BEFORE THE

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, Complainant, v. PACIFICORP D/B/A PACIFIC POWER & LIGHT COMPANY, Respondent.	)	**Docket No. UE-061546** **Docket No. UE-060817** *(consolidated)*
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.	)	

INITIAL BRIEF OF

THE INDUSTRIAL CUSTOMERS OF NORTHWEST UTILITIES

REDACTED VERSION

(Confidential Information Removed)

April 23, 2007

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I. INTRODUCTION

1 The Industrial Customers of Northwest Utilities ("ICNU") submits this Initial Brief requesting that the Washington Utilities and Transportation Commission ("Commission" or "WUTC") reject PacifiCorp's proposed rate increase and order a rate reduction of up to $29.1 million. The Commission should deny the Company's Mid-American Energy Holdings Company ("MEHC") transition cost deferral, adopt a modified version of the Company's proposed West Control Area ("WCA") interstate cost allocation methodology that more accurately reflects the costs of resources used to serve Washington, and reject PacifiCorp's proposed power cost adjustment mechanism ("PCAM"). If the Commission determines that a PCAM is appropriate, then it should adopt ICNU's hydro-only PCAM and a reduction to PacifiCorp's return on equity ("ROE").

II. BACKGROUND

2 On May 19, 2006, PacifiCorp filed a deferral request related to the MEHC transaction requesting to defer costs associated with the ownership change, severance costs, new software costs, and benefits due to workforce reductions.[1/] On October 3, 2006, PacifiCorp filed its 2007 general rate case with the Commission proposing a $23.2 million, or 10.2% average (10.8% for industrial customers), rate increase.[2/] Pursuant to an expedited procedural schedule, ICNU, Public Counsel, Staff and the Energy Project submitted direct testimony on February 16, 2007. Staff proposed minimal modifications

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1/ Re PacifiCorp, Docket No. UE-060817, Initial Application ¶ 4 (May 19, 2006).
2/ Exh. No. 37 at 2 (Griffith Direct).

to PacifiCorp's PCAM and WCA cost allocation methodology, and proposed that PacifiCorp's rates should be increased by $15.9 million, if the Commission does not approve a PCAM.[3/] Included in Staff's adjustments were over $1 million in revenue requirement increases, and approximately $3.7 million of revenue requirement reductions that directly rely upon issues or adjustments previously identified by ICNU.[4/]

3 On March 5, 2007, PacifiCorp filed rebuttal testimony and Staff filed cross answering testimony. PacifiCorp adopted certain revenue requirement proposals resulting in a revised rate increase of about $19 million.[5/] PacifiCorp also revised its PCAM to conditionally accept some of Staff's minor changes.[6/] Staff filed extensive testimony addressing ICNU and Public Counsel's revenue requirement and cost allocation testimony.[7/]

4 PacifiCorp has failed to demonstrate that it is entitled to a rate increase, and the evidence establishes that the Company's rates should be reduced. PacifiCorp's claimed revenue deficiency is based on a results oriented cost allocation methodology designed to increase Washington rates. ICNU has proposed a number of revisions to the WCA, which more accurately reflect how PacifiCorp operates its system to serve Washington customers, including: 1) compensating Washington for a portion of the benefits western generating resources provide to the east; 2) incorporating in rates the

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3/ Exh. No. 321 at 4 (Schooley Direct).
4/ See id. at 10-12; Exh. No. 261 at 6-9 (Buckley Direct).
5/ Exh. No. 136 at 5 (Wrigley Rebuttal).
6/ Exh. No. 88 at 43 (Widmer Rebuttal).
7/ Exh. No. 235 (Buckley Cross Answering); Exh. No. 314 (Kermode Cross Answering); Exh. No. 328 (Schooley Cross Answering).

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pre-merger Wyoming resources that are used and useful to Washington; and 3) normalizing PacifiCorp's loss factors.

5 PacifiCorp has also inflated its costs and failed to remove certain non-beneficial, imprudent, or non-recurring costs. The Commission should correct these errors by adopting the adjustments related to: 1) replacement costs associated with Centralia; 2) imprudent Sacramento Municipal Utility District ("SMUD") contract; 3) improper modeling of short-term firm sales, the GP Camus contract, hydroelectric output, outage rates, and regulating margins; 4) inflated pension, health care expenses, and executive compensation; 5) tax expenses that will never be paid; 6) ScottishPower management fees; and 7) changes PacifiCorp's A&G costs to comply with the MEHC merger commitment.

6 The record also establishes that PacifiCorp's PCAM is a perilous proposal that will shift risk from PacifiCorp to customers without any corresponding benefits to ratepayers. PacifiCorp's PCAM is also ripe for manipulation and will be based on an untried cost allocation method and computer model results rather than actual costs ("pseudo actual costs"). The Commission should reject the PCAM and reconsider the adoption of such a mechanism only after the Commission has experience working with an approved cost allocation methodology. If the Commission intends to adopt a PCAM, then ICNU recommends that the Commission adopt a hydro-only PCAM and a reduction in the Company's ROE to reflect the value of the risk that would be shifted to ratepayers.

7 The Commission should also reject PacifiCorp's deferral of its costs associated with the MEHC transition because these costs are excessive, primarily benefit

the Company's shareholders, violate the MEHC merger agreement, and represent one-time, nonrecurring costs. Instead, the Commission should lower rates by including the MEHC transition savings because they are a reasonable representation of the savings that will occur due to the recent employee reductions.

8 Adoption of all of ICNU's proposed cost allocation and revenue requirement reductions would reduce PacifiCorp's proposed rate increase by $45.8 million. ICNU supports most of the non-duplicative rate reductions proposed by Staff, but Staff's MEHC deferral adjustment should not be adopted if ICNU's proposal is adopted. The table below provides ICNU's proposed adjustments, as well as $2.3 million of non-duplicative staff adjustments supported by ICNU.

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ICNU Proposed Adjustments to PacifiCorp's Rate Increase on a <u>Washington Jurisdictional Basis (000)</u>	
Energy Value of Western Resources to the East	$5,685
Value of Western Reserves to the East	$1,900
Wyoming Resources (Actual Flow)	$3,842
Wyoming Resources (Including Wyoming loads)	$8,244
Historical Loss Factors	$637
Short-term firm Transactions	$7,937
SMUD Contract	$2,770
Centralia Risk Sharing	$1,785
GP Camus	$31
Hydro Water Year Modeling	$1,569
Phantom Outages	$259
Regulating Margin Modeling	$191
PCAM ROE Adjustment	$1,200
Income Taxes	$3,079
MEHC Transition Costs Deferral	$2,457
Pension Expense	$944
Incentive Compensation	$2,045
Health Care	$282
ScottishPower Management Fees	$675
A&G Rate Cap	$266
Total ICNU Adjustments	**$45,798**
Staff Working Capital Adjustment	$1,260
Staff IRS Settlement Amortization	$1,083
Total Staff Non-Duplicative Adjustments[8/]	**$2,343**
Total Revenue Requirement Reductions	**$48,141**

[8/] Not included are Staff's power supply adjustments. Staff proposes $480,136 in power supply adjustments for transmission related costs and spinning reserves. Exh. No. 261 at 19-21 (Buckley Direct). Staff's spinning reserves adjustment should not be adopted if ICNU's dynamic overlay adjustment is adopted.

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III. ARGUMENT

A. PacifiCorp Has the Burden of Proof to Support Its Requested Rate Increase

9 PacifiCorp bears the burden of proof to demonstrate that its proposed tariffs are just and reasonable.[9/] This burden includes "the burden of going forward with evidence and the burden of persuasion."[10/] The Company retains this burden throughout the proceeding and must establish that the rate change is just and reasonable.[11/] Accordingly, PacifiCorp also retains the burden of proof to demonstrate that its proposed PCAM and MEHC transition cost deferral should be adopted.[12/]

10 When setting rates, a utility is allowed an opportunity to recover its operating expenses and to earn a rate of return on its property that is used to provide service.[13/] The amount of a utility's operating expenses included in rates is typically "based on actual operating expenses in a recent past period referred to as the 'test period' or 'test year'."[14/] A utility "cannot include every expense it wishes" in rates because the Commission reviews the utility's costs "to disallow those which were not prudently incurred."[15/] The Commission also removes from rate base all property not used and useful to serve Washington customers,[16/] and all non-recurring, one-time expenses and

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9/ RCW § 80.04.130(4); WAC § 480-07-540; WUTC v. PacifiCorp, Docket No. UE-061546, Order No. 1 at ¶ 9 (Oct. 10, 2006).

10/ WAC § 480-07-540.

11/ WUTC v. Pacific Power & Light Co., Cause No. U-84-65, Fourth Supp. Order at 17 (Aug. 2, 1985).

12/ See WUTC v. PacifiCorp, Docket No. UE-061546, Order No. 1 at ¶ 9; Re PacifiCorp, Docket Nos. UE-991832 and UE-020417, Eighth/Sixth Supp. Order at ¶ 22 (July 15, 2003).

13/ People's Org. for Wash. Energy Resources v. WUTC, 104 Wn.2d 798, 808-11 (1985).

14/ Id. at 810.

15/ Id.; see also WUTC v. Puget Sound Energy, Inc. ("PSE"), Docket No. UE-031725, Order No. 14 at ¶ 93 (May 13, 2004) (disallowing imprudent gas costs).

16/ RCW § 80.04.250; WUTC v. PacifiCorp, Docket Nos. UE-050684 and UE-050412, Order No. 4 at ¶¶ 48-70 (April 17, 2006).

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other costs that a utility is unlikely to experience during the term of the proposed rates.[17] Costs which are abnormal, fluctuate, or are not accurately estimated in the test period must be normalized to achieve an expected level of costs based on typical conditions.[18] Finally, regardless of prudence, all costs and expenses that do not benefit ratepayers or were incurred to benefit shareholders must be removed from rates.[19]

B. PacifiCorp's WCA Is a Flawed Cost Allocation Methodology Designed to Increase Washington Rates

11 The Commission should adopt a cost allocation methodology that accurately assigns costs to Washington based on the costs and benefits PacifiCorp actually incurs to provide electric service to Washington customers. The WCA is a simplistic approach that is based on the Company's western and eastern control areas, but incorrectly assumes that there are no interconnections between the two control areas.[20] This results in the WCA ignoring how the Company operates its system and dramatically overstating the costs to serve Washington customers.[21]

12 The WCA fails to allocate to the western control area any portion of the power cost related benefits of PacifiCorp operating as a merged company.[22] PacifiCorp allocates to the western control area the full cost of all generation, transmission and contracts located in the west, and assumes that these resources "have no connection to the

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[17] WUTC v. Avista Corp., Docket Nos. UE-991606 and UG-991607, Third Supp. Order at ¶¶ 205-07 (Sept. 29, 2000).
[18] Id. at ¶ 34.
[19] See U.S. West v. WUTC, 134 Wn.2d 74, 126-27 (1997); WUTC v. Avista Corp., Docket Nos. UE-991606 and UG-991607, Third Supp. Order at ¶¶ 239-40.
[20] Exh. No. 161 at 8: 16 – 10: 8 (Falkenberg Direct); Exh. No. 265 at 11: 10-17 (Buckley Cross Answering); Exh. No. 103 (PacifiCorp Response to ICNU data request number ("DR") 2.8).
[21] Exh. No. 161 at 8-10 (Falkenberg Direct); Exh. No. 503 (PacifiCorp Response to ICNU DR 8.36).
[22] Exh. No. 161 at 17: 7-20 (Falkenberg Direct).

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eastern side of system . . . ."[23/] This is inconsistent with how the Company "built and actually operates its system," and "completely ignores the fact that [the western] resources provide benefits to the integrated system, and would have opportunities to make profitable energy sales in eastern markets."[24/] The WCA also harms Washington ratepayers by failing to allocate to Washington the value of certain low-cost former Pacific Power and Light Company ("PP&L") resources that have always been included in Washington rates and continue to be used and useful for ratepayers.[25/]

13 The overall unreasonableness of the WCA method is demonstrated by the fact that it results in Washington becoming a high-cost state. The Commission has long recognized that PP&L's electric system was lower cost due to the predominance of hydro, low-cost coal, and the Company's lowest cost gas-fired generation.[26/] Although the west is served by these low-cost resources, the WCA assumes the west has significantly higher power costs than the east.[27/]

14 PacifiCorp recognizes that its WCA produces higher net power costs, but claims that comparing net power costs is not "valid" because overall "average system costs" should be considered.[28/] The hollowness of this argument is revealed in that PacifiCorp's own analysis shows that "average system costs" for the western system are higher than the east under the WCA.[29/] Staff, for its part, did not even analyze whether

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23/ Id. at 16-17.
24/ Id. at 10: 1-3, 17: 18-20.
25/ Id. at 9-12, 16-18.
26/ See Re PP&L, Docket No. U-87-1338-AT, Second Supp. Order at 14 (July 15, 1988); Exh. No. 161 at 6-7, 11-12 (Falkenberg Direct); Exh. No. 285 at 4-6 (Excerpt of Buckley Direct in UE-032065).
27/ Exh. No. 161 at 11-13 (Falkenberg Direct); TR 328: 6-13 (Buckley Cross Exam).
28/ Exh. No. 88 at 9-10 (Widmer Rebuttal).
29/ Id.

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the WCA produces higher average power costs on the east or the west.[30] The Commission should be highly skeptical of any cost allocation methodology that produces such unrealistic and counter-intuitive results.

15 The Commission should resolve interstate cost allocation issues by adopting ICNU and Public Counsel witness Randall Falkenberg's proposed revisions to the WCA. Mr. Falkenberg proposes two adjustments to modify the WCA to reflect the system interconnection benefits associated with the western system providing: 1) valuable electricity to the east, and 2) operating reserves to the east.[31] Mr. Falkenberg also proposes that the Commission include the pre-merger PP&L Wyoming resources (Dave Johnson and Wyodak) in Washington rates, and to update the WCA to account for more accurate loss factors.[32] Mr. Falkenberg's proposed revisions provide the Commission with a variety of options to adjust the WCA to produce reasonable overall results and more accurately reflect how PacifiCorp operates its system.

1. PacifiCorp and Staff Have Distorted the Commission's Used and Useful Standard

16 The Commission has provided PacifiCorp and the parties guidance regarding how to apply Washington's used and useful statute.[33] The statute allows the Commission "to ascertain and determine the fair value for rate making purposes of" only

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[30] Exh. No. 269 (Staff Response to ICNU DR 2.5); Exh. No. 270 (Staff Response to ICNU DR 2.6).

[31] Exh. No. 161 at 21-22 (Falkenberg Direct); Exh. No. 165 (Calculation of Interconnection Benefits).

[32] Exh. No. 161 at 22-27 (Falkenberg Direct). Mr. Falkenberg's direct testimony also proposed the use of traditional fixed cost jurisdictional cost allocators for demand and energy. Id. at 26; Exh. No. 172 at 12 (Excerpt of PacifiCorp Response to ICNU DR 2.6). PacifiCorp agreed with Mr. Falkenberg's adjustment in rebuttal testimony. Exh. No. 136 at 3-4 (Wrigley Rebuttal).

[33] WUTC v. PacifiCorp, Docket Nos. UE-050684 and UE-050412, Order No. 4 at ¶¶ 48-70.

that utility property that is "used and useful for service in this state . . . ."[34/] The Commission explained that resources must provide "benefits to ratepayers in Washington, either directly (e.g., the flow of power from a resource to customers) and/or indirectly (e.g., the reduction of cost to Washington customers through exchange contracts or other tangible or intangible benefits)."[35/] Resources that provide indirect, occasional or potential benefits may be allocated to Washington after a "more complex analysis, which must consider and quantify any indirect benefit sought to be recovered in rates."[36/]

17 According to PacifiCorp, the used and useful standard prevents the Company from determining the Washington's share of the value of any system wide benefits that are created by Western resources because it is "impossible to tell which resources generated the benefits and we would back to the Revised Protocol approach of allocating all resources to Washington."[37/] PacifiCorp misinterprets the Commission's order as essentially requiring that the only resources that are physically located inside the western control area can be found to be used and useful to Washington.[38/] Although the Commission concluded that resources that "indirectly" benefit Washington can be included in rates if they are properly calculated,[39/] PacifiCorp believes otherwise.[40/] Thus, according to PacifiCorp, Washington is forced to choose between a total system wide allocation that has no relationship to which generating resources serve Washington

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[34/] RCW § 80.04.250.

[35/] WUTC v. PacifiCorp, Docket Nos. UE-050684 and UE-050412, Order No. 4 at ¶ 50.

[36/] Id. at ¶ 51.

[37/] Exh. No. 88 at 12-15 (Widmer Rebuttal).

[38/] Id.

[39/] WUTC v. PacifiCorp, Docket Nos. UE-050684 and UE-050412, Order No. 4 at ¶ 51.

[40/] Exh. No. 501 (PacifiCorp Response to ICNU DR 8.31).

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(e.g., the Revised Protocol) or an isolated control area approach that ignores how the Company actually operates its system (e.g., the WCA).

18 Staff acknowledges that the used and useful standard is not an absolute bar to providing Washington customers with the full value of the resources used to serve them,[41/] but does not propose meaningful revisions to the WCA. Now that Staff has finally obtained PacifiCorp's agreement to propose a "workable" control area cost allocation method that will reduce its administrative burden, Staff is willing to ignore, or put off for future study, any significant problems in PacifiCorp's WCA.[42/] For example, in past proceedings Staff believed that a "fair cost allocation scheme would assign the higher power costs . . . primarily to those jurisdictions with high summer loads."[43/] Staff now supports the WCA and the allocation of higher power costs to Washington, despite the fact that Washington is a winter peaking state and Utah's two highest peaks are July and August.[44/] Similarly, Staff appears to have abandoned its previous position that any control area based method should include an evaluation of "inter-change transfer pricing, treatment of exchanges, and transmission cost allocation."[45/]

2. The WCA Fails to Compensate Washington for the Value of Western Resources that Benefit the Eastern System

19 The evidence establishes that the western control area, including Washington, derives some benefits from PacifiCorp operating its system on an integrated basis. For example, in the multi-state process, the Company estimated the benefits of

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41/ E.g. Exh. No. 261 at 12-13, 16-18 (Buckley Direct).
42/ See id. at 17: 16 – 18: 6; Exh. No. 265 at 11: 18 – 12: 6, 13: 10-22 (Buckley Cross Answering).
43/ Exh. No. 286 at 14 (Excerpt of Buckley Direct in UE-020417).
44/ Exh. No. 134 at 10.13 (Results of Operation).
45/ Exh. No. 285 at 30 (Excerpt of Buckley Direct in UE-032065); TR 329: 16 – 330: 6 (Buckley Cross Exam).

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system integration to be more than $200-300 million for the period 2005 to 2018.[46] Unlike past proceedings in which PacifiCorp did not provide specific evidence of how Utah generation resources benefited Washington, ICNU and Public Counsel have sponsored detailed calculations of Washington's share of system integration benefits based on how the Company actually operates its system.

20 ICNU's proposed adjustments satisfy the Commission's used and useful standard because they accurately calculate the value of PacifiCorp using western resources to benefit the east, and how the west benefits from the low-cost Wyoming resources that deliver power to Washington. Washington should be provided its share of the actual interconnection benefits and the Commission should reject PacifiCorp's position that Washington should be penalized for not agreeing to the Revised Protocol.

a. Washington Ratepayers Should Be Compensated for the Value of PacifiCorp Providing Electricity to the Eastern States

21 During the course of PacifiCorp's normal operations, the western control area provides low-cost energy to the eastern system that reduces the Company's overall costs of system operation.[47] PacifiCorp's WCA methodology allocates to the west the full costs of the western generation and transmission resources, but arbitrarily fails to reflect that these resources can and do provide power to the east.[48] Since these generation and transmission costs are included in Washington rates, the value of the benefits they provide to Washington should also be accounted for.[49]

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[46] Exh. No. 15 at 14 (Andrea Kelly Supp. Direct in OPUC Docket No. UM 1050).
[47] Exh. No. 161 at 17: 5-20 (Falkenberg Direct).
[48] Id. at 17: 16-20, 18: 5-11; Exh. No. 140 (PacifiCorp Response to ICNU DR 3.3).
[49] Exh. No. 161 at 18: 1-11 (Falkenberg Direct).

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22 The Commission should adopt Mr. Falkenberg's $5.7 million adjustment to PacifiCorp's WCA methodology because it an accurate assessment of the value of sales western resources make in the east. Mr. Falkenberg calculated his adjustment utilizing PacifiCorp's GRID computer model that is used to set power costs. Mr. Falkenberg first corrected the bias in the WCA methodology that excludes the actual interconnections to the east.[50/] Mr. Falkenberg then modeled sales to the east that would be made when western prices were lower than eastern prices, limited by the transfer capabilities inherent in GRID.[51/] Although he used GRID, Mr. Falkenberg's adjustment is "based on the real world operational constraints of PacifiCorp's system."[52/] Mr. Falkenberg's overall adjustment is conservative because it is limited to "only the actual transmission capabilities between the" western and eastern control areas.[53/]

23 PacifiCorp argues that the Commission should reject this interconnection benefit adjustment because it allegedly does not show "tangible and quantifiable benefits."[54/] Notably, PacifiCorp fails to present any evidence disputing that sales can be, or are actually, made from western resources to the eastern market hubs.

24 PacifiCorp's fundamental argument is that its GRID model, which it uses to set rates and intends to use to set "pseudo" actual power costs in its proposed PCAM, incorrectly models its transmission interconnections. If GRID is insufficient to adjust the WCA, then it should not be used to set net power costs or to construct fake "actual" numbers for a PCAM. In contrast, Mr. Falkenberg's methodology is consistent with

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50/ Id. at 21-22.
51/ Id. at 21: 16 – 22: 2.
52/ Id. at 22: 1-2.
53/ Id. at 22: 10-12.
54/ Exh. No. 88 at 16: 14-15 (Widmer Rebuttal).

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how, in PacifiCorp's recent Oregon rate case, PacifiCorp normalized its net power costs based on the assumption that the Company optimized its entire system to use the available transmission to sell western power in the eastern market hubs.[55/] Mr. Falkenberg's overall adjustment is "reasonable because the amount of generation flowing from west to east . . . was less than the amount shown by the Company in its recent GRID studies filed in Oregon as part of" its recent Oregon rate case.[56/]

25 PacifiCorp also alleges flaws because Mr. Falkenberg's interconnection adjustment allegedly overestimates the transmission connections and understates the costs of transmission.[57/] Although PacifiCorp alleges "errors," the Company does not providing an alternative calculation based on its proposed "corrections" to how GRID simulates sales of power from the western control area to the east. The Company only makes unsubstantiated claims that the adjustment is too large, without providing its estimate of what the adjustment should be.[58/] Ultimately, PacifiCorp has the burden of proof and persuasion, and it is up to the Company to submit an alternative calculation.[59/] ICNU's proposal, therefore, provides the best evidence in the record from which the Commission can base a decision.[60/]

55/ Id. at 19: 14 – 20: 15.
56/ Id. at 22: 7-10.
57/ Exh. No. 88 at 18: 6 - 21: 2 (Widmer Rebuttal).
58/ See id. at 20-21; Exh. No. 503 (PacifiCorp Response to ICNU DR 8.36).
59/ See WAC § 480-07-540.
60/ See WUTC v. PacifiCorp, Docket Nos. UE-050684 and UE-050412, Order No. 6 at ¶ 52 (July 14, 2006) (not the Commission's burden to develop an alternative methodology when the utility fails to present one).

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b. Washington Ratepayers Should Be Compensated for the Value of the Operating Reserves that Are Provided to the East

26 Washington should be allocated a portion of the benefits associated with providing operating reserves (called "dynamic overlay") to the eastern system.[61/] Mr. Falkenberg calculated this adjustment based on PacifiCorp's estimates of these benefits in the multi-state process.[62/] This adjustment would reduce PacifiCorp's revenue requirement by about $1.9 million.[63/]

27 PacifiCorp argues that the spinning reserves portion of the dynamic overlay adjustment should be rejected because these reserves should be retained for future resources in the west, and that the east can potentially provide its own spinning reserves.[64/] The Company's position should be rejected because it does not present any evidence that the west is not in fact now providing valuable spinning reserves to the east.

28 PacifiCorp also proposes that the total value of the dynamic overlay adjustment should be reduced by 50% to account for "sharing."[65/] PacifiCorp does not identify who these benefits should be shared with or the basis for the 50%. This arbitrary sharing reduction should be rejected as there is no evidentiary basis as to why the dynamic overlay benefits that the western system provides to the east should be "shared."

[61/] Exh. No. 161 at 17: 10-11, 22: 13-14 (Falkenberg Direct).

[62/] Id. at 22: 13-14.

[63/] ICNU's original dynamic overlay adjustment was $2.9 million, including $1.2 million related to ready reserves and $1.7 million related to spinning reserves. Exh. No. 165 (Calculation of Interconnection Benefits); Exh. No. 88 at 21: 3-9 (Widmer Rebuttal). In rebuttal PacifiCorp provided new evidence of changed circumstances that demonstrates the ready reserve adjustment should be reduced from $1.2 million to $0.17 million. Exh. No. 88 at 21: 3 – 22: 8 (Widmer Rebuttal). ICNU agrees that this new evidence supports a ready reserve adjustment of $0.17 million.

[64/] Exh. No. 88 at 23: 4 -21 (Widmer Rebuttal).

[65/] Id. at 24: 6-12.

c. Staff's Eastern Market Bubble Adjustment Is Insufficient and Poorly Supported

29 Staff recognizes that the WCA methodology fails to account for the fact that PacifiCorp's western system provides benefits to the eastern system and proposes a $1.05 million adjustment to the WCA.[66] Staff recognizes "that a number of other potential alternative methodologies could be developed"[67] and that its modified WCA "may not capture all of the costs and benefits of the Company's system operations."[68]

30 Staff's adjustment is based on a potential sale from the western system to the east along the Bridger transmission path at high load hours.[69] Staff did not calculate or develop the adjustment itself, but based the adjustment upon a GRID run performed by PacifiCorp.[70] In calculating the adjustment, PacifiCorp arbitrarily reduced the volumes available for the sales and then split the benefits associated with the western sales, which reduced their total value by 76%.[71] Staff's testimony provides no support or justification for this reduction in benefits. Similarly, PacifiCorp refused to provide direct support for the reasons for the reduction in benefits, simply explaining it was based on "the Company's professional knowledge and experience in the wholesale market."[72] A correct calculation of Staff's adjustment should reverse these arbitrary reductions.

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[66] Exh. No. 261 at 7-9 (Buckley Direct); Exh. No. 265 at 11: 10 – 12: 6 (Buckley Cross Answering).
[67] Exh. No. 261 at 8: 4-7 (Buckley Direct).
[68] See id. at 17: 16-22.
[69] Id. at 7: 9-13.
[70] Id. at 8: 1-7; Exh. No. 262 (PacifiCorp Response to Staff DR 88).
[71] Exh. No. 262 (PacifiCorp Response to Staff DR 88) (the value is reduced 40% to account for competition from other generators and then further reduced, with no justification, by 60%, which results in the west being provided only 24% of the benefits of western sales to the east).
[72] Exh. No. 498 (PacifiCorp Response to ICNU DR 8.14).

31 Staff's adjustment also suffers from other inadequacies when compared to Mr. Falkenberg's interconnection adjustments. For example, Staff's adjustment lacks the analytical support because it is not based on the actual interconnections, and ignores PacifiCorp's other transmission routes that are used to sell the western generation surplus in the east.[73/] Staff also fails to account for the fact that the western system provides operating reserves to the east. Staff did not submit any testimony disputing that these operating reserves are provided to the east, but appears to merely propose to add this to a long list of issues to be reviewed by the WCA monitoring committee.

d. PacifiCorp's Line Losses Should Be Normalized

32 PacifiCorp submits that the Company's forecasted line losses are 10.95%. For the past five fiscal years, however, PacifiCorp's line losses have averaged 10.107%.[74/] Rates are normalized to achieve an expected level of costs based on typical conditions,[75/] and to assure that rates are fair, just, reasonable and sufficient.[76/] To base future rates on typical conditions in this case, normalization of line losses is essential.

33 PacifiCorp witness Mark Widmer recognizes the need for normalization, and advocates for the normalization of retail load, thermal availability, and hydro generation.[77/] The Company also made a temperature normalization adjustment to its loads in GRID. Mr. Widmer correctly states that the basis for normalization is to remove extraordinary or unexpected costs from rates.[78/]

73/ See Exh. No. 161 at 18: 20 – 20: 23 (Falkenberg Direct).
74/ Id. at 27: 10-11.
75/ WUTC v. Avista Corp., Docket Nos. UE-991606 and UG-991607, Third Supp. Order at ¶ 34.
76/ WUTC v. PSE, Docket Nos. UE-011163 and UE-011170, Sixth Supp. Order at ¶ 36 (Oct. 4, 2001).
77/ Exh. No. 88 at 19: 4-5 (Widmer Direct).
78/ Id. at 19: 16 – 20:7.

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34 The same rationale applies to line losses. PacifiCorp's use of a single year to forecast line losses "has little value in determining likely future events."[79] Use of the most recent five years provides a more accurate portrayal of what level of line losses PacifiCorp is likely to experience in the future. PacifiCorp has not presented sufficient evidence to demonstrate that its forecasted line losses would be more accurate than normalized amounts. The Commission has normalized various aspects of the revenue requirement in the past, and there is no reason why the Commission should not do so with regard to line losses.[80] Applying ICNU's line loss adjustment would reduce PacifiCorp's revenue requirement by $0.64 million.[81]

3. Washington Ratepayers Should Benefit From the Low-Cost Wyoming Resources that Have Always Been Included in Rates

35 The Commission should adjust the WCA methodology to reflect the fact that the Wyoming generating resources (Dave Johnson and Wyodak) are used and useful to Washington. Mr. Falkenberg has provided the Commission with two potential adjustments to the WCA that could properly include the costs and benefits of these resources in Washington rates. At a minimum, the Commission should adopt a $3.8 million adjustment that would reflect the direct benefits of energy from these resources flowing to the western system.[82] In addition, Mr. Falkenberg has calculated an $8.2

79/ See WUTC v. Avista Corp., Docket No. UG-021584, Sixth Supp. Order at ¶ 66 (Feb. 13, 2004).

80/ See, e.g., WUTC v. PSE, Docket Nos. UE-060266 and UG-060267, Order No. 8 at ¶ 159 (Jan. 5, 2007) (weather normalization); WUTC v. Puget Sound Power & Light Co., Cause No. U-81-41, Second Supp. Order at 15-18 (Mar. 12, 1982) (hydro normalization).

81/ Exh. No. 161 at 5 (Falkenberg Direct).

82/ Id. at 2: 17-23, 5, 24: 8-17.

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million adjustment if the Commission fully incorporates all the former PP&L Wyoming loads and resources into rates.[83]

36 Both Dave Johnson and Wyodak were part of the pre-merger PP&L system and have been included in Washington rate base since they were first installed.[84] The starting point for the Commission's analysis of cost allocation issues has always been the pre-merger PP&L system, and PacifiCorp should have a heavy burden to exclude these resources from rates.[85] It is particularly inappropriate to have burdened Washington ratepayers with the high costs and risks associated with these resources during their early years and then remove them from rates now that they are low cost.

37 Power from these resources can be, and is, delivered to Washington ratepayers.[86] Although transmission constraints limit deliverability, "substantial amounts of power from [Dave] Johnson and Wyodak are delivered to" the western system.[87] PacifiCorp asserts that it is not possible to quantify how much energy is available from these resources because electrons are not "color coded," and that the power actually delivered to Washington may be from new Wyoming resources.[88] The Commission should reject these arguments because the Company assumes, without any proof, that Washington would be served by very recently built resources rather than those that have been included in rates for over thirty years.

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[83] Id. at 24: 18 – 25: 9.
[84] Id. at 22: 22 – 23: 1.
[85] Id. at 23: 2-6; Re PP&L, Docket No. U-87-1338-AT, Second Supp. Order at 13-14.
[86] Exh. No. 161 at 23: 12-20, 25: 19 – 26: 2 (Falkenberg Direct).
[87] Id. at 25: 19 – 26: 2.
[88] Exh. No. 88 at 25: 1-20 (Widmer Rebuttal).

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38 PacifiCorp also disagrees with the manner in which Mr. Falkenberg calculated his adjustment related to the Wyoming resources.[89] Again PacifiCorp makes unsupported assertions of "flaws" that go to the overall amount of the adjustment, but fails to recalculate the adjustment. For example, PacifiCorp asserts that the Wyoming adjustment was based on the wrong study and should have used monthly instead of annual prices.[90] Despite these assertions, PacifiCorp does not provide the "correct" study, nor does the Company recalculate the adjustment based on the "correct" study. If these criticisms were meritorious, then the Company should have provided supporting documentation and "corrected" values.

39 Staff also criticizes the proposal to include Dave Johnson and Wyodak and excluded the resources because they are outside of the western control area.[91] Staff agrees that these resources provide benefits to Washington, but disagrees about the manner in which Mr. Falkenberg calculated the Wyoming resources adjustment.[92] Staff, however, failed to make any proposals to allocate to Washington any of its share of the benefits of these resources.

C. The Commission Should Reject PacifiCorp's One-sided PCAM

40 In rejecting the PCAM in the Company's last rate case, the Commission explained that a PCAM should:

- Address short term cost changes that are caused by events beyond the Company's control;[93]

89/ Id. at 25: 21 – 26: 11.
90/ Id.
91/ Exh. No. 281 (Staff Response to ICNU DR 2.25).
92/ Exh. No. 274 (Staff Response to ICNU DR 2.16); Exh. No. 265 at 13: 10 – 15: 9 (Buckley Cross Answering).
93/ WUTC v. PacifiCorp, Docket Nos. UE-050684 and UE-050412, Order No. 4 at ¶¶ 91, 99.

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- Adjust the utility's cost of capital in a manner that reflects the shift risk between shareholders and ratepayers;[94]

- Have deadbands and sharing mechanisms that appropriately allocate risk and motivate management to mange and reduce power costs;[95] and

- Be based on an acceptable cost allocation methodology.[96]

41 PacifiCorp and Staff have proposed a highly flawed PCAM that does not comply with these requirements. PacifiCorp and Staff's PCAM inappropriately relies on fake or "pseudo" actual power costs, includes costs that are not beyond the Company's control, fails to strike a reasonable balance between ratepayers and shareholders, is based on an unproven and easily manipulated cost allocation methodology, and will likely result in an automatic $5 million rate increase. PacifiCorp even refuses to acknowledge that a PCAM should include a reduction in its cost of capital.

42 ICNU recommends that the Commission reject the proposed PCAM and reconsider the adoption of a PCAM in the next general rate case after the Commission has experience working with an appropriate cost allocation methodology. If the Commission wishes to adopt a PCAM, however, the Commission should adopt a hydro-only PCAM with an ROE adjustment to reflect the value of the risk that is shifted to ratepayers. A hydro-only PCAM would focus on those short-term costs beyond the Company's immediate control, and would avoid the problems caused by reliance upon pseudo actual results and an untested cost allocation methodology.

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[94] Id. at ¶¶ 91, 97.
[95] Id. at ¶¶ 91, 96, 99.
[96] Id. at ¶ 99.

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1. PacifiCorp's PCAM Is Not Based on Actual Expenses, But Upon an After the Fact Compilation of Fake Numbers

43 The proposed PCAM is highly capable of manipulation. Under the WCA, PacifiCorp has not developed a way to separate actual western power costs from its overall power costs.[97] Instead, the Company proposes to use a GRID model run to "manufacture pseudo-actual costs" that would be compared with normalized power costs in rates to produce its annual PCAM update.[98] There is no reason to believe that this will accurately reflect actual costs; instead, they will likely be similar to a movie "inspired by actual events" in which fact is sacrificed for fiction, or in this case to produce a desired end result.

44 PacifiCorp's WCA-only GRID model significantly overstates PacifiCorp's actual power costs. While PacifiCorp itself has not developed any analysis of actual western system power costs,[99] Mr. Falkenberg's analysis demonstrates that the WCA GRID model "consistently overstates power costs for the WCA . . . ."[100] Despite PacifiCorp's criticism, there remains the fundamental problem "that without some form of actual cost to compare the model against, there is no basis for assuming the model provides realistic results."[101]

45 The use of pseudo actual results for a PCAM is highly unusual and probably without precedent anywhere. PCAMs are typically based on actual costs, not a

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[97] Exh. No. 161 at 57: 8-12 (Falkenberg Direct).
[98] Id. at 57: 2-12, 59: 1-21.
[99] Id. at 12: 14-16, 57: 10-12; Exh. No. 172 at 6 (PacifiCorp Response to ICNU DR 1.27).
[100] Exh. No. 161 at 13: 10-12 (Falkenberg Direct).
[101] Id. at 57: 14-16.

"model fed with a veritable witches' brew of both actual and projected data . . . ."[102] In fact, the Oregon Public Utility Commission ("OPUC") recently rejected a similar type of mechanism that had been proposed by the OPUC Staff and Portland General Electric Company ("PGE").[103] Ratepayers should only be charged normalized projected costs reviewed in rate proceedings or verifiable actual costs subject to an appropriate review. It would be an inappropriate and highly questionable regulatory experience to charge ratepayers a "combination of some actual and some projected data plugged into an untested (and ever changing) model . . . ."[104]

2. PacifiCorp's PCAM Should Only Include Hydro Changes

46 Staff and PacifiCorp's proposed PCAM is not limited to rely only upon short-term items beyond PacifiCorp's control. The Commission has explained that a PCAM should address short-term cost changes that are "a result of abnormal weather conditions that are out of a utility's control"[105] and rejected PacifiCorp's PCAM because, in part, it did not focus on short-term costs that are beyond its control.[106]

47 The primary risk that is beyond the Company's control, and that potentially warrants inclusion in a PCAM, is changes in hydro conditions.[107] PacifiCorp has not presented sufficient evidence that demonstrates power cost volatility or any other short-term market changes are a significant problem.[108] PacifiCorp's fuel purchases in

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[102] Id. at 58: 11-18.
[103] Re PGE, OPUC Docket Nos. UE 165 and UM 1187, Order No. 05-1261 (Dec. 21, 2005).
[104] Exh. No. 161 at 59: 1-7 (Falkenberg Direct).
[105] WUTC v. PacifiCorp, Docket Nos. UE-050684 and UE-050412, Order No. 4 at ¶ 91; see WUTC v. Avista Corp., Docket Nos. UE-991606 and UG-991607, Third Supp. Order at ¶ 172 (Sept. 29, 2000).
[106] WUTC v. PacifiCorp, Docket Nos. UE-050684 and UE-050412, Order No. 4 at ¶ 99.
[107] Exh. No. 161 at 72: 1-18 (Falkenberg Direct).
[108] Id. at 63: 12 – 69: 16.

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the western system are under long-term contracts, far more stable than the market, and are not beyond the Company's control.[109] In addition, as PacifiCorp tends to purchase from the wholesale market in advance of its need and sell more power than it buys in the west, changes in short-term markets typically are not a problem.[110] Essentially, PacifiCorp has been able to successfully manage its power costs without a PCAM in Oregon, Washington, and Utah, and maintain favorable bond ratings;[111] thus, the Commission should reject PacifiCorp's attempt to use a PCAM to pass ordinary cost increases to Washington ratepayers outside of a general rate proceeding.

3. PacifiCorp's PCAM Includes an Inappropriate Deadband and Sharing Mechanism

48 PacifiCorp and Staff have proposed a deadband and sharing mechanism that unduly shifts risks to ratepayers. The Commission has recognized that deadbands and sharing mechanisms must be set to appropriately allocate risk and "to motivate management to effectively manage or even reduce power costs."[112] The goal of a PCAM should not be set simply to shift the risk of power cost changes from shareholders to ratepayers.[113] The Commission rejected PacifiCorp's previous PCAM because it did not adequately balance risks and benefits between shareholders and ratepayers.[114]

49 PacifiCorp, in rebuttal testimony, conditionally accepted Staff's proposed changes to the Company's deadband and sharing mechanism.[115] PacifiCorp appears to

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109/ Id. at 67: 1-9.
110/ Id. at 67: 10-24.
111/ Id. at 64: 7-20; Exh. No. 118 (S&P's: "PacifiCorp's $600 Million Bonds Are Rated 'A-'").
112/ WUTC v. PacifiCorp, Docket Nos. UE-050684 and UE-050412, Order No. 4 at ¶ 96.
113/ WUTC v. Avista, Docket Nos. UE-991606 and UG-991607, Third Supp. Order at ¶ 185.
114/ WUTC v. PacifiCorp, Docket Nos. UE-050684 and UE-050412, Order No. 4 at ¶ 99.
115/ Exh. No. 88 at 42: 23 – 43: 9 (Widmer Rebuttal).

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now be proposing a PCAM with a $4 million deadband, 50/50 sharing between $4 million and $10 million, and an allocation of 90% of costs above $10 million to ratepayers.[116/] Staff originally supported its $4 million deadband (an increase from PacifiCorp's original $3 million deadband) based on a concern with the use of pseudo actual instead of actual power costs.[117/] Both PacifiCorp and Staff also support their proposed deadband and sharing mechanism because they are similar to Avista's.[118/]

50 PacifiCorp's different circumstances militate strongly in favor of a larger deadband and sharing mechanism than Avista. The Commission recognized that PacifiCorp faces different risks than Avista, "which may suggest a differently structured PCAM."[119/] Not only does Avista have a different power supply portfolio, but the Avista PCAM was adopted pursuant to an all party settlement and at a time when the utility was in serious financial difficulties.[120/] Even ignoring the different context, Avista's PCAM is significantly different because it does not rely upon pseudo actual results. To address Staff's "concern" about using "a model to determine actual power costs,"[121/] PacifiCorp's PCAM should have a much larger deadband and sharing mechanism.

51 Use of PacifiCorp and Staff's proposed deadband and sharing mechanism will likely also result in double recovery by PacifiCorp. Mr. Falkenberg and Mr. Buckley have proposed nearly identical water year adjustments, which will remove from base net power costs all water years that exceed one standard deviation on each side of the normal

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116/ Id. at 41: 8 – 43: 9; Exh. No. 261 at 39: 18-22 (Buckley Direct).
117/ Exh. No. 261 at 40: 8-20 (Buckley Direct).
118/ Id. at 41: 17-21; Exh. No. 88 at 44: 7-12, 45: 4-6 (Widmer Rebuttal).
119/ WUTC v. PacifiCorp, Docket Nos. UE-050684 and UE-050412, Order No. 4 at ¶ 93.
120/ Exh. No. 161 at 65: 1-18 (Falkenberg Direct); WUTC v. Avista Corp., Docket No. UE-011595, Fifth Supp. Order at ¶¶ 6-7 (June 18, 2002).
121/ Exh. No. 261 at 40: 15-20 (Buckley Direct).

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distribution of water generation.[122] If the Commission adopts this adjustment, then base rates will be set excluding the costs of water years more than one standard deviation from the norm. A one standard deviation in hydro generation levels is equal to an $8.6 million change in power costs to Washington.[123] Therefore, to reflect the amount of hydro variability assumed in rates, any deadband should be at least $8.6 million.

4. PacifiCorp and Staff's PCAM Will Automatically Increase Rates $5 Million Next Year

52 PacifiCorp and Staff's PCAM should also be rejected because it is likely to result in an automatic $5 million rate increase. Due to the expiration of the TransAlta contract, PacifiCorp's PCAM will result in "a $5 million net increase to Washington, everything else being equal."[124] Ratepayers should not have to shoulder the increased costs associated with new contracts or cost increases like the expiration of the TransAlta contract outside of a general rate case.

5. ICNU's Hydro-Only PCAM Is the Only Reasonable PCAM

53 ICNU's has proposed a hydro-only PCAM to provide the Commission a realistic option if it wishes to adopt to a PCAM. ICNU's proposed PCAM would not require a determination of PacifiCorp's pseudo actual costs, but address Washington's share of the variances in hydro costs.[125] These costs can be tracked without the need to resolve jurisdictional allocation issues or constructing pseudo actual power costs.[126] ICNU's proposal also meets the Commission's announced standards because it is limited

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[122] Id. at 22-25 (Buckley Direct); Exh. No. 161 at 41- 47: 11 (Falkenberg Direct).

[123] Exh. No. 161 at 66: 4-6 (Falkenberg Direct); Exh. No. 170 (Sensitivity of PacifiCorp Washington NPC).

[124] Exh. No. 161 at 68: 13-21 (Falkenberg Direct).

[125] Id. at 71: 1-12.

[126] Id. at 71: 4-5.

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to only those short-term weather-related costs that are not controllable by the Company.[127]

The deadband and sharing mechanism of ICNU's hydro-only PCAM are reasonable and consistent with normalized rates. The deadband would be $8.6 million (one standard deviation in hydro variation), which is the amount of hydro variability that would be set in rates under the water year adjustment of Messrs. Buckley and Falkenberg.[128] ICNU proposes that shareholders and ratepayers share evenly between variations between $8.6 million and $17.2 million (between one and two standard deviations), and ratepayers shoulder 85% of the costs of hydro variations above $17.2 million.[129] This would provide PacifiCorp with protection from abnormal hydro conditions, but continue to motivate the Company to effectively manage or even reduce power costs.

6. The Commission Should Adopt an ROE Adjustment if it Adopts ICNU's Hydro-Only PCAM

54 PacifiCorp's ROE should be reduced by 0.3% if the Commission adopts ICNU's proposed hydro-only PCAM.[130] The Commission concluded that if a PCAM is adopted, then "[r]atepayers should receive the benefit of a reduction in cost of capital, as a power cost adjustment introduces rate instability for ratepayers and earnings stability for stockholders . . . ."[131] The evidence in the record supports the Commission's

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[127] Id. at 72: 1-11.
[128] See id. at 66: 3-15, 71: 16-19.
[129] Id. at 71: 13-23; Exh. No. 171 (Hydro Hedge PCAM Illustration of Payments and Credits).
[130] Exh. No. 181 at 1: 21 – 3: 8 (Gorman Direct); Exh. No. 161 at 70: 7-12 (Falkenberg Direct).
[131] WUTC v. PacifiCorp, Docket Nos. UE-050684 and UE-050412, Order No. 4 at ¶ 91.

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conclusion that implementation of a PCAM will reduce the risks to shareholders and shift power cost volatility risk to customers.[132/]

55 ICNU's proposed ROE adjustment "is based on an assessment of reduced capital cost recovery risk demanded by the market" if ICNU's PCAM is adopted.[133/] If the Commission adopts PacifiCorp's PCAM, then a larger cost of capital adjustment should be made.[134/] ICNU witness Michael Gorman calculated the value of this risk based on an "assessment of the marketplace of the difference in valuation of utility bonds that takes place for differences in credit quality."[135/] Mr. Gorman based this risk on the differential between a single "A" utility bond and a triple "B" utility bond.[136/] PacifiCorp agrees that Mr. Gorman "correctly measures the recent 'A'/'BBB' spread for utility bonds . . . ."[137/]

56 Although the calculation of the change in bond ratings must be based on the Company's total financial position, Mr. Gorman's adjustment only impacts the Company's Washington ROE.[138/] This is appropriate because the adjustment reflects the impact on the Company's Washington operations based on a Washington–only hydro PCAM. Thus, this adjustment is very modest.

132/ TR 301: 8-23; Exh. No. 181 at 2: 15- 23 (Gorman Direct); Exh. No. 294 at 1-3 (Elgin Cross Answering); Exh. No. 161 at 72: 2-11 (Falkenberg Direct).

133/ Exh. No. 181 at 2: 26 – 3: 1 (Gorman Direct); Exh. No. 161 at 70: 2-12 (Falkenberg Direct).

134/ Exh. No. 294 at 2: 13-16 (Elgin Cross Answering).

135/ TR. 301: 18 – 302: 10 (Gorman); Exh. No. 181 at 2: 23 – 3: 8 (Gorman Direct).

136/ Exh. No. 181 at 3: 1-8 (Gorman Direct); TR 302: 6-10 (Gorman).

137/ Exh. No. 51 at 13: 23 – 14: 2 (Hadaway Rebuttal).

138/ Exh. No. 181 at 1: 21-24 (Gorman Direct).

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57 PacifiCorp argues that the Commission should not adjust its ROE because an ROE adjustment was not adopted in some past proceedings approving PCAMs.[139/] This position ignores the Commission's direction in the last general rate case requesting that there should be a cost capital adjustment based on "how the mechanism shifts risks between investors and ratepayers."[140/] PacifiCorp also fails to note that its circumstances are dramatically different from Avista and PSE, whose PCAMs were adopted with the support of customers and at a time when the utilities were experiencing serious financial difficulties.[141/]

58 PacifiCorp also argues that an ROE adjustment should be rejected because most of the utilities in the proxy group used to estimate the Company's ROE have fuel or purchased power adjustment mechanisms.[142/] The Commission should reject this argument because the proxy group "was based on PacifiCorp's risk that existed at that time, which did not include a fuel adjustment mechanism."[143/] The fact that many of the proxy group utilities had fuel adjustment clauses is less important than that "they had other risk factors which PacifiCorp did not have . . . [and] when you mix them all together, the proxy group as a whole had comparable risk to PacifiCorp."[144/] The Commission approved an overall ROE for PacifiCorp in its last proceeding based on the then current market and PacifiCorp's risks, which included power cost volatility, and

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139/ Exh. No. 51 at 12: 8-11 (Hadaway Rebuttal).
140/ See WUTC v. PacifiCorp, Docket Nos. UE-050684 and UE-050412, Order No. 4 at ¶ 97.
141/ Exh. No. 161 at 65: 1-18 (Falkenberg Direct).
142/ Exh. No. 51 at 12: 12-16 (Hadaway Rebuttal).
143/ TR 303: 24 – 304: 3 (Gorman Cross Exam).
144/ Id. at 304: 4-8 (Gorman).

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PacifiCorp would be overcompensated if it was allowed to shift some of those risks to customers without a corresponding reduction in its cost capital.

D. PacifiCorp's Revenue Requirement Request Is Significantly Overstated

1. PacifiCorp's Power Costs Should Be Reduced

59 The testimony of Mr. Falkenberg, ICNU and Public Counsel's power cost witness, demonstrates that the Company's $417 million net power costs should be reduced by approximately $64 million, resulting in a Washington revenue requirement reduction of about $14 million.[145/] For its part, Staff proposes less than $0.5 million in non-duplicative power cost adjustments,[146/] even though this is the first time the Company's power costs will be set since before the PP&L and UP&L merger.

a. PacifiCorp's GRID Model Improperly Accounts for the Company's Short-Term Sales

60 The Commission should remove PacifiCorp's short-term firm transactions from rates because GRID fails to properly account for them. In addition, many of these transactions are below market and have not been shown to be prudent. Removing the short-term firm transactions would reduce the revenue requirement by $7.9 million.[147/]

61 PacifiCorp's GRID model includes two types of short-term transactions. There are firm purchased sales contracts with a term of less than one year which are not forecast or simulated. These purchased sales contracts are a fixed input with pre-determined energy volumes and prices. GRID also includes secondary balancing

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[145/] Exh. No. 161 at 5 (Falkenberg Direct).

[146/] Exh. No. 263 (Summary of Net Power Supply Expense Adjustments). Mr. Buckley's $0.48 million in miscellaneous power supply adjustments are not prudency issues, but primarily related to adjusting net power costs to comply with the WCA methodology. Exh. No. 261 at 20: 13 – 21: 19 (Buckley Direct).

[147/] Exh. No. 161 at 5 (Falkenberg Direct).

transactions (hour-to-hour trades) which are simulated when the model sells or purchases these transactions based on the forward price curve.[148/]

62 Ratepayers are harmed because the Company uses a biased sample of short-term firm transactions for the test period which includes a large amount of below-market transactions and excludes many potentially profitable sales. PacifiCorp only includes the trades it had arranged at the time it filed its case, and this results in the exclusion of numerous transactions.[149/] This fails to recognize that PacifiCorp can "make profitable trades in the future," and prevents power costs from being reduced due to "the additional benefits of a better balancing of the system and the numerous profit opportunities that the Company's traders will strive to exploit . . . ."[150/] Essentially, PacifiCorp's modeling of the short-term firm transactions would set normalized rates on the unrealistic assumption that unanticipated market fluctuations always cause the Company to have more below-market transactions than above-market sales.[151/]

63 PacifiCorp also has failed to demonstrate the prudence of its below-market short-term transactions. PacifiCorp may have made many of these "transactions well in advance of the time necessary, with the net effect being to place the Company in a position of betting on a decline in market prices, which never materialized."[152/] PacifiCorp supported the prudence of these transactions with the conclusory statement that "[t]he transactions were unquestionably prudent because they were entered at then

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148/ Id. at 29: 4-12.
149/ Id. at 29: 14 – 30: 8.
150/ Id. at 31: 1-8.
151/ Id. at 31: 10-19.
152/ Id. at 30: 16-23.

prevailing market prices to balance and optimize the WCA."[153/] The Company refused to provide any actual data, evidence, or analysis to support this conclusion, merely stating that "[g]iven the number of transactions involved, the supporting data are too voluminous to provide."[154/] This is insufficient evidentiary support to justify the prudence of the below-market transactions. Even if the transactions were not below market, PacifiCorp has not justified the need for the trades, or why it was necessary to expose ratepayers to the risk of entering into them far in advance of the time they were needed.

64 ICNU proposes that the Commission correct this problem by removing all short-term transactions and pricing system balancing at the forward curve price.[155/] PacifiCorp argues that this is unrealistic, but the Company does not propose a different solution to remedy the problems with the GRID model's accounting for short-term firm transactions.[156/] PacifiCorp also fails to recognize that the GRID model already prices much of the system's other balancing requirements on the forward price curve.[157/] PacifiCorp essentially criticizes ICNU for treating all the short-term transactions how the Company already treats most of them.

b. The Commission Should Remove the Imprudent SMUD Contract from Rates

65 The Commission should disallow the entire contract between PacifiCorp and SMUD, because the contract was imprudent and ratepayers did not receive any

153/ Exh. No. 88 at 30: 14-16 (Widmer Rebuttal).
154/ Exh. No. 505 (PacifiCorp response to ICNU DR 8.41).
155/ Exh. No. 161 at 32: 9-18 (Falkenberg Direct).
156/ See Exh. No. 88 at 30: 5-13 (Widmer Rebuttal).
157/ Exh. No. 161 at 32: 14-18 (Falkenberg Direct).

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benefit from the bargain. Removing the SMUD contract from rates would reduce PacifiCorp's revenue requirement by approximately $2.77 million.[158/]

66 PacifiCorp and SMUD entered into a 30-year contract in 1987 that obligated PacifiCorp to serve SMUD at $16.85 per MWh, which was "a rate much lower than the then-current rate for power."[159/] In exchange for entering into this below market contract, PacifiCorp received an upfront payment of $94 million from SMUD that the Company "retained and was not used to benefit ratepayers."[160/]

67 PacifiCorp agrees that the contract was below market when signed and that the original contract price should not be used. In this proceeding, PacifiCorp has proposed to impute the $16.85 per MWh price in the SMUD contract with a $37 per MWh price based on a 20-year contract with Southern California Edison ("SCE").[161/] PacifiCorp justifies revenue imputation based on the SCE contract because it was signed about the same time as the SMUD contract.[162/]

68 It would not be proper to impute revenue based on the SCE contract because the two contracts were executed for significantly different terms.[163/] While the $37 per MWh price may be reasonable for a contemporaneous 20-year contract, there is no evidence that the price would be reasonable for a more risky 30-year contract. The Commission should simply remove the SMUD contract and make PacifiCorp solely

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158/ Id. at 5.

159/ Re PacifiCorp, Utah Public Service Commission Docket No. 01-035-01, Report and Order at 24-25 (Sept. 10, 2005); Exh. No. 88 at 31: 14-20 (Widmer Rebuttal).

160/ Re PacifiCorp, Utah Public Service Commission Docket No. 01-035-01, Report and Order at 24-25.

161/ Exh. No. 88 at 31: 1 – 33: 2 (Widmer Rebuttal).

162/ Id. at 32: 1-3.

163/ Exh. No. 161 at 34: 21-25 (Falkenberg Direct).

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responsible for signing a below-market contract in exchange for a large up-front cash payment that was never shared with ratepayers.

c. PacifiCorp Shared the Benefits of the Centralia Sale and Should Now Share the Costs of Replacement Power

69 The Commission should reduce power costs to reflect the risk PacifiCorp accepted when it sold the Centralia plant to TransAlta. ICNU proposes that 50% of the costs of replacement power for Centralia be allocated to PacifiCorp to reflect the fact that PacifiCorp retained 50% of the appreciation of the investment in Centralia.[164/] This adjustment would reduce the Company's revenue requirement by $1.78 million.[165/] PacifiCorp opposes the adjustment, but offers an alternative adjustment that would allocate 12.5% of the costs of replacement power to the Company.[166/]

70 In 1999, PacifiCorp decided to sell its approximately one-half interest in the Centralia plant to TransAlta. The sale of Centralia has been a substantial factor in the Company's need to purchase power and without the sale "the Company would have had more than enough energy to meet its native system requirements with low-cost coal and hydro generation."[167/] At the time, PacifiCorp's risk analysis showed that retaining Centralia would be preferable to market.[168/]

71 The Commission, in approving the Centralia sale, concluded that the risks and burdens associated with the plant were borne by both shareholders and ratepayers.[169/]

[164/] Id. at 39: 14-24.
[165/] Id. at 5.
[166/] Exh. No. 136 at 21: 6-14 (Wrigley Rebuttal).
[167/] Exh. No. 161 at 36: 24 – 37: 2 (Falkenberg Direct).
[168/] Id. at 37: 9-15.
[169/] Re Avista Corp., Docket Nos. UE-991255, UE-991262, and UE-991409, Second Supp. Order at ¶¶ 84-85 (Mar. 6, 2000).

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The Commission returned the net book value to shareholders, the remainder up to original cost to ratepayers, and evenly split the appreciation between ratepayers and shareholders.[170/] The Commission based this sharing upon the conclusion that "both ratepayers and shareholders have and will incur risks and burdens."[171/] The Commission adopted a policy that risk should follow the reward, and found that ratepayers and shareholders would share the risks associated with the sale.[172/]

72 PacifiCorp retained half the appreciation from the sale of Centralia and should bear half the risk of not replacing the power and relying on market purchases. If the Commission does not apportion some of the replacement power costs associated with the Centralia sale, then ratepayers "will have been given 50% of the appreciation on the sale, but bear 100% of the risks."[173/]

73 ICNU's position is consistent with how the Wyoming Public Service Commission addressed the issue of replacement power for Centralia. The Wyoming Commission adopted an adjustment that reflects "the fact that it would be unreasonable for ratepayers to absorb all of the risk of replacing Centralia-related power after the Commission ordered a sharing of risk with respect to the Centralia sale transaction which allocated 64% of the gain to ratepayers and 36% to PacifiCorp shareholders."[174/] The same reasoning applies in this proceeding.

170/ Id. at ¶ 7.
171/ Id. at ¶ 84 (emphasis added).
172/ Exh. No. 161 at 38: 15-23 (Falkenberg Direct).
173/ Id. at 39: 17-20.
174/ Re PacifiCorp, Wyoming Public Service Commission Docket No. 20000-ER-02-184, Final Order at ¶¶ 192(d), 206 (Mar. 6, 2003).

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74 Although PacifiCorp proposes that ratepayers would bear the burden of 100% of the market risks associated with the Centralia sale, the Company did not submit testimony supporting its position.[175] Instead of responding to the merits of whether an adjustment should be made, the Company proposes that it should be based on the overall gain that was allocated to ratepayers.[176] According to the Company, 87.5% of the total gain was allocated to ratepayers.[177] While this proposal ignores that the Commission only adopted a risk sharing methodology for the appreciation of the sale (which was split 50/50),[178] it would at least recognize that it would be unreasonable "to shield the Company from all of the risks of its controversial decision to sell the plant."[179]

d. The Commission Should Continue to Set PacifiCorp's Rates Based on "Filtered" Water Years

75 PacifiCorp's hydro modeling should be modified to exclude water years that result in power costs that are more than one standard deviation from the mean because the Company will seek to recover these costs in a PCAM or power cost deferral. ICNU and Staff have independently proposed the same hydro modeling adjustment, which would reduce rates by approximately $1.5 million.[180] PacifiCorp has proposed a

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[175] In rebuttal testimony, Mr. Wrigley testifies that PacifiCorp is opposed to the Centralia sale adjustment, but he does not provide the basis for the Company's opposition, merely stating that "Mr. Widmer in his testimony demonstrates why this adjustment is inappropriate." Exh. No. 136 at 21: 15-17 (Wrigley Rebuttal). Neither Mr. Widmer nor any other PacifiCorp witness provides any testimony or other evidence on this issue. PacifiCorp cannot meet its burden of proof by making up for this evidentiary short fall through creative briefing or other measures.

[176] Exh. No. 136 at 21: 6-14 (Wrigley Rebuttal).

[177] Id.

[178] Re Avista Corp., Docket Nos. UE-991255, UE-991262, and UE-991409, Second Supp. Order at ¶¶ 84-86.

[179] Exh. No. 161 at 38: 21-23 (Falkenberg Direct).

[180] Id. at 5; Exh. No. 261 at 25: 17-20 (Buckley Direct); Exh. No. 88 at 34: 2-5 (Widmer Rebuttal).

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40-year water study to set normalized power costs in this proceeding.[181] ICNU and Staff have proposed that the Commission remove "extraordinary" water years, which are defined as more than one standard deviation from the mean annual generation.[182] This adjustment is described as "filtering" the water years to remove extreme dry or wet years.[183] These extraordinary water years should be excluded because they would likely be captured in a PCAM or power cost deferral.[184]

76 PacifiCorp agrees that a water year adjustment should be made, but only if the Commission adopts a PCAM.[185] PacifiCorp also proposes modifications that would reduce the adjustment to a $0.6 million revenue requirement reduction.[186] The water year adjustment is appropriate even without a PCAM, as PacifiCorp's current rates were set based upon the inclusion of this type of water year adjustment.[187] The water year adjustment is reasonable because PacifiCorp will likely request a power cost deferral during poor water years and is unlikely to request a power cost deferral during good water years. For example, PacifiCorp was granted a power cost deferral based on poor water conditions last year.[188] Without the water year adjustment, customers will be required to pay for poor hydro conditions twice—once in rates and once after the power

181/ Exh. No. 161 at 42: 8-9 (Falkenberg Direct).
182/ Id. at 42: 13-18, 44: 10-18; Exh. No. 261 at 22-25 (Buckley Direct).
183/ Exh. No. 261 at 24: 1-20 (Buckley Direct).
184/ Exh. No. 161 at 42: 13 – 44: 24 (Falkenberg Direct); Exh. No. 261 at 22-25 (Buckley Direct).
185/ Exh. No. 88 at 34: 13-18 (Widmer Rebuttal).
186/ Id. at 8: 16-18.
187/ See WUTC v. PacifiCorp, Docket No. UE-032065, Order No. 6 Appendix A at Attachment B (Oct. 27, 2004); Exh. No. 161 at 42: 13 – 44: 9 (Falkenberg Direct).
188/ WUTC v. PacifiCorp, Docket Nos. UE-050684 and UE-050412, Order No. 4 at ¶¶ 312-13.

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cost deferral—if power costs are set based on the assumption that good and bad hydro years will occur, but PacifiCorp obtains a deferral when poor water conditions occur.[189/]

77 PacifiCorp proposes to reduce the value of the water year adjustment because the adjustment assumes that the Company will experience better than normal hydro conditions 59% of the time.[190/] This is not a basis to modify the water year adjustment as the Company's original proposed 40-year water study assumed that better than normal water conditions would occur the majority (52.5%) of the time.[191/] In addition, the adoption of PacifiCorp's adjustment would allow the Company to double recover these costs through both base rates and a PCAM or deferral.

e. PacifiCorp Should Not Be Permitted to Artificially Increase Its Outage Rates

78 The Commission should reject PacifiCorp's proposal to create "phantom outages" in GRID to increase rates.[192/] Elimination of PacifiCorp's phantom outages would reduce Washington net power costs by $0.26 million.[193/]

79 PacifiCorp asserts that GRID produces an excess of coal fired generation and that the availability of coal resources should be reduced.[194/] PacifiCorp's claims that the alleged excess generation is caused by ramping down coal generation for maintenance and ramping up after maintenance.[195/] This assertion, however, is not supported by any

189/ Exh. No. 161 at 44: 19 – 47: 11 (Falkenberg Direct).
190/ Exh. No. 88 at 6: 5 –7: 5 (Widmer Rebuttal).
191/ See id. at 7: 1-2.
192/ Exh. No. 161 at 51: 1-8 (Falkenberg Direct).
193/ Id. at 5.
194/ Exh. No. 88 at 36: 21 – 38: 15 (Widmer Rebuttal).
195/ Id. at 37: 12 –38: 3.

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studies or other factual evidence.[196] The Company's proposal to artificially increase its outage rates should be rejected because it is extremely unusual, contrary to standard industry practice, and inconsistent with the North American Electric Reliability Council's standard formula for computation of forced outages.[197]

f. PacifiCorp's Departure from Historic Regulating Margins Is Not Based on Changes in Actual Operations

80 The Commission should reject PacifiCorp's proposal to increase the maximum regulating margin requirements from 125 MWs to 225 MWs. Rejection of PacifiCorp's change to the regulating margins in GRID would reduce the Company's filed Washington revenue requirement by about $0.19 million.[198] In the past, PacifiCorp's GRID model has consistently assumed regulating margins of 125 MWs because the Company's actual regulating margin is only 125 MWs.[199] PacifiCorp justifies an increase in regulating margin requirements on a study performed by the Company; however, the study only changes the methodology used to analyze the requirements and does not imply any changes in actual operations.[200] PacifiCorp's change should be rejected because the Company has not shown that its maximum regulating margin has increased.

g. The Output from the GP Camus Contract Should Reflect the Amount of Power PacifiCorp Expects to Receive

81 The Commission should reduce net power costs by $30,952 to account for PacifiCorp's overstatement of the generation purchased from the Georgia Pacific ("GP")

196/ See id.
197/ Exh. No. 161 at 51: 12-19 (Falkenberg Direct).
198/ Id. at 5.
199/ Id. at 53: 7-22.
200/ See Exh. No. 88 at 39: 10 – 40: 18 (Widmer Rebuttal).

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Camus contract.[201] The Commission should make this adjustment because generation from this project has been steadily declining for the past several years.[202] PacifiCorp admits that generation has been declining from this project, but asserts that the decline has stabilized.[203] PacifiCorp has not provided any reason as to why it believes this generation has stabilized, or any factual proof that the generation has in fact stabilized; thus, there is no reason to assume that the decline in generation output will cease.

2. Ratepayers Should Not Be Responsible for Excessive Utility Bonuses

82 The Commission should reduce PacifiCorp's excessive incentive compensation for its employees by excluding 100% of the executive incentive costs and 50% of the non-executive incentive compensation.[204] Adopting ICNU's incentive compensation adjustment would reduce PacifiCorp's revenue requirement by $2.0 million,[205] and is consistent with the Commission's concern that "in this era of substantially escalating executive compensation we are obligated to consider how much the ratepayers of a regulated monopoly should be required to pay."[206]

83 The Commission has concluded that it will only allow incentive compensation when the total overall compensation is reasonable and the incentives provide benefits to ratepayers.[207] PacifiCorp's incentive compensation does not meet this standard and should be reduced because it is "tied to corporate or business

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201/ Exh. No. 161 at 5, 40: 14-21 (Falkenberg Direct).
202/ Id. at 40: 14-21.
203/ Exh. No. 88 at 33: 3-22 (Widmer Rebuttal).
204/ Exh. No. 201C at 10: 12-16 (Iverson Direct).
205/ Id. at 11: 5-10; Exh. No. 211 (PacifiCorp Incentive Compensation Adjustment).
206/ See WUTC v. PSE, Docket Nos. UE-060266 and UG-060267, Order No. 8 at ¶ 97.
207/ WUTC v. PacifiCorp, Docket Nos. UE-050684 and UE-050412, Order No. 4 at ¶ 128; U.S. West, 134 Wn.2d 126-27 (Court upheld WUTC's exclusion of non-beneficial bonuses from rates).

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performance."[208/] A reduction is appropriate because "[s]hareholders, not ratepayers, benefit from incentives related to the utility's financial performance."[209/] Additional evidence that these bonuses are unreasonable and do not benefit ratepayers is that the Company provided approximately $1.6 million for its top nine executives.[210/] Ratepayers should not be responsible for these excessive bonuses.

84 PacifiCorp's base pay also provides adequate compensation and the Company does not need to provide bonuses to attract quality employees. According to PacifiCorp, its employees are provided with competitive base pay.[211/] In this proceeding, however, PacifiCorp tells a different story and alleges that its incentives are not "bonuses," but simply part of an overall compensative level.[212/] Apparently, PacifiCorp entices prospective employees with claims that its base pay is competitive, but then makes different claims in this case to meet the Commission's standards for incentive compensation recovery. The Commission should reject this after the fact characterization because other PacifiCorp materials state that its base salary is competitive and that incentive payments are in fact "bonuses."[213/] Therefore, PacifiCorp's overall compensation is unreasonable since the bonuses are not needed to provide competitive pay.

208/ Exh. No. 201C at 10: 23 – 11: 1 (Iverson Direct).
209/ Id. at 11: 1-2.
210/ Id. at 10: 8-22; Exh. No. 210 (PacifiCorp Response to ICNU DR 3.6).
211/ Exh. No. 124 (PacifiCorp Compensation and Benefits).
212/ Exh. No. 121 at 3: 5-8 (Wilson Rebuttal).
213/ Exh. No. 124 (PacifiCorp Compensation and Benefits); Exh. No. 139C (Confidential PacifiCorp Response to ICNU DR 1.84).

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3. PacifiCorp's Pension Expenses Should Be Reduced to Account for the Company's Cost Reduction Plans

85 PacifiCorp's pension expense should be adjusted to reflect the fact that the Company has recently made changes to its traditional defined benefit pension plan in order to reduce its costs.[214/] As PacifiCorp has not provided details of its new pension expenses, ICNU proposes that pension expenses should be based on the normalized average of FY 2005 and FY 2006, which "makes some recognition that pension expenses should be lower going forward and especially when the rates being developed in this proceeding will be in place."[215/] ICNU's pension adjustment would reduce the Company's revenue requirement by approximately $0.9 million.[216/]

86 PacifiCorp and Staff argue against making an adjustment for pension expenses because the Company did not provide the parties with the exact details of its new pension plan.[217/] PacifiCorp and Staff assert that ICNU's pension adjustment is not "known and measurable" because PacifiCorp has not provided the specific amounts that will be saved under its new pension plan.[218/] This argument fails to acknowledge that the pension expenses included in the Company's filing are incorrect because it is changing its pension plan to reduce costs.[219/] Thus, the change in pension expenses is a known and measurable event, and the only known fact is that the amount PacifiCorp proposes to include in rates is too high. Ratepayers should not be required to pay higher pension

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214/ See Exh. No. 201C at 9: 7-11 (Iverson Direct); Exh. No. 208 at 1 (PacifiCorp Response to ICNU DR 6.2).
215/ Exh. No. 201C at 9: 21 – 10: 2 (Iverson Direct).
216/ Id. at 10: 3-6.
217/ See Exh. No. 321 at 8: 1-13 (Schooley Cross Answering); Exh. No. 136 at 19: 17-20 (Wrigley Rebuttal).
218/ Exh. No. 321 at 8: 1-13 (Schooley Cross Answering); Exh. No. 136 at 19: 17-20 (Wrigley Rebuttal).
219/ Exh. No. 201C at 9: 6-17 (Iverson Direct).

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expenses than the Company will actually incur merely because it has decided not to provide sufficient cost information.

4. PacifiCorp's Shareholders Should Be Required to Bear a Portion of the Costs of Its Gold-Plated Medical Plan

87 The Commission should adjust PacifiCorp's medical costs to reflect industry averages because ratepayers should not be required to pay for overly generous medical benefits. If PacifiCorp wishes to provide gold-plated medical coverage for its employees, then shareholders—not ratepayers—should be required to pay for these extra costs. Adjusting PacifiCorp's medical expense to ensure it is more consistent with industry averages would result in a $0.3 million revenue requirement reduction.[220/]

88 PacifiCorp's rates assume that its employees will make medical cost contributions far below industry averages. PacifiCorp's filed medical costs are based on the Company's non-union employees contributing from 10-20% of medical costs and union employees contributing between 10-12.5%.[221/] In contrast to PacifiCorp's generous medical program, industry averages show that employees pick up approximately 20-25% of medical costs.[222/] PacifiCorp's rates should be set based on the assumption of 22% employee contributions because "PacifiCorp's ratepayers should not be expected to shoulder more of the Company's medical costs than the average contribution made by other competitive companies across the U.S."[223/]

220/ Id. at 3, 12: 18-25.
221/ Id. at 11: 15-20; Exh. No. 212 (PacifiCorp Response to ICNU DR 6.3).
222/ Exh. No. 201C at 11: 21 – 12: 13 (Iverson Direct).
223/ Id. at 12: 15-17.

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5. Taxes That Are Never Paid to Taxing Authorities Should Not Be Collected in Rates

89 The Commission should reduce PacifiCorp's revenue requirement by $3.0 million to remove the taxes that will be collected from Washington ratepayers but never actually paid to the taxing authorities. The taxable income of PacifiCorp on a stand alone basis is offset by the debt interest on the debt capital used by MEHC to fund its investment in PacifiCorp's common stock.[224/] Because PacifiCorp's taxes are filed on a consolidated basis, the income taxes that PacifiCorp collects from ratepayers is never actually paid to the taxing authorities and would represent a windfall to the Company's shareholders if ICNU's adjustment is not adopted.

a. Regulatory Principles Dictate That Amounts for Income Taxes Not Owing to Taxing Authorities Should Not Be Included in Rates

90 PacifiCorp argues that charging ratepayers for taxes that are never paid is "cost-justified," and that ICNU's adjustment seeks to obtain the benefit of MEHC's capital structure without assuming any of the risk.[225/] To the contrary, ICNU's proposed tax adjustment is intended to allow PacifiCorp to recover only those expenses that it actually incurs, and in no way reflects the business risks assumed by any other affiliated company.

91 ICNU's proposed adjustment accounts for the interest expense experienced as a result of financing the acquisition of PacifiCorp by MEHC. PPW Holdings LLC ("PPW") currently owns PacifiCorp and provides ring fence protections to

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224/ Exh. No. 181 at 3: 12-19 (Gorman Direct).
225/ Exh. No. 21 at 10: 9-20 (Evans Rebuttal).

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protect ratepayers from the activities of unregulated affiliates.[226/] PPW, however, receives all of its capitalization from MEHC; therefore, MEHC owns 100% of the common equity in PacifiCorp. The debt portion of this capital structure creates interest deductions that ultimately reduce the tax payable on PacifiCorp's taxable income.[227/]

92 Imputing to PacifiCorp the debt interest expense of $5.5 million that MEHC incurs as a result of MEHC's investment in PacifiCorp's common equity, PacifiCorp's income tax expense increases by $0.7 million.[228/] Consequently, PacifiCorp's rate of return increases to 5.8%. Using the 5.8% rate of return to recalculate PacifiCorp's revenue deficiency reduces PacifiCorp's claimed revenue requirement by approximately $3 million.[229/]

93 Without ICNU's proposed adjustment, PacifiCorp would be collecting in rates amounts that do not constitute a cost of providing utility service and provide no benefits to customers.[230/] Ratepayers should not be required to pay taxes that are not part of PacifiCorp's actual cost of service. Because taxes are costs, if a utility pays income taxes, it generally can recover from ratepayers the amount of the taxes paid.[231/] When a utility is part of a consolidated group, and the members of the group file a consolidated return, if "the out-of-pocket tax cost of the regulated affiliate is reduced, there is an

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226/ Exh. No. 181 at 4: 21-22 (Gorman Direct).
227/ Id. at 4: 22-25.
228/ Id. at 6: 16-22; Exh. No. 184 at 3 (Income Tax Expense Adjustment).
229/ Exh. No. 181 at 7: 2-7 (Gorman Direct); Exh. No. 184 at 2 (Income Tax Expense Adjustment).
230/ Exh. No. 181 at 7: 11-19 (Gorman Direct).
231/ BP W. Coast Prods., LLC v. FERC, 374 F.3d 1263, 1286 (D.C. Cir. 2004).

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immediate confrontation with the ratemaking principle that limits cost of service to expenses actually incurred."[232/]

94 The argument that these costs are cost justified[233/] has been rejected by the U.S. Supreme Court.[234/] The Court held that tax savings resulting from applying non-jurisdictional losses to jurisdictional income in a consolidated return may be used to reduce a utility's cost of service, "even if on a consolidated bases system losses exceed system gains and neither the affiliated group nor any member in it has any tax liability."[235/] The Court explained:

> Rates fixed on this basis would give the [utility] company and its stockholders not only the fair return to which they are entitled but also the full amount of an expense never in fact incurred. In such circumstances, the Commission could properly disallow the hypothetical tax expense and hold that rates based on such an unreal cost of service would not be just and reasonable.[236/]

95 The Court also rejected two other arguments similar to those that PacifiCorp has put forth in opposition to ICNU's proposed adjustment. First, the Court found it proper to set rates that recognize the tax savings associated with filing a consolidated return without recognizing the expenses associated with the consolidated group's loss:

> Ratemaking is, of course, subject to the rule that the income and expense of unregulated and regulated activities should be segregated. But there is no suggestion in these cases that in arriving at the net taxable income of [the utility] the

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232/ FPC v. United Gas Pipeline Co., 386 U.S. 237, 244 (1967).
233/ Exh. No. 21 at 10: 10 – 11: 3 (Evans Rebuttal).
234/ United Gas, 386 U.S. at 244.
235/ Id. at 243-44.
236/ Id. at 244.

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> Commission violated this rule. Nor did it in our view in determining the tax allowance.[237/]

This contradicts PacifiCorp's argument that accepting ICNU's proposal would "breach[] the carefully established and maintained ring-fences separating regulated and non-regulated operations[.]"[238/]

96 Second, the Court rejected an argument essentially identical to PacifiCorp's claim that ICNU's proposal violates the stand-alone tax computation by "tak[ing] the asset of its non-regulated second-tier parent affiliate without compensation."[239/] The Court stated:

> Nor did the Commission 'appropriate' or extinguish the losses of any member of the affiliated group, regulated or unregulated. Those losses may still be applied to system gains and thereby be turned into instant cash. . . .[T]he losses of unregulated companies are in no way destroyed. They remain with the system, readily available to reduce the taxes of the profitable affiliates to the maximum extent allowed by the tax law.[240/]

Thus, there is no "loss" to PacifiCorp's unregulated affiliates that customers must "pay back."[241/] Regulatory principles mandate that customers pay only the amount that PacifiCorp actually pays to the taxing authorities.

b. The "Benefits/Burdens Test" Does Not Produce a Different Result

97 PacifiCorp's rebuttal testimony on the income tax issue is replete with references to a "benefits/burdens" test. PacifiCorp describes this test as "similar to cost-

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237/ Id. at 243.
238/ Exh. No. 21 at 15: 13-14 (Evans Rebuttal).
239/ Id. at 11: 9-10.
240/ United Gas, 386 U.S. at 247.
241/ Exh. No. 21 at 11: 16-17 (Evans Rebuttal).

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causation," and that "before the Commission can allocate the *benefits* of a consolidated tax adjustment to ratepayers it must first determine that ratepayers bear the *burden* that created the consolidated tax adjustment[.]"[242/] The Commission, however, is not required to follow the benefits/burdens test. The benefits/burdens test is essentially one possible method for determining whether an expense is properly included in a utility's cost of service.[243/] There is no requirement that this test be employed whenever a consolidated tax adjustment is made. Even if, however, the Commission decides the benefits/burden test is applicable in this case, ICNU's proposed adjustment satisfies that test. PacifiCorp raised the same benefits/burdens argument at the OPUC, and the OPUC ordered an adjustment based on the taxes PacifiCorp will actually pay to the taxing authorities.[244/]

i. The Benefits/Burdens Test Is Inappropriate in This Case

98 While the Commission has stated that it generally follows the benefits/burdens test,[245/] the Commission is not required to do so in this case. In City of Charlottesville, the D.C. Circuit held that the benefits/burdens test is one reasonable method for calculating utility income taxes.[246/] The Court, however, pointed out that the benefits/burdens test is not the only reasonable method of estimating the tax liability of a regulated affiliate:

> There are a number of plausible ways to make that estimation—ranging, perhaps, from an approach that would

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242/ Id. at 11: 21 – 12: 1 (emphasis in original).

243/ City of Charlottesville v. FERC, 774. F.2d 1205, 1217 (D.C. Cir. 1985)

244/ Re PacifiCorp, OPUC Docket No. UE 170, Order No. 05-1050 at 16, 18-19 (Sep. 28, 2005).

245/ See Re Avista, Docket Nos. UE-991255, UE-991262, and UE-991409, Second Supp. Order at ¶ 84 ("In general, the Commission relies on the broad principle that reward should follow risk and benefit should follow burden.").

246/ City of Charlottesville, 774 F.2d at 1221.

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> give the utility's ratepayers the benefit of all tax deductions of the consolidated group offset against the utility's income (since the deductions would have been worthless without the income) to an approach that would give ratepayers the benefit of none of them (since the utility would have had no deductions on its own). Within certain rational limits that have clearly not been exceeded here, which approach to choose is more a matter of regulatory policy than of logic. The approach the Commission has chosen, allowing those deductions made possible by charges to the ratepayers, is an entirely reasonable one, beyond our authority to upset.[247/]

Hence, the benefits/burdens analysis need not always be applied in the context of calculating utility income taxes for ratemaking purposes.

99 Under the circumstances presented by the present case, the benefits/burdens test does not provide a useful means for analyzing the amount of income tax expense to be included in PacifiCorp's cost of service. Even if it is true that MEHC bears the burden of paying interest on the PPW loan, it does not follow that MEHC will lose its corresponding tax benefit if ICNU's adjustment is adopted. As the U.S. Supreme Court recognized in United Gas, "the losses of unregulated companies are in no way destroyed."[248/] Nothing the Commission does will affect the tax benefit that MEHC receives as a result of its interest expense, because the tax benefit does not entitle MEHC to payments from ratepayers.

ii. ICNU's Proposed Adjustment Satisfies the Benefits/Burdens Test

100 For many of the same reasons why the benefits/burdens test is inappropriate to use in the context of income taxes, the benefits/burdens test is satisfied

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247/ Id. (emphasis added).
248/ United Gas, 386 U.S. at 247.

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by ICNU's proposed adjustment. Ratepayers are not receiving any benefit without a corresponding burden from the losses that created the tax savings. Ratepayers bear a significant amount of risk that translates into income for MEHC's shareholders. Without the income generated by PacifiCorp, any tax deductions experienced by companies in the consolidated group are worthless.[249/] Moreover, simply imputing the tax deduction of other consolidated companies to PacifiCorp does not somehow take the benefit of the tax deduction away from those companies.[250/] Thus, it is unclear exactly what "benefit" ratepayers would receive. The only thing that ICNU's proposed adjustment seeks to ensure is that PacifiCorp's rates accurately reflect cost of service. Calculating PacifiCorp's income tax expense without regard to the interest deductions that permanently reduce or eliminate PacifiCorp's taxable income would not only grant MEHC shareholders a windfall, but would also be contrary to the principle that ratepayers should only be charged for reasonable and prudent costs incurred in providing service and should not subsidize unregulated activities.[251/]

c. Climbing the Corporate Ladder to Berkshire Hathaway Is Unnecessary in This Case

101 PacifiCorp argues that ICNU's proposed adjustment fails to account for the proper consolidated tax setting by not recognizing Berkshire Hathaway as the ultimate taxpayer. Going up the corporate ladder to Berkshire Hathaway in this case would make the issue unnecessarily complex, as the significant tax offsets are experienced at MEHC.

249/ See City of Charlottesville, 774 F.2d at 1221.
250/ United Gas, 386 U.S. at 247.
251/ Id.; see id. at 247.

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102 MEHC is the affiliated entity that owns PacifiCorp's common equity through PPW.[252/] MEHC provides all of PPW's capital, as PPW does not issue debt or equity capital on its own.[253/] Since MEHC is the entity that funded the acquisition of PacifiCorp through PPW, the debt portion of that capital creates the interest deductions that have the most significant and relevant effect on the amount of taxes PacifiCorp actually pays to taxing authorities.[254/] Climbing up the corporate ladder all the way to Berkshire Hathaway, therefore, is unnecessary. In any event, should the Commission agree with ICNU's position, then PacifiCorp has the burden to submit an alternative method for calculating these costs since the Company disagrees with ICNU's calculations. PacifiCorp, however, did not do so.[255/] PacifiCorp appears to have raised the Berkshire Hathaway argument in an attempt to distract the Commission from looking at this issue further.

d. ICNU's Proposed Adjustment Does Not Constitute a "Double Leverage" Adjustment

103 Staff asserts that ICNU's proposed adjustment is "simply an uncompleted form of a 'double leverage' adjustment."[256/] Staff's assertion is incorrect. ICNU's proposed tax adjustment is designed to ensure that rates accurately reflect PacifiCorp's cost of service, a fundamentally different issue.

104 A double leverage adjustment is designed to reduce the after tax rate of return on rate base. In a capital structure such as that of MEHC, without a double

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252/ Exh. No. 181 at 4: 19 (Gorman Direct).
253/ Id. at 4: 20-21.
254/ Id. at 4: 22 – 5: 10.
255/ TR 200: 19-20 (Evans Cross Exam).
256/ Exh. No. 314 at 6: 20-21 (Kermode Cross Answering).

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leverage adjustment, there exists a risk that MEHC will earn a return in excess of MEHC's cost of equity capital.[257/] Part of a double leverage adjustment in this case would include the tax effect of MEHC's capital structure on PacifiCorp.[258/] That does not necessarily mean, however, that an adjustment for income taxes alone automatically raises a double leverage issue. ICNU's adjustment focuses only on the tax effects of MEHC's capital structure to ensure rates reflect PacifiCorp's actual cost of service and does not address the after tax rate of return.

6. The Commission Should Reject the MEHC Transition Cost Deferral

105 The Commission should reject PacifiCorp's MEHC transition cost deferral and exclude all severance related costs from customers' rates because the costs are excessive, related to the MEHC transaction, and should be the responsibility of PacifiCorp's shareholders. In contrast, the Commission should reduce base rates to account for the long-term savings that are likely to result from the reduced employee counts that have occurred following the MEHC merger. Adoption of ICNU's MEHC transition cost adjustment would reduce rates by $2.46 million.[259/]

106 PacifiCorp sought a deferral of its transition costs and savings on May 19, 2006.[260/] As of the end of 2006, PacifiCorp's total severance costs were approximately

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257/ See WUTC v. PacifiCorp, Docket No. UE-050684, Order No. 4 at ¶¶ 270, 276 (a double leverage adjustment prevents a return in excess of the cost of equity capital); WUTC v. Pacific Power & Light Co., Cause No. U-84-65, Fourth Supp. Order at 31 (ordering a double leverage adjustment to require equity to be compensated based on the parent corporation's overall cost of capital).

258/ See, e.g., WUTC v. PacifiCorp, Docket No. UE-050684 Order No. 4 at ¶¶ 267, 271.

259/ Exh. No. 201C at 3: 12-16 (Iverson Direct).

260/ Re PacifiCorp, Docket No. UE-060817, Initial Application (May 19, 2006).

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$42.9 million, and total annual savings were approximately $35.9 million.[261/] The Company also sought to defer up to $1 million in computer software changes caused by the MEHC acquisition.[262/] PacifiCorp proposed to amortize the severance costs and software costs over a three-year period.[263/]

107 In direct testimony ICNU witness Katie Iverson opposed the deferral of the severance costs and the computer software costs because the "costs incurred by PacifiCorp in its transition to MEHC ownership should not be borne by ratepayers . . . ."[264/] ICNU also identified additional severance costs that should be removed from rates.[265/] Although PacifiCorp implicitly agreed that the computer software costs should not be borne by ratepayers when the Company removed these costs in its rebuttal testimony,[266/] the Company continues to propose that all of its severance costs be recovered from ratepayers.[267/]

108 PacifiCorp's severance costs should be excluded from rates because they violate the MEHC merger commitment to "exclude all costs of the transaction from PacifiCorp's utility accounts."[268/] PacifiCorp acknowledges that its transition costs are

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261/ Exh. No. 201C at 8: 10-12; Exh. No. 205C at 1 (PacifiCorp Response to ICNU DR 6.4). In rebuttal testimony, PacifiCorp agreed to correct a significant error in its accounting of the MEHC transition costs and savings that had been identified by ICNU in the discovery process. Exh. No. 136 at 11: 7-15 (Wrigley Rebuttal); Exh. No. 201C at 6 (Iverson Direct); Exh. No. 206 (PacifiCorp Response to ICNU DR 3.14).

262/ Re PacifiCorp, Docket No. UE-060817, Initial Application at ¶ 6; Exh. No. 201C at 5: 1-4 (Iverson Direct).

263/ Re PacifiCorp, Docket No. UE-060817, Initial Application at ¶ 7.

264/ Exh. No. 201C at 4: 20-21 (Iverson Direct).

265/ Id. at 4: 11-16.

266/ Exh. No. 136 at 11: 11-12 (Wrigley Rebuttal).

267/ Id. at 6: 8-14.

268/ Re MEHC and PacifiCorp, Docket No. UE-051090, Order No. 7, Appendix A at 3 (Feb. 22, 2006).

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"related to the MEHC transition."[269/] These costs would not have occurred but for the MEHC acquisition and should be treated as MEHC transaction costs.

109 PacifiCorp's severance costs are also improper to recover from ratepayers because they are excessive, one-time expenses. The severance costs are heavily weighted toward and unduly benefit PacifiCorp's top executives.[270/] The elimination of the Company's top twelve executives cost [redacted] million, but resulted in only [redacted] million in annual savings; thus, these twelve executives contributed to over [redacted] of the total severance costs, but resulted in only about [redacted] of the total savings.[271/]

110 PacifiCorp justifies these excessive severance benefits because "senior executives are likely to need more time than the broad-based employee population to secure a comparable position with another employer."[272/] PacifiCorp has not demonstrated that the top executives pay, which was approximately $7.6 million for five of the top six executives in the nine months that ended December 31, 2006,[273/] does not provide sufficient compensation to address the risks of a change in ownership.

111 PacifiCorp also based the top executives' compensation on market data that includes unregulated companies that face far more risk than PacifiCorp, but none of the publicly-owned utilities with risk profiles more similar to the Company's.[274/] PacifiCorp alleges that publicly-owned utilities were not included because of the "size and scope of the organization, the revenue each organization is bringing into their

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269/ Exh. No. 131 at 22: 10-11 (Wrigley Direct).

270/ Exh. No. 201C at 8: 12-17 (Iverson Direct); Exh. No. 205C (PacifiCorp Response to ICNU DR 6.4).

271/ Exh. No. 201C at 8: 12-17 (Iverson Direct).

272/ Exh. No. 121 at 12: 9-11 (Wilson Rebuttal).

273/ PacifiCorp 10k at 102-103 (December 31, 2006) (figures for CEO Greg Abel were not included in the 10k).

274/ See TR 240: 17-25, 244: 2-23 (Wilson Cross Exam).

company as a comparable."[275/] However, many publicly-owned utilities, including the Los Angeles Department of Water and Power,[276/] the Sacramento Municipal Utility District,[277/] and Seattle City Light,[278/] have organizational sizes and scopes more similar to PacifiCorp than some of the "comparable" utilities the Company relied upon to set its exorbitant executive severance benefits.[279/]

112 PacifiCorp's base rates should be set to reflect the reduced labor expenses that have occurred since the MEHC merger. PacifiCorp has significantly reduced the number of its employees,[280/] which resulted in savings.[281/] Although these savings are likely to be higher, ICNU only proposes to include $35.9 million in annual savings.[282/] These savings will occur on an ongoing basis and should be reflected in rates.

113 If the Commission grants the MEHC deferral and allows the Company to amortize its excessive severance costs, then ICNU recommends that the Commission amortize the costs over a five-year period.[283/] Staff argues against a five-year amortization period because, in the long-run, ratepayers will pay less under the Company's proposed three-year amortization period.[284/] Staff's rationale ignores that ratepayers would receive a greater benefit by not being required to repay this very high level of expenses over a short time period.

275/ Id. at 244: 16-19 (Wilson Cross Exam).
276/ With 1.4 million electric customers. http://www.ladwp.com/ladwp/cms/ladwp001870.jsp.
277/ With 578,041 customers. http://www.smud.org/about/facts/index.html.
278/ With 375,869 customers. http://www.seattle.gov/light/aboutus/customerguide/#ConStat.
279/ See Exh. No. 123C at 1 (Severance Comparables).
280/ See, e.g., Exh. No. 142 (PacifiCorp Response to ICNU DR 6.5); Exh. No. 145 (PacifiCorp Response to ICNU DR 7.10).
281/ Exh. No. 201C at 5: 5-13 (Iverson Direct); Exh. No. 205C (PacifiCorp Response to ICNU DR 6.4).
282/ Exh. No. 201C at 5: 20-23 (Iverson Direct).
283/ Id. at 7: 25.
284/ Exh. No. 328 at 6: 2-8 (Schooley Cross Answering).

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114 Should the Commission allow PacifiCorp to amortize the merger costs over either a three or five-year period, those costs should be promptly removed from rates once the time period has expired and the amortized amount has been fully recovered. When a utility is allowed to amortize a deferred expense in rates, "[t]he amortization amount, unless revised in a subsequent rate proceeding, will remain embedded in rates even after full recovery of these costs."[285/] In the past, the Commission has corrected this inequity by removing the amortized amounts outside of a general rate case once the amortization period had expired, stating that "[w]hen that recovery is complete, the item should not stay in rates."[286/] At a minimum, the Commission should condition any amortization upon a requirement that PacifiCorp make a filing to remove the merger costs from rates once the recovery is complete, regardless when the Company files a general rate case.

7. PacifiCorp Has Violated the MEHC Merger Order by Exceeding the A&G Expense Rate Cap

115 PacifiCorp's administrative and general ("A&G") expenses exceed the A&G cap the Company agreed to the MEHC merger by approximately $3.13 million. As part of the MEHC merger, PacifiCorp agreed to cap total Company-wide A&G expenses at $222.8 million.[287/] If the Company exceeds this A&G cap, then it must refund these amounts, up to $6 million, to customers.[288/] PacifiCorp's overall A&G expenses in this proceeding are approximately $225.9 million, and the Commission should require

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285/ WUTC v. PSE, Docket Nos. UG-040640, UE-040641, UE-031471, and UE-032043, Order No. 7 at ¶ 13 (Mar. 1, 2005).

286/ E.g. WUTC v. PSE, Docket No. UE-920630, First Supp. Order at 15-16 (Sep. 24, 1992).

287/ Re MEHC and PacifiCorp, Docket No. UE-051090, Order No. 7, Appendix A at 15-16.

288/ Id.; TR. 256: 19 – 257: 3 (Wrigley Cross Exam).

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PacifiCorp to abide by its merger commitments and refund the excess amounts to Washington ratepayers. Washington's allocated portion of the refund would result in a reduction in the Company's revenue requirement of $265,875.

116 Under PacifiCorp's original filed testimony the Company included a refund to customers because its total Company-wide A&G expense was $229.1 million, which exceeded the A&G cap.[289/] PacifiCorp made changes and corrections to A&G expenses in its rebuttal testimony that have resulted in the Company's A&G expenses exceeding $222.8 million. In rebuttal testimony, PacifiCorp proposed four new changes to its A&G expenses,[290/] including the addition of $14.36 million in pro forma wages,[291/] the elimination of the $0.46 million in EEI dues,[292/] the elimination of $0.037 million in customer deposits,[293/] a $17.12 million reduction in A&G expense related to the MEHC transaction, and a $6.3 million increase in A&G expense from eliminating the A&G cap adjustment.[294/] Summing the total of these A&G adjustments establishes that the Company has now exceeded the A&G cap by $3.13 million. The A&G cap would not have been exceeded if Staff had not proposed to increase PacifiCorp's labor costs.[295/]

117 PacifiCorp argues that the A&G expense cap has not actually been violated because the $14.36 million pro forma wage increase was simply placed in the A&G account as a matter of convenience.[296/] PacifiCorp asserts that it could have

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289/ Exh. No. 134 at 4.9.1 (Results of Operation for Period Ending March 31, 2006).
290/ Exh. No. 137 at 44: 18 (Revised Revenue Requirement).
291/ Id. at 48.
292/ Id. at 46.
293/ Id. at 51.
294/ Id. at 52.
295/ See TR 260: 2-8 (Wrigley Cross Exam).
296/ Id.

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included the pro forma wage increase on a "different line."[297/] This is mere unsupported speculation because, as PacifiCorp did not place the pro forma wage increase "on a separate line," there is no way to verify if this "separate line" would be the correct account. More importantly, there is no dispute that PacifiCorp actually placed these costs in the A&G account and the Company has not provided evidence that these costs are not A&G related. Thus, the Commission should conclude that the A&G cap has been exceeded and require the Company to refund $265,875 to ratepayers.

8. The ScottishPower Management Fees Should Be Removed from Rates

118 PacifiCorp has proposed that ratepayers should be responsible for $9.14 million in ScottishPower management fees.[298/] Removal of these fees would reduce Washington rates by approximately $675,000.[299/] The MEHC acquisition of PacifiCorp is a known and measurable event and with this change in ownership, the basis to include management fees from ScottishPower no longer applies.[300/]

9. The Commission Should Adopt PacifiCorp's Rate Spread Proposal

119 PacifiCorp's proposed rate spread and rate design should be approved. Both ICNU and Staff have submitted testimony in support of the Company's proposal to apply a uniform percentage rate increase to most classes.[301/] The proposed rate spread

297/ Id.
298/ Exh. No. 141 (PacifiCorp Response to ICNU DR 3.11).
299/ TR 255: 9-19 (Wrigley Cross Exam).
300/ See WUTC v. PacifiCorp, Docket Nos. UE-050684 and UE-050412, Order No. 4 at ¶ 159 (The Commission refused to adopt a revenue requirement adjustment based on ScottishPower ownership because MEHC's acquisition became effective on March 21, 2006, and mooted the adjustment).
301/ Id.; Exh. No. 321 at 44 (Schooley Direct).

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and rate design are reasonable, and it is also consistent with the study the Company filed in its last general rate case, which was acceptable to the parties.[302/]

IV. CONCLUSION

120 ICNU urges the Commission to adopt the following adjustments to PacifiCorp's proposed revenue requirement increase that would result in an approximately $29.1 million rate reduction:

- Modify the WCA cost allocation methodology to ensure that Washington is compensated for the value of energy and operating reserves that it provides to the east;
- Include the costs and benefits the low-cost Wyoming generating resources in rates because they are used and useful and have always been included in rate base;
- Deny the MEHC transition cost deferral and reduce base rates to reflect the savings associated with recent employee reductions;
- Reduce PacifiCorp's inflated power costs to remove the imprudent SMUD contract, share the risk of Centralia replacement power, and correct the modeling errors related to the short-term firm sales, the GP Camus contract, hydroelectric output, thermal ramping and regulating margins;
- Reduce the Company's revenue requirement to eliminate inflated pension and health care costs, tax expense that will not be paid to the taxing authorities, excessive incentive compensation, the ScottishPower management fees, the non-duplicative Staff adjustments, and the MEHC A&G rate cap; and
- Reject PacifiCorp's PCAM and adopt ICNU's proposed hydro-only PCAM with a corresponding ROE adjustment.

[302/] Exh. No. 201C at 13: 10-18 (Iverson Direct).

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Respectfully submitted,

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