

Exhibit No. NLK-1T
Docket UE-180778
Witness: Nikki L. Koblaha

**BEFORE THE WASHINGTON
UTILITIES AND TRANSPORTATION COMMISSION**

In the Matter of the Petition of

PACIFIC POWER & LIGHT COMPANY

For an Order Approving a Change in
Depreciation Rates Applicable to Electric
Property.

Docket UE-180778

**PACIFIC POWER & LIGHT COMPANY
DIRECT TESTIMONY OF NIKKI L. KOBLIHA**

September 2018

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1 **Q. Please state your name, business address, and present position with Pacific**
2 **Power & Light Company (Pacific Power), a division of PacifiCorp.**

3 A. My name is Nikki L. Koblaha. My business address is 825 NE Multnomah Street,
4 Suite 1900, Portland, Oregon, 97232. My present position is Vice President, Chief
5 Financial Officer and Treasurer for PacifiCorp.

6 **QUALIFICATIONS**

7 **Q. Briefly describe your education and professional experience.**

8 A. I received a Bachelor of Business Administration with a concentration in Accounting
9 from the University of Portland in 1994. I became a Certified Public Accountant in
10 1996. I joined the company in 1997 and have taken on roles of increasing
11 responsibility before being appointed Chief Financial Officer in 2015. I am
12 responsible for all aspects of the company's finance, accounting, income tax, internal
13 audit, Securities and Exchange Commission reporting, treasury, credit risk
14 management, pension, and other investment management activities.

15 **PURPOSE OF TESTIMONY**

16 **Q. What is the purpose of your testimony?**

17 A. My testimony:

- 18 • Summarizes the company's proposal for new depreciation rates and their effect on
19 annual depreciation expense. The proposed depreciation rates are based on
20 projected December 31, 2020 plant balances. The proposed depreciation rates are
21 contained in the "Depreciation Study - Calculated Annual Depreciation Accruals
22 Related to Electric Plant as of December 31, 2017" (Depreciation Study), which
23 was performed on behalf of the company by Mr. John J. Spanos of Gannett

1 Fleming Valuation and Rate Consultants, LLC. The Depreciation Study is
2 provided as Exhibit No. JJS-3 to Mr. Spanos's testimony.

- 3 • Provides a description of the development of the Depreciation Study and explains
4 why the depreciation rates resulting from the Depreciation Study are accurate and
5 reasonable.
- 6 • Identifies and discusses the key factors considered during the preparation of the
7 Depreciation Study. These factors were addressed in the data provided to Mr.
8 Spanos and, in turn, this data formed the basis for the Depreciation Study and the
9 recommended changes in depreciation rates.
- 10 • Introduces the other company witnesses who will testify in this proceeding and
11 provide a brief description of their respective subject matter.
- 12 • Briefly summarizes the company's recommendations to the Washington Utilities
13 and Transportation Commission (Commission).

14 **RESULTS OF THE DEPRECIATION STUDY**

15 **Q. Please explain the depreciation rates for which the company is seeking**
16 **Commission approval in this proceeding.**

17 A. Pacific Power seeks Commission approval of the depreciation rates contained in the
18 Depreciation Study based on December 31, 2020 projected balances as shown in the
19 Appendix of the Depreciation Study provided in Exhibit No. JJS-3 on page 1393 and
20 as summarized in Mr. Spanos's testimony.

21 **Q. Please explain how the depreciation rates were developed.**

22 A. The company instructed Mr. Spanos to use December 31, 2017 historical data as the
23 basis for his depreciation life study analysis, which was then used to develop

1 depreciation rates based on projected December 31, 2020 balances. This process is
2 further described in Mr. Spanos's direct testimony, Exhibit No. JJS-1T. Projecting
3 balances through December 31, 2020, aligns with the January 1, 2021 proposed
4 effective date wherein all anticipated plant additions have been considered when
5 developing the depreciation rates. The reasons for using a January 1, 2021 effective
6 date are further described in Mr. Steven R. McDougal's testimony.

7 **Q. How will the depreciation rates recommended by Mr. Spanos affect annual**
8 **depreciation expense?**

9 A. The Depreciation Study proposes a system-wide increase of 1.97 percent to the
10 current composite depreciation rate of 2.74 percent for the company's electric utility
11 plant, resulting in a new composite depreciation rate of 4.71 percent as shown in
12 Mr. McDougal's direct testimony, Exhibit No. SRM-1T. Applying the recommended
13 depreciation rates to the projected December 31, 2020 depreciable plant balances
14 results in an increase in total-company annual depreciation expense of approximately
15 \$561.7 million, compared with the level of annual depreciation expense developed by
16 application of the currently authorized depreciation rates to the same plant balances.

17 Adoption of the proposed depreciation rates results in an increase of
18 approximately \$37.4 million in annual Washington depreciation expense, based on
19 projected December 31, 2020 depreciable plant balances. In addition, the company
20 has assumed the current excess reserve amortizations stipulated in the company's
21 2013 depreciation study will be eliminated, as further described in Mr. McDougal's
22 testimony. Eliminating this excess reserve amortization results in an increase in
23 Washington's jurisdictional depreciation expense of \$0.5 million. The calculation of

1 the Washington jurisdictional amount under the West Control Area Inter-Jurisdictional
2 Allocation Methodology is also described in Mr. McDougal's testimony, which is
3 provided as Exhibit No. SRM-1T.

4 **DEPRECIATION STUDY BACKGROUND**

5 **Q. Please explain the concept of depreciation related to electric utility plant.**

6 A. There are many definitions of depreciation. The following definition was offered by
7 the American Institute of Certified Public Accountants in its Accounting Research
8 Bulletin #43:

9 Depreciation accounting is a system of accounting which aims to
10 distribute the cost or other basic value of tangible capital assets, less
11 salvage (if any), over the estimated useful life of the unit (which may
12 be a group of assets) in a systematic and rational manner. It is a
13 process of allocation, not of valuation.

14 The actual payment for an electric utility plant asset occurs in the period in
15 which it is acquired through purchase or construction. Depreciation accounting
16 spreads this cost over the useful life of the asset. The fundamental reason for
17 recording depreciation is to accurately measure a utility's operating costs. Capital
18 investments in the buildings, plant, and equipment necessary to provide electric
19 service are essentially a prepaid expense, and annual depreciation allocates that
20 prepaid expense applicable to each successive accounting period over the service life
21 of the asset. Annual depreciation is an important and essential factor in informing
22 investors and others of a company's periodic income. If it is omitted or distorted,
23 a company's periodic income statement is distorted and would not meet required
24 accounting and reporting standards.

1 **Q. Why is depreciation especially important to an electric utility?**

2 A. An electric utility's business is capital intensive; that is, it requires a continuous
3 investment in generation, transmission, and distribution equipment with long lives to
4 provide electric service to customers. The annual depreciation of this equipment is a
5 major component of expense to the utility. Regulated electric rates are set to allow
6 the utility the opportunity to fully recover its operating costs, earn a fair return on its
7 investment, and equitably distribute the cost of the assets to customers using the
8 facilities. If depreciation rates are established at an unreasonably low or high level
9 for ratemaking purposes, the utility will not recover its operating costs in the
10 appropriate period, which will shift either costs or benefits from current customers to
11 future customers.

12 **Q. Why was it necessary for the company to conduct the Depreciation Study?**

13 A. It is prudent accounting practice to periodically update depreciation rates to recognize
14 additions to investment in plant assets and to reflect changes in asset characteristics,
15 technology, salvage, removal costs, life span estimates, and other factors that impact
16 depreciation rate calculations. The company conducts depreciation studies as it
17 deems appropriate or as mandated by the Commission. The company's last
18 depreciation study was conducted approximately five years ago. The company's
19 current depreciation rates in Washington were effective on January 1, 2014, based on
20 a 2013 depreciation study. The Commission order approving the depreciation rates in
21 Docket UE-130052 required the company to file a new depreciation study no later
22 than December 31, 2018, or if completed earlier than December 31, 2018, within
23 30 days of the completion of a new depreciation study.

1 **Q. Was the Depreciation Study prepared under your direction?**

2 A. Yes. As Vice President, Chief Financial Officer and Treasurer, I am responsible for
3 the company's corporate accounting departments and for ensuring compliance with
4 company accounting policies and procedures. This includes periodic review and
5 study of depreciation rates.

6 **Q. Do you believe that the estimated plant depreciable lives and depreciation rates**
7 **developed in the Depreciation Study result in a fair level of depreciation expense**
8 **for customers to reimburse the company for its investment in electric utility**
9 **plant and equipment?**

10 A. Yes. I believe that the Depreciation Study is well supported by the underlying
11 engineering and accounting data, and that the resulting depreciation rates produce an
12 annual depreciation expense that is fair and reasonable for both financial reporting
13 and ratemaking purposes.

14 **Q. What is the basis for your conclusions about the Depreciation Study?**

15 A. A good depreciation study is the product of sound analytical procedures applied to
16 accurate, reliable accounting, and engineering data. I have reviewed Mr. Spanos's
17 work in preparing the Depreciation Study and concur with his methodologies and
18 application of analytical procedures as described in his testimony. With respect to
19 data inputs, Mr. Spanos used the estimated economic lives for thermal generation
20 plant provided by the company, as further explained in Mr. Chad A. Teply's
21 testimony. Mr. Spanos used the estimated economic lives for wind and hydro plant
22 provided by the company, as further explained in Mr. Timothy J. Hemstreet's
23 testimony. Depreciable life estimates for other types of plant and equipment are

1 based on Mr. Spanos's actuarial analysis of the data and reviewed for reasonableness
2 by the company. The accounting data has also been carefully and consistently
3 prepared. I recommend approval of the rates contained in the Depreciation Study.

4 **SIGNIFICANT ISSUES**

5 **Q. What are the steam generating facilities-related factors the company considered**
6 **in the Depreciation Study?**

7 A. The company considered:

- 8 • Recognizing the impact of incremental capital additions;
- 9 • Shortening of the terminal lives for several of the company's coal-fired units;
- 10 • Shifting group depreciation from a plant level to a unit level; and
- 11 • Changing the method used to determine terminal removal costs for each steam
12 generating facility.

13 **Q. Explain the impact of capital additions to the company's steam generating**
14 **facilities.**

15 A. Additions to property, plant and equipment balances, more commonly referred to as
16 capital additions, are one of the primary drivers that increase depreciation expense.
17 Because the company's steam facilities have set terminal lives, incremental capital
18 additions have to be depreciated over a shorter remaining life. Further explanation of
19 the need for these additions is included in Mr. Teply's testimony, Exhibit No. CAT-
20 1T.

21 **Q. Is this a new issue in relation to the steam generating facilities?**

22 A. No. This issue was identified in previous studies where the company proposed to
23 include projected capital additions in the development of depreciation rates to help

1 mitigate potential future depreciation step increases. The Commission's adoption of
2 depreciation rates arising out of those studies did not allow recognition of any
3 additions occurring after the implementation of those rates.

4 **Q. Did the company consider extending the depreciation lives of the steam
5 generating facilities to mitigate the increase in depreciation expense?**

6 A. No. There is uncertainty regarding the period in which steam generating facilities
7 will be allowed to continue to operate due to existing, evolving, or emerging
8 environmental regulations. Given this, the company does not recommend extending
9 the depreciation lives of the steam generating facilities. Instead the company
10 recommends shortening the depreciable terminal life of steam generating facilities.

11 **Q. For which steam generating facilities is the company recommending to shorten
12 the terminal life?**

13 A. The company is recommending shortening the terminal lives for all of its coal-fired
14 steam generating facilities. The reasons for shortening the terminal lives of these
15 facilities are discussed in Mr. Teply's testimony.

16 **Q. Explain the change made to the company's group method of depreciation for
17 steam generating facilities.**

18 A. In the depreciation study performed in 2013, depreciation for steam facilities were
19 grouped by Federal Energy Regulatory Commission (FERC) account at a plant level,
20 merging all units within one facility into one common group. For this Depreciation
21 Study, steam facilities are grouped by FERC account at a unit level. This shift in
22 methodology allows the company the flexibility to retire different units in different
23 years.

1 **Q. Please explain the adjustment made to decommissioning costs for steam**
2 **generating facilities.**

3 A. In the 2013 depreciation study, the company determined the decommissioning costs at
4 each facility by applying \$40 per kW. In this Depreciation Study, the company has
5 provided plant-specific estimates of decommissioning costs. Further explanation of
6 this issue is included in Mr. Teply's testimony.

7 **Q. Has the company changed any of the significant issues considered for**
8 **hydroelectric facilities lives in this Depreciation Study?**

9 A. No. The 2013 depreciation study based hydroelectric plant terminal lives primarily
10 on FERC hydroelectric plant license termination dates. For this Depreciation Study,
11 the company continued to use the FERC hydroelectric plant license termination dates
12 and has updated those lives where new licenses have been issued or are estimated to
13 be reissued within the next five years.

14 **Q. Please discuss the other hydroelectric facilities-related factors you considered**
15 **in this Depreciation Study.**

16 A. The 2013 depreciation study included removal cost for hydroelectric facilities where
17 the company has entered into negotiations or settlements to remove those facilities,
18 as well as a decommissioning reserve for minor hydroelectric facilities that may be
19 removed in the near future. The company has updated this Depreciation Study to
20 reflect the current projection for small plants where the company has estimated some
21 probability of them being decommissioned in the near future. This reserve is not
22 intended to cover the decommissioning or removal of any large facility.

1 **Q. Please discuss the wind generation facilities-related factors in the Depreciation**
2 **Study.**

3 A. The company will repower many of its wind generation facilities in 2019 and 2020.
4 The estimated balances in the Depreciation Study schedule for projected plant
5 balances as of December 31, 2020, reflect both the new investment in plant due to the
6 repowering, as well as the retirement of wind turbine equipment associated with the
7 repowered assets, with the retirement costs included in the depreciation reserve.

8 The treatment of retired wind turbine equipment included in the depreciation reserve
9 is consistent with the composite or group procedure of depreciation the company
10 applies to all facilities.¹ With the repowering of the wind generation facilities, the
11 company is recommending the terminal lives of wind generation facilities to be
12 30 years from the time of repowering. The repowering of the wind generation
13 facilities is discussed further in Mr. Hemstreet's testimony, Exhibit No. TJH-1T.

14 **Q. Please discuss the natural gas generation facilities-related factors in the**
15 **Depreciation Study.**

16 A. Since the 2013 depreciation study, the company has continued to experience interim
17 retirements related to scheduled overhauls on its natural gas facilities. This interim
18 retirement experience has allowed the company to provide Mr. Spanos with additional
19 historical retirement data to aid in his analysis and determination of interim retirement
20 patterns used in the calculation of the composite remaining lives. Changes to the
21 projected future interim retirements have contributed to an increase in depreciation
22 expense.

¹ The group depreciation procedure is discussed in Part V of Exhibit No. JJS-3 to Mr. Spanos's testimony.

1 **Q. Were there any significant changes in the Depreciation Study related to**
2 **transmission, distribution, and general plant assets?**

3 A. No. The company provided Mr. Spanos with the historical data for transmission,
4 distribution, and general plant assets including removal costs, salvage, and third-party
5 accommodation payments related to removal costs, to use in determining the
6 proposed depreciation lives and rates. There were no significant changes to the
7 depreciable lives and rates for these assets, outside of those which would normally
8 result from updating the study.

9 **INTRODUCTION OF WITNESSES**

10 **Q. Who will be testifying on behalf of Pacific Power in support of the company's**
11 **Petition?**

12 A. Four other witnesses will testify on behalf of the company: Mr. John J. Spanos,
13 Senior Vice President of Gannett Fleming Valuation and Rate Consultants, LLC,
14 Mr. Steven R. McDougal, Director of Revenue Requirements, Mr. Chad A. Teply,
15 Senior Vice President of Strategy and Development, and Mr. Timothy J. Hemstreet,
16 Director of Renewable Energy Development.

17 Mr. Spanos presents the Depreciation Study and the depreciation rates for
18 which the company is seeking Commission approval. Mr. Spanos describes how the
19 Depreciation Study was prepared and discusses the basis for the recommended
20 changes in depreciation rates.

21 Mr. McDougal describes and provides support for the jurisdictional allocation
22 of the Depreciation Study to Washington and identifies and discusses state-specific
23 factors considered during the preparation of the Depreciation Study.

1 Mr. Teply describes the process used by company’s engineers to evaluate the
2 current approved plant depreciable lives for steam and natural gas generating
3 facilities and estimates the retirement date for those generating facilities. Mr. Teply
4 demonstrates that the estimated retirement dates proposed by the company for
5 generation plants are reasonable and prudent and are appropriate inputs for Mr.
6 Spanos’s depreciation analysis. Mr. Teply also explains why the amounts the
7 company proposes to include as terminal net salvage, or “decommissioning costs,” in
8 the calculation of depreciation rates for generating plants are reasonable and prudent.

9 Mr. Hemstreet describes the company’s repowering project for its wind
10 facilities and the process of determining an appropriate life for the repowered wind
11 facilities. Mr. Hemstreet also describes the methodology used to estimate the
12 retirement date for the company’s hydroelectric generating stations. Mr. Hemstreet
13 demonstrates that the estimated retirement dates proposed by the company for wind
14 and hydroelectric generation plants are reasonable, prudent, and are appropriate
15 inputs for Mr. Spanos’s depreciation analysis.

16 **SUMMARY OF RECOMMENDATIONS**

17 **Q. Please summarize your recommendations to the Commission.**

18 A. I recommend that the Commission find that the depreciation rates sponsored by
19 Mr. Spanos in the Depreciation Study based on projected December 31, 2020 plant
20 balances are fair and reasonable for the company. I further recommend that the
21 Commission approve the company’s request to implement these depreciation rates in
22 its accounts and records effective January 1, 2021.

1 **Q. Does this conclude your direct testimony?**

2 **A. Yes.**