

1 **Q. Please state your name, occupation, and business address.**

2 A. My name is Barry G. Cunningham. My position is Vice President of Generation for
3 PacifiCorp. My business address is 201 South Main, Suite 2300, Salt Lake City,
4 Utah.

5 **Q. Briefly describe your educational background, professional training and
6 experience.**

7 A. I received a Bachelor of Arts degree in Physical Science from the University of
8 Wyoming in 1968. I began my career with PacifiCorp in 1977. While at PacifiCorp,
9 I have served as a Trainer, Training Manager, Assistant Operations Superintendent, a
10 Maintenance Superintendent, a Plant Manager, and the Director of Technical Support
11 with responsibility for all of PacifiCorp's small plants. I became Assistant Vice
12 President of Generation in 1998 and Vice President of Generation in 1999 with
13 responsibility for all thermal and hydro assets.

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

15 A. My testimony outlines the proposed sale of the water rights and assets associated with
16 the Naches hydroelectric facility (the "Naches Project" or "Project"), and explains in
17 general terms why the sale benefits PacifiCorp and its customers and why the
18 proposed sale is in the public interest. I also introduce the other witnesses who testify
19 in support of this Application. The purpose of this Application is to seek
20 Commission authority to execute the sale of the water rights and assets related to the
21 Naches Project.

22 **Q. Please introduce the witnesses that will provide testimony on the proposed sale.**

1 A. Other than myself, testimony will be presented by Randy Landolt, Managing Director
2 of Hydro Resources; Craig Johnson, Regulatory Consultant; and James A. Esget,
3 Manager of the United States Bureau of Reclamation's ("Reclamation") Yakima
4 River Basin Water Enhancement Project. Mr. Landolt will provide more detailed
5 testimony on the Naches Project, the proposed sale, the implications of Federal
6 Energy Regulatory Commission ("FERC") licensing, and the financial analysis of the
7 proposed transaction. Mr. Johnson will provide testimony on the regulatory treatment
8 of the proposed sale and expected rate impacts. Mr. Esget will provide testimony on
9 why Reclamation wishes to purchase the water rights and related assets of the Naches
10 Project and why, from Reclamation's perspective, the purchase will serve the public
11 interest.

12 **Q. Please describe how you have organized your testimony.**

13 A. First, I briefly describe the Naches Project. Then I summarize the sale of the water
14 rights and associated assets of the Naches Project and explain why the sale benefits
15 PacifiCorp, PacifiCorp customers and the public generally. Finally, I will explain
16 that the Naches Project is the first of a number of small hydro facilities PacifiCorp is
17 considering selling.

18 **Q. Please describe the Naches Project.**

19 A. The Naches Project is a run-of-river project located on the Naches River in the state
20 of Washington. The Naches River is a tributary of the Yakima River, which in turn is
21 a tributary of the Columbia River. The Project begins with a concrete diversion dam
22 across the Naches River, an intake structure, fish screens, and the approximately
23 eight-mile long concrete-lined Wapatox canal. Water flows travel approximately

1 4.8 miles along the Wapatox canal before entering the Naches Drop Plant through a
2 340-foot long penstock leading to one 1.4 MW turbine-generator. Flows continue
3 through the remaining 3.4 miles of the canal to the Naches Plant fed by two 545-foot
4 long penstocks leading to two turbine generators rated at 3.0 MW and 3.37 MW,
5 respectively. Water from the Naches Plant tailrace is returned to the Naches River.
6 Exhibit ___ (BGC-1) shows the location of the Naches Project in the Yakima River
7 Basin and the location of the various elements of the Project I have just described.
8 The Wapatox canal not only provides water to the Naches Project, it also distributes
9 about 50 cubic feet per second (“cfs”) of irrigation water to over 100 shareholders of
10 the Wapatox Ditch Company and Lower Wapatox Ditch Company.

11 The Naches Plant was constructed in 1909. The Naches Drop Plant was
12 constructed in 1914. Although the total nameplate rating of the turbine-generators is
13 7.8 MW, the Project is “run-of-river” meaning that the energy produced depends on
14 upstream flows over which PacifiCorp has no control or storage rights. As a result,
15 the Project provides no peaking value. Historically, the Project has generated about
16 3.5 average megawatts (“MWa”) of energy. The forecasted generation level from the
17 Project is 3.1 MWa due to expected declines in power production as a result of recent
18 court rulings that require Reclamation to ensure survivability of downstream fish
19 populations. Reclamation controls upstream water releases and also further dictates
20 diversionary canal flows. The impact of these controls is expected to reduce available
21 flows into the Wapatox canal. As downstream fish populations improve, the
22 minimum flow releases into the Naches River will need to increase for their

1 survivability, thus further reducing flows into the Wapatox canal for power
2 generation.

3 **Q. Please explain the proposed sale.**

4 A. PacifiCorp has entered into an agreement with Reclamation to sell PacifiCorp's water
5 rights associated with the Naches Project, the generation assets, the Naches River
6 diversion dam, the in-take structure and associated fish screens, the Wapatox canal
7 and the associated land and property. Reclamation will assume the perpetual
8 obligation to operate and maintain the Wapatox canal that serves the irrigators.
9 PacifiCorp will transfer its easements as needed to operate and maintain the Wapatox
10 canal. PacifiCorp will keep the Naches Plant Substation as well as the
11 transmission/distribution line located on the right of way between the Naches Plant
12 and Naches Drop Plant. In addition, PacifiCorp will keep the company cottages and
13 associated property adjacent to the Naches Plant as well as a small area of land in the
14 City of Naches. PacifiCorp is evaluating the course of action it will take with regard
15 to the disposition of these retained properties. PacifiCorp will retain and redistribute
16 the tools and equipment not required by Reclamation. Reclamation will be
17 responsible to remove the generation capability of the facilities. Exhibit ____ (BGC-2)
18 is a copy of the signed agreement between PacifiCorp and Reclamation.

19 **Q. Are there other parties involved in this transaction?**

20 A. Yes. Reclamation is purchasing the water rights and assets associated with the
21 Naches Project under the auspices of the Yakima River Basin Water Enhancement
22 Project. The State of Washington Department of Ecology is a co-funder. The
23 purchase is strongly supported by the Yakama Indian Nation.

1 **Q. Why is Reclamation purchasing the water rights and assets associated with the**
2 **Project?**

3 A. Mr. Esget addresses the reasons that Reclamation is purchasing the water rights and
4 assets associated with the Project. It is my understanding that Reclamation's primary
5 interest in purchasing the water rights and associated assets of the Project is to
6 increase water flows in the stretch of the Naches River between the Wapatox canal
7 and the Naches Plant tailrace. Reclamation's purpose in increasing water flows in
8 this part of the Naches River is to improve stream and other wildlife habitat.

9 Reclamation is not interested in generating power. Reclamation's interest in the
10 generation facilities is limited to using some of the existing structures and
11 improvements to control water flows in the Wapatox canal. It is expected that once
12 Reclamation takes over operation of the Wapatox canal that canal flows will be
13 limited to only that required to meet irrigators' water rights plus any required carriage
14 water. There would be inadequate water available for meaningful power production.

15 **Q. Please provide a brief history of the sale.**

16 A. Federal acquisition of the Naches Plant and Naches Drop Plant was contemplated in
17 1989 as part of the proposed Yakima River Basin Water Enhancement Project. In
18 April 2000, Reclamation began discussions with PacifiCorp on the concept of
19 purchasing PacifiCorp's water rights. Beginning in April 2002, earnest negotiations
20 were held and the structure of a proposed sale agreement was developed. Both
21 parties executed a Letter of Intent on June 19, 2002 outlining the proposed sale
22 agreement. The sale agreement was signed by both parties on August 21, 2002.

1 **Q. Briefly explain why PacifiCorp believes it is in its customers' best interest to sell**
2 **the water rights and associated assets of the Naches Project.**

3 A. PacifiCorp's financial analysis indicates it would be a lower cost option to purchase
4 energy at market than to continue to invest in and operate and maintain the Project.
5 The Project is approximately 90 years old. Significant capital investment and extra-
6 ordinary operation and maintenance ("O&M") costs will be needed to ensure the
7 Project continues to be viable, safe and economically efficient for an additional
8 30 years. In addition, in recent years, generation levels have been reduced as the
9 result of biological requirements to increase in-stream flows in the Naches River.
10 Lastly, FERC has opined that the Project is located on a navigable waterway, which
11 would subject the Project to FERC licensing requirements. Although FERC has not
12 issued an order regarding Naches, it is likely that some time in the future FERC will
13 require PacifiCorp to go through the FERC licensing process. When required, the
14 process of obtaining a FERC license is extremely costly and time consuming. It is
15 also expected that a condition of any license ultimately issued would be a further
16 increase in natural Naches River flows; this would result in further energy reductions
17 from the Project. Consequently, a likely outcome in the absence of a sale would be a
18 requirement to license the Project at the FERC under conditions that would provide
19 little or no generation, while simultaneously being required to perpetually operate and
20 maintain the Wapatox canal to serve the obligations to the irrigators.

21 Moreover, there are environmental benefits of the proposed transaction. As
22 discussed in the testimony of James Esget, the proposed sale benefits fish species that
23 are at risk of extinction.

1 **Q. Will there be a gain or profit on the sale?**

2 A. The Company considers this sale a “break even” transaction. The agreed-to purchase
3 price for the water rights, associated generation facilities, and canal is approximately
4 \$7.48 million. In addition, PacifiCorp will be paid for the assessed value of the land
5 associated with the sale. The price to be paid for the land will be based on a fair
6 market appraisal performed by a mutually acceptable appraiser. The current
7 undepreciated book value of the assets expected to be transferred, including real
8 property, is \$10.6 million. As of end of September 2002, the net book value of the
9 Naches Project assets is approximately \$5.1 million.

10 PacifiCorp will incur a variety of costs to effect the sale. Costs will be
11 incurred to perform a variety of activities which includes environmental remediation,
12 relocation of substation controls and boundaries, modification of the existing
13 substation access, and legal and project management. In addition, there will be a
14 deferred tax adjustment. We expect the transaction to produce a slight after-tax gain.

15 **Q. What forces are changing the economics of the Naches Project?**

16 A. The Naches Project is a very small hydro project. As mentioned earlier, this is an old
17 resource and major investments will be necessary to maintain the Naches Project as a
18 viable facility. Historically, the energy provided by the Naches and Naches Drop
19 Plants is less than 0.7% of the total amount of hydro-based generation in the
20 PacifiCorp system. Current and projected flow reductions in the Wapatox canal are
21 expected to reduce future generation. The high probability of having to apply for a
22 FERC license provides further incentive for PacifiCorp to divest itself of this
23 resource.

1 **Q. Are the changing economics of small hydro facilities affecting more than the**
2 **Naches Project?**

3 A. Yes. For many of the same reasons that PacifiCorp has determined that sale of the
4 Naches water rights and associated facilities is prudent, we are finding that a growing
5 number of small hydro projects are becoming less economic to own and operate.
6 PacifiCorp anticipates it will seek to divest itself of a number of other small hydro
7 projects in the future. To put this issue in perspective, approximately one half of the
8 hydro projects PacifiCorp owns and operates are small hydro facilities, yet on average
9 these small hydro facilities typically produce less than 5% of the total energy
10 generated by PacifiCorp hydro resources. The age of the facilities, pressures to
11 increase in-stream flows, and the issues and costs associated with FERC licensing
12 combine to create conditions under which it is becoming uneconomic to continue to
13 own and operate some of these facilities.

14 **Q. Has PacifiCorp identified the other small hydro projects it is considering selling?**

15 A. Not yet. There are a number of small hydro projects that are under consideration but
16 the Company has not completed the work necessary to support firm plans to sell the
17 projects.

18 **Q. Why does PacifiCorp propose selling the Naches Project now?**

19 A. PacifiCorp has a willing buyer at a fair price and the buyer has agreed to assume the
20 obligations to operate and maintain the irrigation canal.

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

22 A. Yes, it does.