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May 10, 2007

BY ELECTRONIC AND OVERNIGHT MAIL

Ms. Carole J. Washburn
Executive Secretary
Washington Utilities and Transportation Commission
1300 S. Evergreen Park Drive SW
Olympia, WA 98504

Re: ***Dockets UE-061546 and UE-060817 (consolidated):***
PacifiCorp's Answer to ICNU's Motion to Strike PacifiCorp's Reply Brief

Dear Ms. Washburn:

Enclosed for filing in the above-referenced proceedings are an original and twelve (12) copies of PacifiCorp's Answer to Industrial Customers of Northwest Utilities' Motion to Strike PacifiCorp's Reply Brief and Certificate of Service in the above-referenced proceedings.

Thank you for your attention to this matter.

Sincerely yours,

James M. Van Nostrand

Enclosures
cc: Service List
The Honorable Dennis Moss

24878-0038/LEGAL13216333.1

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, Complainant, v. PACIFICORP d/b/a PACIFIC POWER AND LIGHT COMPANY, Respondent.	**DOCKET UE-061546**
In the Matter of the Petition of PACIFICORP d/b/a PACIFIC POWER AND LIGHT COMPANY, For an Accounting Order Approving Deferral Of Certain Costs Related to the MidAmerican Energy Holdings Company Transition	**DOCKET UE-060817** ***(Consolidated)*** PACIFICORP'S ANSWER TO ICNU'S MOTION TO STRIKE

1 PacifiCorp d/b/a Pacific Power and Light ("PacifiCorp" or the "Company") hereby submits its Answer to the Motion to Strike of the Industrial Customers of Northwest Utilities ("ICNU"). PacifiCorp has fully complied with WAC 480-07-395(1) – the Commission rule governing the formatting requirements for briefs submitted to the Commission – and respectfully urges the Commission to deny ICNU's Motion.

2 WAC 480-07-395(1), in relevant part, provides that:

> (1) **Format.** All pleadings, motions, and briefs must meet the following format requirements:
>
> (a) ***Paper size; legibility; margins.*** All pleadings, motions, and briefs must be:
>
> . . . .
>
> • Presented in double-spaced, 12-point, palatino, times new Roman, or an equally legible serif font, with footnotes in the same font and of at least 10-point type.

PacifiCorp's Reply Brief in this proceeding complies with this rule in all respects.

3 **The Required Font Sizes Were Used.** PacifiCorp's Reply Brief used the Times New Roman font, with 12-point size for the main text and 10-point size for footnotes, all as prescribed by the Commission's rule. The rule specifies no requirement as to the proportion of argument to be presented in the text versus presented in the footnote, nor should it. That is not a matter of format, but rather relates to the elements of advocacy style. The Commission in its decision will reflect its view as to whether a particular style of advocacy is effective.

4 **The Required Double-Spacing Was Used.** Double-space line spacing is, in the simplest terms, equal to twice the font size. Where, as here, the requirement is to use a 12-point type, spacing set at 24 points – which was the format followed in PacifiCorp's Reply Brief – meets the double-spacing requirement (*i.e.*, 12 x 2 = 24). Another alternative would be to use the spacing defined by reference to what Microsoft's *Word* software calls "double space," which is something in excess of twice the width of the font. The Commission's rule imposes no such requirement, nor should it. The Commission's format requirements should not be defined by what a particular software manufacturer chooses to identify as "double space," but rather should incorporate the simple arithmetic concept of twice the width of the required font size.

5 **The Font Size Met the Legibility Requirement**. Nothing in the Commission's rule addresses the issue of character spacing, *i.e.*, whether or not it is impermissible to depart from the Microsoft *Word*-prescribed spacing of the characters on each line. Rather, the requirement set forth in the rule is in terms of legibility: it must be a ***legible*** serif font. That is the standard which governs whether a particular level of character compression is acceptable or unacceptable. If the Commission wishes to adopt the Microsoft *Word*-prescribed character spacing as an element of its format requirements, it can certainly do so prospectively. Imposing such a requirement for the first time in an adjudicative proceeding, however, would be unwarranted. Nonetheless, as a matter of information for the Commission, included as Attachment 1 is a reformatted Reply Brief using the Microsoft *Word*-prescribed character spacing. Under this format, two lines of text fall outside the 10-page limit. Any relief granted in response to ICNU's

Motion to Strike should be limited to striking the two lines of text that appear on page 11 in the document included as Attachment 1. For the reasons stated herein, however, PacifiCorp respectfully urges the Commission to deny the Motion to Strike.

DATED: May 10, 2007.

PERKINS COIE LLP

By _____

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Attachment 1

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, Complainant, v. PACIFICORP d/b/a PACIFIC POWER AND LIGHT COMPANY, Respondent.	**DOCKET UE-061546**
In the Matter of the Petition of PACIFICORP d/b/a PACIFIC POWER AND LIGHT COMPANY, For an Accounting Order Approving Deferral Of Certain Costs Related to the MidAmerican Energy Holdings Company Transition	**DOCKET UE-060817** ***(Consolidated)*** **REPLY BRIEF OF PACIFICORP d/b/a PACIFIC POWER AND LIGHT COMPANY**

Dated May 7, 2007

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I. INTRODUCTION

1 Throughout the course of these proceedings, Staff and the Company have diligently pursued fair and balanced compromise in an effort to reach agreement on major issues, including substantial agreement on the West Control Area ("WCA") cost allocation methodology and the structure of a power cost recovery mechanism ("PCAM"). Moreover, Staff and the Company are in the same "neighborhood" with respect to the need for a modest rate increase after 2 ½ years of frozen rates for the Company in Washington: the Company is requesting an increase of $18.58 million, while Staff recommends $12.8 million.[1]

2 In stark contrast, the recommendations of the Industrial Customers of Northwest Utilities ("ICNU") and Public Counsel are from a different planet. Both recommend rejection of the WCA method, without proposing any alternative proposal of their own; and both oppose any form of PCAM for the Company and, in that respect, would require the Company to gain experience under an acceptable inter-jurisdictional cost allocation method before even being ***eligible*** for implementation of a PCAM. This position, when combined with their refusal to engage in any form of constructive dialogue regarding development of an acceptable inter-jurisdictional cost allocation methodology, has the practical effect of slamming the door shut on any regulatory relief whatsoever for PacifiCorp in Washington. ICNU takes their opposition a step further, by actually recommending a ***rate reduction of nearly 10 percent***. (Public Counsel, for its part, declines to make any recommendation on overall revenue requirement.) The extremeness of their positions in this case is striking in and of itself. In the context of these parties' opposition to ***any*** regulatory relief for the Company since January 2003 – and going so far as to sue the Commission in two separate appeals for providing any regulatory relief for the Company[2] – their

[1] This is Staff's recommendation assuming approval of a PCAM; Staff recommends $16.5 million without a PCAM.
[2] Public Counsel and ICNU have opposed any regulatory relief for the Company in Washington since the 1.0 percent rate increase allowed in January 2003 under the rate plan approved in the 1999 rate proceeding. *See Washington Utilities and Transportation Commission v. PacifiCorp d/b/a Pacific Power and Light Company*, Docket UE-991832, Third Supplemental Order (Aug. 9, 2000). When the Commission modified that rate plan in Docket UE-020417 to allow the Company to seek rate relief, ICNU and Public Counsel unsuccessfully appealed the decision to Thurston County Superior Court and then to the Washington State Court of Appeals. *Washington State Attorney General's Office v. Washington Utilities and Transportation Commission*, 128 Wash. App. 818, 116 P.3d 1064 (Wash. Ct. App. Aug. 3, 2005). When the Commission approved a settlement agreement in Docket UE-032065 granting a 7.5 percent rate increase for the Company, ICNU and Public Counsel opposed the settlement and appealed the Commission's

advocacy spins out of orbit (*i.e.*, it has "slipped the surly bonds of earth"[3]), and is worthy of no serious consideration.

II. ARGUMENT

A. The Company's WCA Method Reflects in Rates Only Those Resources that Are "Used and Useful" to Washington Customers.

3 Both ICNU and Public Counsel recommend that the Commission reject the Company's proposed WCA method as unjust and unreasonable in favor of their proposed modifications.[4] The Company, however, has satisfied its burden of proof that the WCA method produces results that satisfy the "used and useful" standard from the 2005 Rate Case Order and that it includes in rates only those resources that provide "tangible and quantifiable" benefits to Washington customers,[5] a conclusion also shared by Staff.[6] The recommendations of ICNU and Public Counsel, as offered through the testimony of Mr. Falkenberg, which advocate for the inclusion in the WCA of certain alleged interconnection benefits from the East and eastern resources, contradict positions taken in the 2005 Rate Case, are based on flawed analyses, and would include resources that are not "used and useful" to Washington customers.

4 ICNU/Public Counsel's proposed interconnection benefit adjustment to the WCA method to account for energy sales in eastern markets falsely assumes that available transmission capacity exists, an assumption which is inconsistent with the 2005 Rate Case Order, which noted

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decision – again unsuccessfully – to Thurston County Superior Court. *Washington State Attorney General's Office v. Washington Utilities and Transportation Commission*, No. 04-2-02511-4 (Wash. Sup. Ct. Oct. 26, 2005).

[3] John Gillespie Magee, Jr., *"High Flight," The Complete Works of John Magee, The Pilot Poet,* This England Books, (1989).

[4] As part of its argument in favor of rejection of the WCA method, ICNU claims that it is a "results-oriented cost allocation methodology designed to increase Washington rates" and suggests that the Company is proposing the WCA method in order to "penalize" Washington for not agreeing to the Revised Protocol. ICNU Initial Brief at ¶¶ 4, 20. Public Counsel characterizes the WCA Method as a "fictional pure 'stand-alone' methodology" that produces "perverse results" of higher costs to Washington. Public Counsel Initial Brief at ¶ 29. ICNU/Public Counsel's position that the WCA method results in higher costs is flawed and misleading because it selectively focuses on the impact of variable costs *only*: factoring in fixed costs *in addition to* variable costs results in insignificant higher overall average system costs related to delivering power in the western control area. Staff agrees with the Company's assessment and also notes that the WCA helps control Washington's costs by isolating it from rapid growth in the eastern control area, a problem which was well documented in the 2005 Rate Case. Staff Initial Brief at ¶¶ 32, 34.

[5] *Washington Utilities and Transportation Commission v. PacifiCorp d/b/a Pacific Power and Light Company*, Docket UE-050684, Order 04; *In the Matter of the Petition of PacifiCorp d/b/a Pacific Power and Light Company for an Accounting Order For an Order Approving Deferral of Costs Related to Declining Hydro Generation*, Docket UE-050412, Order 03 (consolidated) (Apr. 17, 2006) ("2005 Rate Case Order").

[6] Staff Initial Brief at ¶¶ 12, 16.

significant transmission constraints between the western and eastern control areas.[7] Accordingly, the proposal fails because, although the Commission's "used and useful" standard allows for the allocation of indirect benefits, those benefits must still be "tangible and quantifiable."[8] Similarly, ICNU/Public Counsel 's proposal to include eastern Johnston and Wyodak resources in the WCA is a thinly veiled attempt to allocate cheap, highly-depreciated coal resources to Washington in contravention of the directives of the 2005 Rate Case Order. ICNU's argument that the resources should be included because they have "always been included in rates"[9] is circular, self-serving and does not directly address the Commission's "used and useful" standard. As noted by Staff, how the Company allocated resources in the past has nothing to do with how they should be allocated under a new allocation methodology, particularly in light of the Commission's rejection of the system-wide approach of the Revised Protocol.[10] Furthermore, also as noted by Staff, ICNU has failed to demonstrate that these resources are needed to serve Washington load or that there is adequate transmission capacity to move that power from East to West during peak hours.[11]

B. The Proposed PCAM Adequately Balances Risks Between Customers and the Company.

As noted above, ICNU and Public Counsel oppose implementation of a PCAM until the Company gains experience under an approved inter-jurisdictional cost allocation methodology.[12] In addition, Public Counsel suggests that a PCAM is not warranted because the Company does not experience sufficient power cost volatility, citing a statement by Staff witness Buckley at the hearing that there is a level of fluctuation that does not trigger the need for a PCAM.[13] Public

[7] Exh. No. 88 at 18:9-20 (Widmer Rebuttal), 2005 Rate Case Order at ¶ 53.
[8] 2005 Rate Case Order at ¶¶ 68, 340.
[9] ICNU Initial Brief at p. 18 (heading 3), ¶ 36.
[10] Staff Initial Brief at ¶ 36.
[11] In response to testimony highlighting the various flaws contained within its proposed adjustments to include interconnection benefits and Johnson and Wyodak resources, ICNU suggests that the Company should have corrected its analyses. ICNU Initial Brief at ¶¶ 25, 38. In taking this position, ICNU disregards the 2005 Rate Case Order's rejection of the inclusion of benefits not shown to be "used and useful" to Washington customers. Indeed, the Company designed the WCA method in response to the guidance provided in the Order. In contrast to the speculative interconnection benefits recommended by ICNU/Public Counsel, the Company allocates a portion of Bridger generation to Utah because the interconnection benefit is clearly established under the Idaho Power Revised Transmission Service Agreement, which identifies a unit-specific energy transfer from West to East. Exh. No. 88 at 17:5-7 (Widmer Rebuttal), Staff Initial Brief at ¶ 17.
[12] ICNU Initial Brief at ¶ 42, Public Counsel Initial Brief at ¶ 23.
[13] Public Counsel Initial Brief at ¶ 10. Public Counsel attempts to characterize the Company's position as supporting adoption of a PCAM under *any* circumstances by pointing to the hearing testimony of Mr. Widmer. *Id.* However,

Counsel's argument, however, fails to acknowledge Staff's testimony that the Company experiences "significant" variability and that a PCAM is appropriate, or to give weight to any of the evidence offered by the Company in support of a PCAM.[14] ICNU's use of a 10 percent variance measure for power cost volatility is unrealistic because it ignores the volatility of power costs experienced by the Company as recently as the summer of 2006.[15] In addition, Public Counsel's attempt to minimize the Company's level of hydro variability by measuring it on a Company-wide basis is entirely inconsistent with its own position in the 2005 Rate Case – where it advocated a "Hydro Endowment" proposal that disproportionately allocates the Company's hydro resources to Washington – and totally disregards the Commission's rejection of a system-wide approach in the 2005 Rate Case Order.

6 ICNU and Public Counsel attempt to minimize the precedential effect of the Commission's approval of Avista's Energy Recovery Mechanism by noting the different volatility experienced by the two companies.[16] As noted by Staff, however, although the Company may have fewer hydro resources than Avista, its incremental cost to replace that power in the event of hydro decline is higher because its thermal generation resources located in the WCA are primarily base load resources and, as a consequence, the Company must obtain replacement power from fully-loaded short-term contracts, which have a greater impact on net power costs.[17]

7 Public Counsel also argues that the normalization process is a sufficient substitute for a

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this testimony was given in the context of *lengthy* questioning during which Mr. Widmer discussed the Company's exposure to power cost volatility. Widmer, TR. 215:13–223:2. Furthermore, taken in full context, Mr. Widmer's response to Public Counsel's line of questioning was to explain that the Commission has apparently made the policy decision in the case of both Avista and PSE that flowing through power cost volatility, at least in part, to customers is in the public interest. Widmer, TR. 214:18–215:3. Public Counsel also mischaracterizes the Company's position by claiming that it has indicated that "it can live without a PCA unless it gets a mechanism to its liking." Public Counsel Initial Brief at ¶ 8. The Company's position is simply that it reserves the right to decline implementation of a PCAM if the Commission adopts Staff's water year adjustment without modification and proposed cost of capital adjustments, which would eviscerate the incentives provided by a PCAM.

[14] Buckley, TR. 332:20-25. Public Counsel's description of the Company's volatility charts as reflecting only "a regular and predictable fluctuation of prices within a constant range" does not take into account the Company's testimony that the charts nevertheless demonstrate how much forecasted prices can vary even if that variance has the general appearance of a pattern. Public Counsel Initial Brief at ¶ 13, Widmer, TR. 216:22–217:18. Public Counsel also fails to take into account the fact that the 2000-2001 power crisis spike has a "dulling effect" on the appearance of charts attempting to demonstrate volatility of previous years. Widmer, TR. 220:5-15.

[15] Exh. No. 88 at 48:19–49:2 (Widmer Rebuttal), Widmer TR. 221:2-8.

[16] Public Counsel Initial Brief at ¶ 12, ICNU Initial Brief at ¶ 50.

[17] Staff Initial Brief at ¶ 61, Exh. No. 265 at 3:15–4:6 (Buckley Cross-Answering).

PCAM.[18] However, Public Counsel fails to recognize that the normalization process is ill-equipped to capture significant variability in overall power costs and is fraught with uncertainties due to the long-term nature of the data used in normalization rate setting.[19] In addition, Public Counsel fails to recognize that the Commission has clarified that a PCAM is appropriate for factors other than abnormal weather, such as market volatility and other events beyond a utility's control.[20] Staff notes that a PCAM is designed to provide better price signals to customers for the effect on power costs of changes in weather or energy market prices, but that the normalization process cannot achieve such signals.[21]

8 ICNU, for its part, attempts to discredit the Company's proposed PCAM by characterizing the underlying power cost data produced by the GRID model as being "fake."[22] Public Counsel also takes issue with the use of pseudo-actual results.[23] ICNU and Public Counsel unfairly malign the quality of the data which, as explained at length in testimony, is: 1) based on actual costs or calculated from actual information, and 2) is necessary because the Company accounts for its power supply costs on an integrated basis, not by separate jurisdictions.[24]

C. Staff and ICNU's Proposed Cost of Capital Adjustments Ignore the Commission's Discussion from the 2005 Rate Case Order that a Reduction is Not Necessarily Required, Depending upon the Manner In which Risks are Allocated.

9 Staff, Public Counsel and ICNU base their discussions of this issue on a mischaracterization of Commission precedent: They assume the Commission rigidly requires a cost of capital reduction associated with implementation of a power cost recovery mechanism. In fact the precedent suggests the Commission has carefully avoided a rigid application, and instead considers "***whether*** a reduction in the cost of capital" is necessary at all, in the context of its

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[18] Public Counsel Initial Brief at ¶ 6.
[19] Buckley, TR. 334:5-15, 336:2-15, 341:23–343:9.
[20] 2005 Rate Case Order at ¶ 91.
[21] Exh. No. 261 at 36:3-6 (Buckley Direct), Staff Initial Brief at ¶ 106.
[22] ICNU Initial Brief at ¶ 41.
[23] Public Counsel Initial Brief at ¶ 18.
[24] Exh. No. 88 at 42:5-9 (Widmer Rebuttal), Exh. No. 261 at 14:22–15:2 (Buckley Direct). As explained by Staff, "a 'pseudo-actual' issue . . . will exist regardless of the allocation methodology that is used, because the Company does not incur power costs by jurisdiction." Staff Initial Brief at ¶ 103 Staff summarizes that "in some respects, all PCAMs for a multi-jurisdictional utility are, by definition, using some sort of allocated (*i.e.,* 'pseudo-actual') costs. *Id.* Moreover, in an effort to accommodate any concerns Staff once had with respect to the use of pseudo-actual data, the Company agreed to accept Staff's recommendation to increase the dead band to $4 million. Company Initial Brief at ¶ 24.

"overall analysis of how the mechanism shifts risks between investors and ratepayers."[25] For the reasons stated in PacifiCorp's Initial Brief, PacifiCorp respectfully submits that an adjustment is unnecessary in this proceeding.[26]

10 ICNU, for its part, misrepresents the testimony of its own witness on this issue. ICNU's brief creates the impression that Mr. Gorman calculated his recommended 30-basis point reduction in ROE on the basis of the risk-shifting attributes of the "hydro hedge" PCAM recommended by ICNU/Public Counsel witness Falkenberg.[27] In fact, Mr. Gorman's testimony clearly states that his adjustment is based on the adoption of "the Company's PCAM," not on Mr. Falkenberg's recommended mechanism. Exhibit 189, Mr. Gorman's response to PacifiCorp Data Request No. 24, confirms that his analysis is based on PacifiCorp's proposed mechanism, and that his analysis would "possibly" change if the design of the sharing bands were altered and would "probably" change if recovery of fixed costs were eliminated.[28] As discussed above, PacifiCorp has moved considerably from its original PCAM proposal – upon which Mr. Gorman's analysis was based – to reduce any risk shifting from the Company to customers. Accordingly, even if his approach were valid (which it is not, for the reasons discussed in PacifiCorp's Initial Brief), the 30 basis point adjustment is substantially overstated if applied to PacifiCorp's current PCAM proposal. Mr. Falkenberg's hydro hedge PCAM, which features a deadband more than twice as great as PacifiCorp's current proposal ($8.6 million versus $4 million) would shift virtually no risk to customers, and would completely strip away even the slightest rationale for an adjustment.

11 Staff, having based its entire analysis on an S&P metric (times interest coverage) that is no longer used by S&P for evaluating the creditworthiness of electric utilities, attempts unsuccessfully to rehabilitate its analysis by suggesting that it really wasn't looking to S&P or its

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[25] 2005 Rate Case Order at ¶ 97 (emphasis added).
[26] The record is clear from cross-examination of Company witness Hadaway and ICNU witness Gorman that the measurement of any cost of capital adjustment as a result of the adoption of a PCAM would be very difficult – if such an adjustment is measurable at all. Hadaway, TR. 192:24 – 193:11; Gorman, TR. 302:11 – 304:14.
[27] ICNU Initial Brief at ¶ 54.
[28] Exh. No. 89 at pp. 1-2.

times interest coverage standard after all, and now refers to the discredited standard as merely a "benchmark."[29] Staff's testimony speaks for itself on this issue, however, where it unequivocally and incorrectly represents that "[a] 2.50 coverage ratio still satisfies S&P's criteria for a 'BBB' bond rating, which is an investment grade rating."[30] Moreover, Staff failed to address the serious technical errors in its analysis identified in Dr. Hadaway's testimony and discussed in PacifiCorp's Initial Brief.[31] While Staff complains that "PacifiCorp offered no benchmark" or "no calculation of risk shifting,"[32] in fact PacifiCorp thoroughly addressed the issue by showing how the design of its proposal mirrors that currently in place for another Washington utility (Avista) for which no cost of capital adjustment was found to be necessary. In fact, given the widening of the deadband from $3 million to $4 million, PacifiCorp's current proposal now involves ***less*** risk shifting than the mechanism upon which it was modeled.

D. Adjustments to the Company's Net Power Costs Proposed by Staff, Public Counsel and ICNU are Unreasonable and Unsupported.

1. Staff's Proposed Water Year Adjustment Methodology Significantly Changes the Proportion of Above-Normal to Below-Normal Water Years.

12 Staff asserts that the Company's proposed modification to Staff's water year adjustment is an attempt to "manufacture a new water year adjustment."[33] Although Staff's adjustment reduces the variance of annual hydro generation by excluding the upper and lower tails of the distribution, on an overall hydro performance basis this adjustment significantly changes the proportion of above-normal to below-normal water years, resulting in an overstated expectation that approximately 60 percent of the time the Company will experience better-than-normal hydro conditions.[34] Understanding the data on a percentile rank approach is superior to the method proposed by Staff. In any event, the Company and Staff are in agreement that a water year

[29] Staff Initial Brief at ¶ 76.
[30] Exh. No. 300 at 17:12-13 (Elgin Direct).
[31] In its Rate of Return summary, Staff refers to the updated long-term debt in the Company's rebuttal testimony as a "limited" updating of costs. Staff Initial Brief at p. 35, ft. 148. In fact, it was a complete updating of long-term debt costs as of December 31, 2006 (Exh. No. 116 at 4:1-8 (Williams Rebuttal)), but has become moot with the withdrawal of the update and the agreement to use the cost of capital components from the Company's direct case.
[32] Staff Initial Brief at ¶ 82.
[33] Staff Initial Brief at ¶ 97.
[34] Exh. No. 88 at 6:12-20 (Widmer Rebuttal).

adjustment is appropriate only in the event that the Commission adopts a PCAM.

2. ICNU Alleges that Short-Term Firm Transactions Should be Removed from Rates Because they Have Not Been Shown to be Prudently Incurred.

13 ICNU argues that the Company has failed to demonstrate the prudence of its "below-market" short-term firm transactions.[35] Staff supports the Company's inclusion of these transactions and notes that they serve Washington because the Company uses them to balance WCA loads and, as such, are necessary transactions.[36]In addition the Company has provided testimony refuting ICNU's assumption that future transactions will always appear economic at the time of delivery and that excluding all actual short-term firm transactions demonstrates that the transactions were demonstrably detrimental.[37]

3. ICNU's Citation to a Wyoming Public Service Commission Order with Respect to Treatment of Centralia is Misplaced.

14 In advocating for its proposal to allocate 50 percent of replacement power costs to the Company to reflect the fact that the Company retained 50 percent of the appreciation of the Centralia sale, ICNU claims that this proposal is consistent with the Wyoming Public Service Commission's treatment of the Centralia sale in *PacifiCorp*, Wyoming Public Service Commission, Docket 20000-ER-02-184, Final Order (Mar. 6, 2003). This precedent is inapposite. The adjustment adopted by the Wyoming PSC corresponded with the sharing of the ***gain*** in the Wyoming PSC's Centralia decision, which allocated 64 percent to ratepayers and 36 percent to the Company's shareholders.[38] A similar approach in this case would suggest an 87.5 percent allocation of replacement power costs to customers, for the reasons discussed in PacifiCorp's Initial Brief. ICNU also asserts, without explanation, that 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."[39] The cost of power to replace the expiring TransAlta contract is unknown at this point. Even accepting ICNU's $5 million figure as true, however, at

[35] ICNU Initial Brief at ¶ 60.
[36] Exh. No. 265 at 16:1-6 (Buckley Cross-Answering),
[37] Exh. No. 88 at 29:15–30:23 (Widmer Rebuttal).
[38] *PacifiCorp*, Wyoming Public Service Commission, Docket 20000-ER-02-184, Final Order at ¶ 192(d) (Mar. 6, 2003).
[39] ICNU Initial Brief at ¶ 52, citing Exh No. 161 at 68:13-21 (Falkenberg Direct).

most only $500,000 would be recovered through the PCAM as proposed by the Company.[40]

E. The Commission Should Reject Certain Adjustments Proposed by Staff, ICNU and Public Counsel.

1. ICNU's Consolidated Tax Adjustment Is Ill-Conceived and, If Calculated Correctly, Would Produce No Adjustment.

15 ICNU's proposed $3 million adjustment to federal income taxes purports to "allow PacifiCorp to recover only those expenses that it actually incurs."[41] In fact, however, the adjustment has nothing to do with reflecting the "actual taxes paid" by PacifiCorp. Rather than attempting to trace the "actual taxes paid" by PacifiCorp through the entire consolidated tax structure in which PacifiCorp participates – which includes Berkshire Hathaway and all its subsidiaries - the adjustment isolates a single expense item (interest expense) and considers the tax deductions for that expense only at PacifiCorp's second-tier entity, MidAmerican Energy Holdings Company ("MEHC"). If the adjustment is calculated in a manner that reflects the complete picture – *i.e.*, what the adjustment purports to do – the adjustment would be zero or, in fact, could result in a ***greater*** tax liability than on a stand-alone basis, according to Staff witness Kermode's analysis.[42] More fundamentally, the "actual taxes paid" concept is a flawed approach. As stated by then D.C. Circuit Judge Anthony Scalia in *City of Charlottesville*: "the imprecision of the 'actual taxes paid' concept is exceeded only by the name of the Holy Roman Empire: two of the three words are wrong. Taxes, yes. But not necessarily *actual* taxes . . . and not necessarily taxes *paid* . . . ."[43] Moreover, the case heavily relied upon by ICNU in support of its "actual taxes paid" approach, *FPC V. United Gas Pipeline*, confirms only that the approach then followed by the FPC was acceptable.[44] Since 1983, however, FERC has abandoned the "actual taxes paid" approach from *United Gas Pipeline* and is using a "stand-alone" approach based largely on a "benefits follows burdens" analysis.[45] ICNU's adjustment fails such an analysis, since the

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[40] Zero recovery through the $4 million deadband, and 50 percent recovery of the remaining $1 million.
[41] ICNU Initial Brief at ¶ 90.
[42] Exh. No. 314 at 6:5-15 (Kermode Cross-Answering).
[43] *City of Charlottesville v. FERC*, 774 F.2d 1205, 1215 (DC Cir 1985).
[44] *FPC v. United Gas Pipeline Co.*, 386 U.S. 237, 245 (1967).
[45] *Columbia Gulf Transmission Co.*, 23 FERC ¶ 61,396, Opinion 173 (1983); *Potomac Edison Co.*, 23 FERC ¶ 61,398, Opinion 163A (1983).

adjustment attempts to capture the "benefits" (interest tax deductions at MEHC) even though customers are not bearing the expenses that create the deductions.

2. ICNU Incorrectly Claims That the Company Has Exceeded the A&G Expense Refund Threshold and That ScottishPower Management Fees Should be Removed.

16 ICNU's claim that the Company has exceeded the A&G expense refund threshold, thereby requiring a revenue requirement reduction of $265,875, is simply inaccurate.[46] ICNU's own witness conceded that the "[s]ince the adjusted A&G expense is now less than the cap, the Company's adjustment should be eliminated."[47] In fact, the Company reversed the original adjustment to reduce A&G for this reason.[48] The effect of ICNU's other proposed adjustments - pension, healthcare and bonuses - all affect A&G and *further* reduce the A&G level below the cap. ICNU, however, has not offered any supporting exhibits quantifying the A&G level produced by its recommendations, and instead maintains that its overall adjustment of $265,875 is warranted. In fact, the record demonstrates why the adjustment is unfounded. Mr. Wrigley explained on the stand that Mr. Schooley's pro-forma wage adjustment affects both O&M and A&G costs and, as a matter of convenience, Staff and the Company agreed to place the entire adjustment amount on the A&G line, given that there was no need for a more complete itemization.[49] Moreover, ICNU's proposal to remove ScottishPower management fees ignores the fact that these are corporate-related services that are provided to PacifiCorp by its owners.[50] While it may be "known and measurable" that ScottishPower is no longer PacifiCorp's owner, it is neither known, nor measurable, nor proven that these services cease to be provided to PacifiCorp.[51] ICNU failed to provide any testimony with respect to this issue, and the evidence

[46] ICNU Initial Brief at ¶ 115.
[47] Exh. No. 201C at 6:24–71 (Iverson Direct).
[48] Exh. No. 136 at 11:12-15 (Wrigley Rebuttal).
[49] Wrigley, TR. 259:13-19.
[50] ICNU Initial Brief at ¶ 118.
[51] Services provided to PacifiCorp by MEHC and its affiliates under the Intercompany Administrative Services Agreement among MEHC and its affiliates totaled $7.6 million between the MEHC transaction closing date (March 21, 2006) and December 31, 2006. *PacifiCorp 10-k at 89, note 20 (December 31, 2006).* It is clear from transaction commitment Wa 4 in Docket UE-051090 that these shared corporate services would cease to be provided by ScottishPower and instead would be provided by MEHC and its affiliates; commitment Wa 4 holds Washington customers harmless from the impacts of "[c]osts associated with functions previously carried out by parents to PacifiCorp and previously included in rates" being shifted to PacifiCorp or otherwise being included in PacifiCorp's

demonstrates that, whether provided by ScottishPower or MEHC, some level of shared corporate services is provided by PacifiCorp's owners to PacifiCorp.

DATED: May 7, 2007.

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rates. *In the Matter of the Joint Application of MidAmerican Energy Holdings Company and PacifiCorp d/b/a Pacific Power & Light Company For an Order Authorizing Proposed Transaction*, Docket UE-051090, Order 08 at Att. 2, p. 13 (Mar. 10, 2006).

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the attached document upon the persons and entities listed on the Service List below by depositing a copy of said document in the United States mail, addressed as shown on said Service List, with first class postage prepaid.

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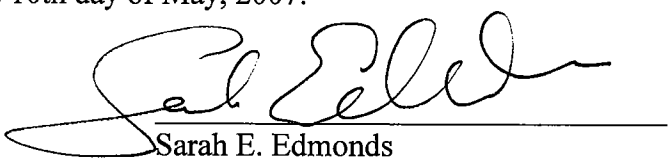

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