Transalta. My analysis assumes that the sale price received by the Companies for their respective interests in Centralia represents the full market value of the plant; therefore, my testimony does not address the prudence of the sale itself. Instead, my testimony addresses the regulatory treatment of any proceeds from the sale of the plant that exceed the Companies’ respective net book investments in Centralia. This net amount, which I will refer to as the gain from the sale, does not represent the creation of new value.

1 Instead, the gain approximates the future value of the plant reduced to the present through
2 the sale process.

3 **Q. PLEASE IDENTIFY THE MAJOR POINTS YOU MAKE IN THIS TESTIMONY.**

4 **A.** The following major points are made in this testimony:

- 5 • Any allocation or other regulatory treatment of the gain from the sale of Centralia
6 should be deferred and considered in the context of the Companies' next rate
7 cases.
- 8 • Allocating any portion of the gain to shareholders provides shareholders with an
9 unjustifiable and excessive return on investment. Therefore, ratepayers are
10 entitled to 100 percent of the gain.
- 11 • The treatment of the gain from the sale of Centralia must be considered in the
12 broader context of the Companies' and their customers' overall exposure to
13 stranded costs that may occur through industry restructuring.
- 14 • In this broader context, any sharing of the gain between customers and
15 shareholders is inappropriate because it provides an inappropriate incentive to the
16 Companies to sell and profit from their below-market assets now, and then claim
17 a right to be reimbursed for the stranded costs associated with their above-market
18 resources when restructuring occurs. Allowing the Companies to share in the
19 gains without demanding that the Companies also share in the losses embraces the
20 "heads the utility wins, tails the ratepayer loses" approach to allocating stranded
21 costs and benefits.
- 22 • The Companies' proposals for sharing the gain are unpersuasive and ignore the
salient fact that ratepayers must receive 100 percent of the gain for the sale to be
in the public interest.

17 **Q. WHY SHOULD THE COMMISSION DETERMINE THE ALLOCATION OF
THE GAIN IN A RATE CASE RATHER THAN IN THIS PROCEEDING?**

18 **A.** Deferring a determination of the ratemaking treatment of the gain from the sale of
19 Centralia until a rate case will allow the Commission to address the allocation and
20 disposition of the gain within the broader context of each of the Companies' operations.
21 The Commission may not have sufficient information in this proceeding to assess the
22 effects any sharing of the gain might have on each of the Companies' overall rate

1 structures. Furthermore, waiting until the next rate case will not unreasonably burden
2 any of the Companies. Since PacifiCorp and Avista have recently filed general rate cases
3 in Washington, the disposition of the gain with respect to those two Companies could
4 occur in proceedings that have already commenced.

5 PacifiCorp has indicated that it would like to be able to make a business decision
6 regarding the sale with knowledge of how the Commission will allocate the gain (*See*
7 Exhibit 602 (LW-2), Excerpts from Anne Eakin's Rebuttal Testimony in Oregon PUC
8 Docket No. UP 168 at PPL/16, Eakin/7 lines 13-21); however, the decision to make the
9 sale should not be tied to the disposition of the gain. In fact, if the Commission finds that
10 the sale is prudent and in the public interest, it would be difficult for PacifiCorp to back
11 out of the sale without incurring consequences in its current rate filing. As for PSE, the
12 proposed sale of Centralia is very similar to PSE's sale of Colstrip. In that case, the
13 Commission found that the gain should be deferred and returned to ratepayers with
14 interest. Third Supplemental Order Approving Sale; Ordering Deferral of Gain and
15 Deferral of Power Cost Changes, Docket No. UE-990267 (September 30, 1999), at 16.
16 Thus, deferring a determination of the allocation of the gain until the next rate case is not
17 prejudicial to any of the Companies.

18 **Q. WHY ARE RATEPAYERS ENTITLED TO 100 PERCENT OF THE GAIN?**

19 **A.** Ratepayers are entitled to one hundred percent of the gain because ratepayers have
20 historically borne the risk and the financial burden of the costs associated with Centralia.
21 Ratepayers have been paying for 100 percent of the costs associated with Centralia since
22 it was first placed in Washington rate base. Since ratepayers have assumed the risk of

1 loss associated with this rate based asset, ratepayers should also enjoy all of the benefits
2 associated with Centralia.

3 This “benefits follows the risk” analysis is consistent with the Commission Staff’s
4 analysis in the Colstrip case. In that case, the Commission Staff explained that the
5 Commission has consistently held that gains should be provided to ratepayers. Third
6 Supplemental Order at 16.

7 In return for paying all of the costs associated with constructing, operating and
8 maintaining Centralia, ratepayers have historically been entitled to the benefits of the
9 power produced at Centralia. Benefits include the actual use of the power produced and
10 any profits associated with the market sale of surplus power. It would be inequitable for
11 these ratepayer benefits to be cut-off or diminished by the utility’s decision to sell the
12 asset. If the proposed sale of Centralia occurs, the only equitable treatment is to return to
13 ratepayers the full benefits they would have received absent the sale.

14 **Q. ARE YOU MAKING A DISTINCTION BETWEEN: (1) THE BENEFITS OF**
15 **CENTRALIA; (2) THE GAIN FROM THE SALE OF CENTRALIA; AND (3) THE**
BENEFITS FROM THE SALE OF CENTRALIA?

16 **A.** Yes. The benefits of Centralia have now been defined whether or not the asset is sold.
17 As ultimate risk takers, ratepayers are entitled to receive all of these benefits, which,
18 assuming that the value of Centralia was maximized through the auction process, are
19 equal to the market sales price less the Companies’ outstanding investment in the plant.

20 The gain from the sale of Centralia does not represent new value created as the
21 direct result of the sale; it merely reduces the future value of the asset to present terms.
22 The value of the asset is realized in the market when Centralia is put up for sale. There is
23 no additional value created by the Companies.

1 To allocate less than 100 percent of the gain to ratepayers would deprive
2 ratepayers of the benefits of the asset they have paid for over time, and which they will
3 otherwise receive if the sale is not completed.

4 **Q. ARE THERE ANY OTHER REASONS RATEPAYERS ARE ENTITLED TO 100
PERCENT OF THE GAIN?**

5 **A.** Yes. The costs associated with Centralia were front-loaded in rate base. Ratepayers paid
6 a disproportionate amount of the costs in the early years of Centralia's operation based
7 upon an understanding that a similarly disproportionate share of the benefits would
8 accrue to ratepayers toward the end of the asset's life. Ratepayers anticipated receiving
9 relatively more benefits as the asset depreciated. It would not be equitable to award
10 ratepayers less than 100 percent of the benefits they anticipated when agreeing to pay the
11 relatively higher costs in the early years of Centralia's operation.

12 **Q. WILL SHAREHOLDERS BE DISADVANTAGED IF RATEPAYERS RECEIVE
100 PERCENT OF THE GAIN?**

13 **A.** Absolutely not. If shareholders receive any portion of the gain they will be receiving an
14 excessive return on their investment in Centralia. As a fundamental principle of
15 ratemaking, the Companies are entitled to receive a return of their investment as an asset
16 is depreciated, and an opportunity to earn a reasonable return on the undepreciated
17 portion of their investment. In the case of Centralia, the Companies' have been provided
18 the opportunity to earn a fair return on the capital that the shareholders provided. Each of
19 the Companies have also received a partial return of its capital through depreciation. The
20 undepreciated value of the plant will be netted from the gross proceeds of the sale and
21 returned to the Companies as part of the proposed transaction. Thus, the Companies'

1 have been adequately compensated for the use of their money, and as a result of the
2 transaction will have 100% of their investments returned.

3 **Q. WHY IS INDUSTRY RESTRUCTURING RELEVANT TO THIS PROCEEDING?**

4 **A.** Each of the Companies has a varied mixed of generation resources which are currently
5 used to serve ratepayers. These generation resources include physical depreciable
6 resources and purchased power resources, such as contracts entered into with Qualifying
7 Facilities (“QF”) pursuant to the Public Utilities Regulatory Policy Act of 1978
8 (“PURPA”). Some of the resources provide relatively high-cost power, while other
9 resources provide relatively low-cost power. Currently, the Companies are able to
10 recapture the costs of both the high-cost and low-cost resources through regulated retail
11 rates. In a competitive marketplace, however, some of the benefits of the low-cost
12 resources may not be delivered to ratepayers and some of the expenses of the high-cost
13 resources may not be recovered by the Companies. To make sure that neither ratepayers
14 nor shareholders are unfairly benefited or burdened by retail open access, it is prudent to
15 adopt policies now that balance the interests of shareholders and ratepayers regarding
16 potential stranded costs or benefits.

17 **Q. WHAT DO YOU MEAN BY THE TERM “STRANDED COSTS”?**

18 **A.** Stranded costs are investments and contractual obligations that are no longer recoverable
19 in a competitive, deregulated energy market. The National Association of Regulatory
20 Utility Commissioners (“NARUC”) provides a common usage definition of stranded
21 costs. NARUC defines stranded costs by reference to the definition of Embedded Costs
22 Exceeding Market Prices (“ECEMP”), which is defined as follows:

1 Embedded costs of utility investments exceeding market prices are:
2 1) costs incurred pursuant to a regulatory or contractual obligation;
3 2) costs that are reflected in cost-based rates; and 3) cost-based
4 rates that exceed the price of alternatives in the marketplace.
5 ECEMPs may become “stranded costs” where they exceed the
6 amount that can be recovered through the asset’s sale

7 NARUC website (<http://www.naruc.org/glossary.htm>). Consistent with NARUC’s
8 definition, I am referring to stranded costs as both utility investments and contractual
9 obligations that would not otherwise be recoverable in a competitive market, including
10 PacifiCorp’s PURPA QF contracts and other purchased power obligations.

11 **Q. HOW COULD IGNORING THE EFFECTS OF INDUSTRY RESTRUCTURING
12 IN THIS PROCEEDING BE POTENTIALLY HARMFUL TO RATEPAYERS?**

13 **A.** Allowing the Companies to share in the gain from the sale of Centralia provides an
14 inappropriate incentive to the Companies to sell off their low-cost assets. The Companies
15 have an incentive to sell off the assets that have a market value in excess of net book now
16 in order to retain some of the net proceeds for shareholders while keeping their high-cost
17 resources in rates. In addition, when restructuring occurs, the companies will
18 undoubtedly seek 100% recovery of any stranded costs associated with the high-costs
19 retained resources when industry restructuring occurs. This result would inequitably
20 benefit shareholders at the expense of ratepayers. The proposed sale of Centralia should,
21 therefore, not be considered in isolation.

22 **Q. DOES ICNU OBJECT TO SELLING-OFF RESOURCES PIECEMEAL?**

23 **A.** No. As part of the restructuring process, the Companies should be allowed to sell
generating resources as long as 100 hundred percent of the gains from selling such
resources are returned to ratepayers, which will ensure that sales of below market
resources will be netted against the Companies’ total stranded costs, if any. At a

1 minimum, a symmetry should be maintained between the allocation of potential stranded
2 costs and benefits, including any stranded costs associated with the so-called regulatory
3 assets, such as the PURPA QF contracts.

4 **Q. DO YOU HAVE COMMENTS ON EACH OF THE COMPANIES INDIVIDUAL
PROPOSALS FOR ALLOCATING THE GAIN?**

5 **A.** Yes. While each Companies' proposal for sharing the gain is slightly different, none of
6 their proposals are equitable for ratepayers. Each of the individual proposals are
7 analyzed below.

8 **PACIFICORP**

9 **Q. BRIEFLY, HOW DOES PACIFICORP PROPOSE TO ALLOCATE THE GAIN
FROM THE CENTRALIA SALE?**

10 **A.** PacifiCorp's proposal is contained in the very brief testimony of Ms. Anne Eakin. In
11 essence, PacifiCorp proposes to share the \$83 million system-wide gain by using a
12 depreciation reserve method. Exhibit 213T at 2-4. The result is that ratepayers receive
13 64% of the net gain, and shareholders receive the remainder.

14 **Q. HOW DOES THE DEPRECIATION RESERVE METHOD WORK?**

15 **A.** The depreciation reserve method divides the share of the net proceeds between
16 shareholders and ratepayers based on the ratio of net book value to original book value.
17 For example, if the plant is 64% depreciated, the net proceeds would be allocated 64% to
18 ratepayers and 36% to shareholders. The ratepayers' share is apportioned based on the
19 percentage of the plant's costs that have been depreciated, whereas the shareholders'
20 portion is based on the percentage of the plant's costs that have not been depreciated.

21 Id. at 3.

1 Ms. Eakin contends that the depreciation reserve method represents a
2 “compromise” between ratepayers and shareholders that takes into account PacifiCorp’s
3 contention that there is an argument for shareholders’ retaining 100% of the gain.
4 PacifiCorp’s argument is based on the fact that shareholders have “placed up-front capital
5 at risk to construct and maintain this generating facility.” *Id.*, lines 4-5.

6 **Q. PLEASE DISCUSS PACIFICORP’S CONTENTION THAT IT MAY BE
ENTITLED TO 100% OF THE NET GAIN.**

7 **A.** PacifiCorp appears to want its shareholders to be treated just like the shareholders of
8 non-monopoly corporations that sell in competitive markets. Non-monopoly
9 shareholders are entitled to the entire amount of any gain associated with the up-front
10 capital they put at risk. However, those shareholders also bear the entire amount of any
11 loss associated with investments or purchase contracts that have costs in excess of the
12 price obtainable in the market. Shareholders of companies operating in competitive
13 markets enjoy symmetrical treatment of their gains and losses, and have no claim to
14 stranded costs.

15 **Q. HOW DOES PACIFICORP’S POSITION REGARDING NET BENEFITS
16 COMPARE TO YOUR UNDERSTANDING OF ITS POSITION REGARDING
NET LOSSES?**

17 **A.** PacifiCorp’s argument that it is entitled to 100% of the gain on Centralia is totally at odds
18 with any claim it might have to recovery of stranded costs associated with its generation
19 resources, including the so-called regulatory assets, such as PURPA QF contracts.
20 PacifiCorp seems to say that the utility can sell off any profitable investment and retain
21 the entire net gain for the shareholders. Meanwhile, of course, PacifiCorp is allowed an

1 opportunity to earn a just and reasonable return on its other investments, including
2 above-market resources.

3 PacifiCorp contends that it is entitled to keep the gain because it has placed
4 up-front capital at risk. Exhibit 213T at 3. However, if PacifiCorp puts capital at risk for
5 assets that have stranded benefits, then it must also put capital at risk for assets that have
6 stranded costs. This rationale also applies to PacifiCorp's PURPA QF contracts because
7 those contracts were priced at the cost of the investments PacifiCorp would have made
8 but for the QF contract. While no up-front capital was initially invested in power
9 purchase contracts, as contractual commitments they may also produce unforeseen costs
10 or benefits with respect to today's market, and therefore require the same symmetrical
11 treatment. The only logical conclusion is that stranded costs and stranded benefits be
12 symmetrically allocated between shareholders and ratepayers.

13 Although PacifiCorp contends that its asymmetrical treatment of stranded costs
14 and stranded benefits is valid, it offers a "compromise" approach instead: something it
15 calls the depreciation reserve method.

16 **Q. IS THE DEPRECIATION RESERVE METHOD A FAIR APPROACH?**

17 **A.** Absolutely not. PacifiCorp's theory results in excessive returns to shareholders.

18 PacifiCorp has been provided the opportunity to earn a fair return on the capital that the
19 shareholders provided. PacifiCorp has received a partial return of its capital through
20 depreciation. The undepreciated value of the plant has been netted from the gross
21 proceeds of the sale and is being returned to PacifiCorp in this transaction. Thus,
22 PacifiCorp has been adequately compensated for the use of its money, and as a result of
23 the transaction will have 100% of its investment returned.

1 Q. **IS THE DEPRECIATION-RESERVE METHOD CONSISTENT WITH WHAT
WOULD HAVE HAPPENED ABSENT THE SALE OF CENTRALIA?**

2 A. No. Absent a sale, the above-book market value of Centralia would accrue to ratepayers
3 through lower power costs. Instead of paying the market price for replacement power in
4 the future, ratepayers would enjoy the cost-based output of the Centralia plant. The
5 market apparently considers the value of Centralia to be higher than the estimated
6 accounting costs of the system; the positive net value embodied in the sale price
7 represents the present value of the purchaser's view of the market versus the costs of
8 operating the plant. Without a sale, ratepayers likely would receive the value that
9 PacifiCorp is proposing be allotted to shareholders.

10 Q. **IS PACIFICORP PROPOSING THAT THE DEPRECIATION RESERVE
METHODOLOGY BE APPLIED TO ASSETS WITH STRANDED COSTS?**

11 A. Not necessarily. PacifiCorp has not clarified its understanding of the effect that adopting
12 the depreciation reserve method in this proceeding would have on future proceedings
13 involving the allocation of stranded costs between shareholders and ratepayers.
14 PacifiCorp is apparently willing to concede that if the depreciation reserve method is
15 used to allocate the gain in this case, that the same method should be used in future
16 proceedings involving the sale of a plant at a book loss. *See Exhibit 603 (LW-3)*
17 *(Excerpts from the Rebuttal Testimony of Anne Eakin in Oregon PUC Docket No. UP*
18 *168 at PPL/16, Eakin/5 lines 20-22).* Of course, the symmetry of this proposal is illusory
19 given that PacifiCorp would not have any reason to sell a plant and incur a loss when it
20 can simply retain the plant in rate base and receive its full return on and return of
21 investment. Moreover, PacifiCorp is apparently not willing to extend the same reasoning
22 to the allocation of any future stranded costs associated with its so-called regulatory

1 assets, such as the PURPA QF contracts. Id. at PPL/16, Eakin/6 lines 1-8. Thus, the only
2 risk faced by PacifiCorp in investing its capital is the uncertainty associated with whether
3 shareholders will receive a just and reasonable return or an even larger return. Under my
4 understanding of PacifiCorp's approach to stranded costs, PacifiCorp's shareholders face
5 no risk of loss.

6 PacifiCorp appears to take the position seems to be saying that if an investment
7 turns out to be particularly lucrative or profitable, shareholders should have the right to
8 capture the benefit of that good investment. On the other hand, if a resource, such as a
9 PURPA QF contract, produces a loss, the shareholder investment should be reimbursed
10 by the ratepayers. This theory is, of course: heads, PacifiCorp wins; tails, the ratepayer
11 loses.

12 If PacifiCorp's position is that all generating resources—owned and purchased,
13 including PURPA QF resources—are the shareholder's responsibility in terms of risk,
14 then this case would take on an entirely different dimension.

15 **Q. PLEASE ELABORATE.**

16 **A.** I strongly oppose PacifiCorp's views on stranded costs generally, and its contention that
17 shareholders are entitled to 100 percent of the net gain from the sale of Centralia.
18 Ratepayers have been paying for PacifiCorp's cost of owning and operating the Centralia
19 since it was first placed in rate base. It is, in effect, a ratepayer asset. Because ratepayers
20 have been responsible for paying all the costs associated with Centralia, ratepayers
21 should receive all of the benefits from the sale. Applying PacifiCorp's stranded costs
22 approach to this context, it is ratepayers, not shareholders, who should receive 100
23 percent of the net gain on the sale of Centralia.

1 Q. **IS THE DEPRECIATION RESERVE METHODOLOGY CAPABLE OF**
2 **ALLOCATING THE STRANDED COSTS OR BENEFITS ASSOCIATED WITH**
3 **REGULATORY ASSETS, SUCH AS PURPA QF CONTRACTS, AND OTHER**
4 **PURCHASED POWER RESOURCES?**

5 A. No. Another reason for rejecting PacifiCorp's so-called "compromise" for allocating the
6 net gain from the Centralia sale, is that the depreciation reserve methodology is not
7 capable of allocating any stranded costs or benefits associated with the PURPA QF
8 contracts and other purchased power resources between shareholders and ratepayers.
9 Purchased power contracts generally are not included in the utility's capital-asset
10 accounts and therefore face no utility depreciation and rate base treatment. Rather, those
11 costs are incorporated into rates through the recovery of the purchase cost.

12 Q. **DO YOU AGREE WITH PACIFICORP'S PROPOSAL TO USE THE**
13 **CUSTOMER'S PORTION OF THE GAIN TO WRITE DOWN**
14 **GENERATION-RELATED REGULATORY ASSETS?**

15 A. No. The customer's portion of any gain should not be used to write down
16 generation-related regulatory assets. Moreover, this is not the appropriate proceeding in
17 which to determine how PacifiCorp should return the ratepayers' portion of the gain.
18 That decision should be made in PacifiCorp's recently-filed general rate proceeding.

19 **Avista**

20 Q. **WHAT IS AVISTA'S POSITION REGARDING DISPOSITION OF THE GAIN**
21 **FROM THE CENTRALIA SALE?**

22 A. Avista's position regarding how the gain is shared is contained in the testimony of
Thomas D. Dukich (Exhibit 306T). Mr. Dukich takes the extremely "aggressive"
position that 100 percent of the gain should be retained for shareholders. Exhibit 360T at
3 lines 8-9. Alternatively, Avista believes an amount greater than PacifiCorp's
depreciation method is supportable. Id.

1 Mr. Dukich contends that the Commission should balance the interests of Avista
2 customers and shareholders in determining disposition of the gain. Mr. Dukich argues
3 that awarding all or most of the gains to shareholders is equitable given Avista's failure
4 to earn its authorized return on equity in the past. Id. at 4. Mr. Dukich also argues that
5 Avista is entitled to the gain because Avista's residential rates have been
6 "consistently . . . among the very lowest in the United States." Id., line 21.

7 Finally, Mr. Dukich identifies write-offs that Avista has taken since 1985. Id. at 5.
8 While he explains that he is not second guessing the Commission's application of the
9 prudence and "used and useful" standards, Mr. Dukich believes these write-offs warrant a
10 sharing of the gain from the sale of Centralia with Avista's shareholders. Id. at 6.

11 **Q. DO YOU AGREE WITH HIS ARGUMENTS?**

12 **A.** Absolutely not. I will take them one at a time.

13 First, as to balancing the interests of the shareholders and ratepayers: As I
14 indicated earlier, Avista has been authorized a fair rate of return for all of its rate-base
15 assets. That authorized return by its definition balances the interests of ratepayers and
16 shareholders. No further balancing is necessary.

17 In addition, Avista's shareholders' investment in Centralia has been partially
18 returned through depreciation, and its remaining investment will be returned through
19 payment for the remaining net book value of the plant when the proposed sale closes.
20 Avista and its shareholders have been able to take the monies returned to them in the past
21 and invest those funds in whatever they think will yield them a fair return; they can do
22 the same with the remaining net book investment. There is no need for ratepayers to
23 provide a "balance" to what Avista on behalf of its shareholders decides to do with the

1 money in its own hands.

2 The issue boils down to whether or not Avista shareholders should obtain a higher
3 return on their investment than the fair return authorized by the Commission from time to
4 time—the result of awarding the gain to shareholders.

5 **Q. PLEASE ADDRESS THE ISSUE OF AVISTA’S OVERALL EARNED RATE OF
RETURN OVER THE YEARS.**

6 **A.** The issue of whether Avista has earned its authorized rate of return historically is
7 between Avista shareholders and Avista management (or, in the past Washington Water
8 Power). It is not an issue for the Commission unless company operations impact safety
9 or reliability. If Avista is unable to meet cost targets or develop used and useful
10 investments, which would be prime causes of under-earning, it should either operate
11 more efficiently or prudently or it could seek rate relief. Avista management’s decision
12 to do neither is certainly not a ratepayer responsibility, and the ratepayers should not be
13 financially penalized for an Avista shareholder/management problem. It is simply not
14 appropriate to award Avista a gain from this sale on the basis of historical under-
15 performance.

16 **Q. SHOULD AVISTA BE AWARDED A GAIN BECAUSE OF ITS HISTORICAL
LOW RATES?**

17 **A.** If the question were phrased “Should Avista be awarded the gain because a large river
18 runs through its service territory?” the answer would clearly be no. Avista’s rates are low
19 primarily because it is largely a hydro-based utility with resources that were built long
20 ago. In fact, if one looks around the country, the prime reason for differences in utility
21 rates is due to the differences in generation resources. The Northwest long has been
22 known for its low rates as a result of its hydro-based generation. The accident of

1 geography does not automatically make Northwest utilities better than their national
2 counterparts. Mr. Dukich's argument implies that Avista is extremely efficient.

3 With resource costs varying greatly between utilities depending on their
4 geography or generation choices, a better measure of efficiency might be the non-
5 production costs of the utility.

6 **Q. HOW DOES AVISTA FARE IN A COMPARISON OF NON-PRODUCTION
COSTS?**

7 **A.** Poorly. In a calculation of non-production costs per customer, Avista isn't even among
8 the top 50% of utilities in the nation. In the ScottishPower/PacifiCorp merger
9 proceeding, Andrew MacRitchie submitted an analysis of non-production costs per
10 customer for 1996 based on EIA summary data from FERC Form 1 reports of 72 utilities.
11 Exhibit 604 (LW-4). The top 10 utilities averaged about \$190 per customer. Puget
12 Sound Energy at \$200.07 per customer was in the top 10, and PacifiCorp at \$300.13 per
13 customer was ranked fifty-sixth. Other utilities ranked among the top 72 utilities were
14 Sierra Pacific at \$247.33 and Idaho Power at \$322.31. By contrast, Avista did not appear
15 in the ranking because its non production costs per customer for 1996 were too high for
16 inclusion in the table. An independent review of Avista's 1996 FERC Form 1 report,
17 however, shows that Avista's non-production costs per customer were \$390.75.
18 Removing an estimate of the higher non-production costs Avista incurred in 1996 due to
19 an unusual ice storm, Avista had an adjusted non-production cost per customer of
20 \$342.01 Exhibit 605 (LW-5). Even after adjusting for the ice storm, Avista's non-
21 production costs per customer exceed the national median for 1996, which was \$328.85.

1 The Commission recently addressed the affect of PSE's Rate Plan on the
2 allocation of the gain from the sale of PSE's interest in Colstrip in Docket No.
3 UE-990267. The sale of Centralia is directly analogous to the sale of Colstrip; therefore,
4 the allocation of the gain should be deferred and distributed with interest to ratepayers in
5 PSE's next rate case and treated in a consistent manner with the sale of Colstrip.

6 **Q. DOES THIS CONCLUDE YOUR TESTIMONY.**

7 **A.** Yes.

WITNESS QUALIFICATION STATEMENT

Name: Lincoln Wolverton

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Education: B.A., 1963, Dartmouth College, English and French
M.A., 1971, University of Washington, Economics
Ph.D Candidate, 1971, University of Washington, Economics

Work Experience: Boeing Computer Services, Consulting Division, Seattle,
1973 – 1978
Portland General Electric, 1978 – 1981
Public Power Council, Vancouver, WA, 1981-1986
Resource Management International, Manager, Portland
Office, 1986 – 1987
East Fork Economics, Owner, 1987 – present

Experience: See attached:

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Record of Testimony
Submitted by
Lincoln Wolverton

Utility	Proceeding	Subject of Testimony	Before	Client	Date
Portland General Electric Company		Load forecasts	Oregon Public Utility Commission	PGE	1979
Portland General Electric Company		Load forecasts	Energy Facility Siting Council	PGE	1979
Bonneville Power Administration	1981 Rate Case	BPA costs, restructuring	BPA	Public Power Council	1981
Bonneville Power Administration	WP-83	Revenue requirements, DSI rate design, preference customer rate test,	BPA/FERC	Public Power Council	1983
Bonneville Power Administration	WP-85	Preference customer rate test, revenue crediting, cost allocation, DSI industrial margin	BPA/FERC	Public Power Council	1985
Bonneville Power Administration	VI-86	Aluminum company variable rate	BPA/FERC	Public Power Council	1986
Bonneville Power Administration	WP-87	Aluminum company variable rate, preference customer rate test, cost of service, revenue requirements	BPA/FERC	Association of Public Agency Customers	1987
Bonneville Power Administration	WP-91	Preference customer rate test, revenue crediting, cost allocation, financial goals, interruptible rates, unbundling of transmission costs	BPA/FERC	Association of Public Agency Customers	1991
Bonneville Power Administration	WP-93	Vintaged rates, financial risk planning, interim rate adjustments, preference customer rate test, revenue requirements, cost of service, rate design	BPA/FERC	Association of Public Agency Customers	1993
Bonneville Power Administration	WP/TR-96 TC-96	Rate design, revenue requirements, industrial margins, eligible customer under open-access tariff	BPA	Association of Public Agency Customers	1995
Puget Sound Power & Light and Washington Natural Gas	UE-960195 UE-951270	Puget Power/Washington Natural Gas merger support	Washington Public Utilities Commission	Industrial Customers of Northwest Utilities	1996
Puget Sound Power & Light	OA96-161-000 et al	Open access tariff recommendations, load forecasts	FERC	Industrial Customers of Northwest Utilities	1996-98
Oregon Generic	UM827	Marginal cost	OPUC	Industrial Customers of Northwest Utilities	1997
Enron/Portland General Electric	UE102	Competitive Choice	OPUC	Industrial Customers of Northwest Utilities	1997

Record of Testimony
 Submitted by
 Lincoln Wolverton

Utility	Proceeding	Subject of Testimony	Before	Client	Date
Washington Water Power	UE971422	Banded Rate discrimination, over-earnings	WUTC	Industrial Customers of Northwest Utilities	1997
Portland General Electric	ER98-3759	PGE OA tariff	FERC	Industrial Customers of Northwest Utilities	1998
ScottishPower/PacifiCorp	UM 918	On proposed ScottishPower/PacifiCorp merger	OPUC	Industrial Customers of Northwest Utilities	1999
Puget Sound Energy	UE-981238/ 9981410	Schedule 48 negotiations	WUTC	Industrial Customers of Northwest Utilities	1999

Docket No. UP 168
PPL Exhibit 16
Witness: A. E. Eakin

BEFORE THE OREGON PUBLIC UTILITY
COMMISSION

PACIFICORP

Rebuttal Testimony of Anne E. Eakin

December 1999

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1 would be satisfied if \$17.8 million of gain is allocated to Oregon customers. The
2 Company is proposing an allocation to Oregon customers of \$29.6 million. This would
3 seem to be dispositive of the only issue before the Commission – whether or not the sale
4 is in the public interest. Messrs. Jenks and Wolverton seem to be suggesting that the
5 Commission should deny approval of the sale unless more of the proceeds go to
6 customers so that the transaction can be made even more in the public interest or so a
7 precedent that they do not like is avoided. In doing so, they put at risk material and
8 tangible benefits to the very customers on whose behalf they are testifying.

9 Q. Staff witness Bryan Conway suggested that one alternative is to approve the sale on the
10 basis of at least \$17.8 million of the gain being allocated to customers, with the issue of
11 the allocation of the balance of the gain deferred to the Company's next general rate case.
12 Does PacifiCorp support such an approach?

13 A. No. PacifiCorp recognizes that it will not be possible to establish the precise ratemaking
14 adjustments associated with the Centralia sale until the conclusion of its ongoing rate
15 case. Among other reasons, the precise amount of the gain will not be known until the
16 sale closes. However, it is not reasonable to expect the Company to decide whether or
17 not to proceed with the sale of the Plant and Mine without knowing what policy this
18 Commission and the other five state commissions regulating PacifiCorp will apply in
19 respect to the allocation of gain. I am not aware of any prior proceeding involving either
20 a proposed merger or disposition of property where the Commission declined to establish
21 ratemaking policies related to the transaction.

Docket No. UP 168
PPL Exhibit 16
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BEFORE THE OREGON PUBLIC UTILITY
COMMISSION

PACIFICORP

Rebuttal Testimony of Anne E. Eakin

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1 A. No. PacifiCorp has proposed that its gain sharing proposal be implemented as of the
2 effective date of new prices resulting from its ongoing rate case.

3 Q. Mr. Wolverton proposes that consideration of the allocation of gain from the Centralia
4 sale should be “deferred and considered as part of the mandated valuation and disposition
5 of PacifiCorp’s resources” under SB 1149. Do you agree?

6 A. No. As indicated in Mr. Miller’s direct testimony, the decision to attempt to sell
7 Centralia was made by the Company independent of any larger decisions concerning
8 industry restructuring or vertical disaggregation. We believe that the Commission’s role
9 in this proceeding is to determine whether the sale of Centralia, on the terms proposed by
10 the Company, is in the public interest. We believe that this determination can and should
11 be made independent of SB 1149 implementation. Furthermore, PacifiCorp is not aware
12 of any provision of SB 1149 which requires all of its generation resources to be subject to
13 either a valuation or a disposition. As we understand it, under SB 1149, valuation would
14 only occur in the context of “transition charges” and “transition credits.” The Company
15 expects that most of the benefits of PacifiCorp’s generation resources will continue to be
16 available to its customers and that no valuation of those resources would be either
17 appropriate or required.

18 Q. What about Mr. Wolverton’s suggestion that PacifiCorp is effectively proposing a “heads
19 the utility wins, tails the ratepayer loses approach?”

20 A. This is not the case. Were the Commission to adopt the depreciation reserve method in
21 this proceeding, there is every expectation that in a future proceeding involving the sale
22 of a plant at a book loss, the results of this case would not go without notice.

1 Furthermore, Mr. Wolverton seems to believe that it is appropriate to throw the
2 Company's generating plants in the same bucket as its regulatory assets and Qualifying
3 Facility (QF) contracts. The Company is not persuaded that this is appropriate.
4 Generating plants represent the product of utility investment decisions. If those decisions
5 are imprudent, shareholders are and should be at risk. If those decisions are good ones,
6 shareholders may have an opportunity to benefit. In contrast, regulatory assets and QF
7 contracts are the product of regulatory decisions and policies over which the Company
8 has no control. They should not result in either losses or gains to shareholders.

9 Q. Both Messrs. Jenks and Wolverton suggest that the Commission's decision in UE 102
10 should be dispositive of the gain issue. Do you agree?

11 A. No. The Commission expressly held that UE 102 was not to be a generic proceeding.
12 Furthermore, UE 102 involved a proposed sale of all of Portland General Electric
13 Company's (PGE) generation so as to accomplish a total restructuring of that company.
14 It also occurred with the backdrop of PGE having been permitted to recover the full
15 amount of its Trojan Nuclear Plant investment. This proceeding involves a discrete
16 transaction by a different utility which is in the interest of consumers independent of any
17 restructuring considerations.

18 Q. Do you have any concluding observations regarding the positions taken by Messrs. Jenks
19 and Wolverton?

20 A. Yes. The unchallenged testimony of the Company and the Staff demonstrates that the
21 sale of Centralia will materially benefit consumers, even if 36 percent of the gain is
22 allocated to shareholders. Specifically, the Staff found that the "no-harm" standard

Comparison of Non-Production Cost/Customer for US Utilities (1996)

	Company	Customers	Non-production Costs per Cust. (\$)
1	Florida Power & Light Company	3,550,742	157.88
2	Florida Power Corporation	1,292,057	179.77
3	Consumers Energy Company	1,580,343	184.08
4	Citizens Electric Company	6,211	191.07
5	San Diego Gas & Electric Company	1,157,452	194.02
6	Northwestern Wisconsin Electric Co.	10,796	195.72
7	Wisconsin Electric Company	961,982	199.24
8	Puget Sound Energy, Inc.	849,065	200.07
9	New Century Energy	1,498,251	205.16
10	Superior Water, Light & Power Co.	13,948	210.57
11	Madison Gas and Electric Company	120,746	214.28
12	WPI Holdings	382,008	214.29
13	Public Service Electric and Gas Co.	1,884,860	221.27
14	WPS Resources	426,234	221.61
15	Northwestern Public Service	55,526	222.20
16	Black Hills Corporation	55,464	227.01
17	Southern California Edison Company	4,201,586	227.18
18	Empire District Electric Co.	137,926	229.40
19	Connecticut Valley Electric Co., Inc.	10,331	231.20
20	Connectiv	915,114	237.34
21	Northern States Power Company	1,411,783	241.81
22	Bangor Hydro-Electric Company	118,760	245.07
23	Sierra Pacific Power Company	746,029	247.33
24	Lockhart Power Company	5,762	247.48
25	Central Maine Power Company	519,005	247.55
26	Commonwealth Edison Company	3,395,802	247.56
27	MidAmerican Energy Company	637,966	247.95
28	LG&E Energy	805,976	250.14
29	Texas Utilities Electric Company	2,409,216	254.03
30	St. Joseph Light & Power Company	61,062	255.85
31	First Energy	2,135,604	259.72
32	Virginia Electric and Power Company	1,943,619	265.16
33	Illinois Power Company	557,638	265.93
34	Tampa Electric Company	506,038	265.99
35	MDU Resources Group, Inc.	112,681	268.63
36	Portland General Electric	660,767	271.04
37	Interstate Energy	498,830	271.51
38	UNITIL Corp.	89,082	273.30
39	South Carolina Electric & Gas Co.	488,984	277.04
40	Oklahoma Gas and Electric Company	680,584	279.14
41	Pacific Gas and Electric company	4,439,305	279.61
42	Central Louisiana Electric Company	219,377	280.17
43	Central Illinois Light Company	193,577	281.18
44	Western Resources	1,040,974	281.63
45	AEP-Central & South West	4,614,022	282.18
46	Detroit Edison Company	2,013,608	285.09
47	Ameren	1,453,972	288.03
48	Tucson Electric Power Company	306,773	288.25
49	Alaska Electric Light and Power	13,840	288.38
50	Indianapolis Power & Light Company	411,218	291.22
51	Southern Indiana Gas and Electric	121,185	292.90
52	New England Electric System	1,281,737	293.79
53	Public Service Co. - New Mexico	337,568	295.47
54	Potomac Electric Power Company	679,426	296.20
55	Baltimore Gas and Electric company	1,100,208	298.78
56	PacifiCorp	1,383,094	300.13
57	Energy Corporation	2,421,875	302.02
58	Central Hudson Gas & Electric Corp.	263,781	302.69
59	Pennsylvania Power & Light Co.	1,230,139	304.81
60	Allegheny Power Systems	1,959,939	305.72
61	Texas-New Mexico Power Company	216,316	306.86
62	UtiliCorp United, Inc.	355,569	310.52
63	Long Island Lighting Company	1,030,010	310.78
64	Dayton Power and light Company	477,307	311.24

Top Ten



Note: Companies in bold have similar operating conditions to PacifiCorp i.e. customer mix and terrain.

1st Quartile



PacifiCorp

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Comparison of Non-Production Cost/Customer for US Utilities (1996)

	Company	Customers	Non-production Costs per Cust. (\$)
65	Edison Sault Electric Company	21,074	312.23
66	New York State Electric & Gas Corp.	807,637	315.52
67	Maine Public Service Company	35,173	317.86
68	Carolina Power & Light Company	1,108,633	321.40
69	Niagara Mohawk Power Corporation	1,553,511	321.71
70	Idaho Power Company	346,436	322.31
71	Con Ed-Orange & Rockland	3,262,722	323.66
72	Cnergy	1,377,077	328.85

Source: EIA summary data from the FERC Form 1

Item	Avista					Adjusted 1996	PacifiCorp 1996
	1993	1994	1995	1996	1997		
FERC page							
Total Power Production Expenses	179795	166431	161557	271374	380794	271374	1241366
page 321							
Total Transmission Expenses	14085	13038	11918	14888	16127	14888	78625
page 321							
Total Distribution Expenses	15847	13588	16806	30800	16295	16550.5	91164
page 322							
Total Customer Accounts Expenses	7866	9097	10192	10409	10595	10409	58732
page 322							
Total Customer Service and Information Expenses	3425	4099	9950	10259	9514	10259	20527
page 322							
Sales Expense	590	468	379	802	363	802	12163
page 322							
Total Administrative and General Expenses	29225	35190	39087	47886	47464	47886	180620
page 323							
TOTAL ELECTRIC O&M	250833	241911	249889	386418	481152	372168.5	1683197
Total Number of Consumers	263813	270533	287133	292366	297198	292366	1383198
page 301							
Non-Generation Expenses	70448	75012	87953	114242	99995	99992.5	429668
Non-Generation Costs per Customer	\$ 267.04	\$ 277.27	\$ 306.31	\$ 390.75	\$ 336.46	\$ 342.01	\$ 310.63

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