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April 16, 2001

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Ms. Carole J. Washburn, Secretary
Washington Utilities & Transportation Commission
1300 S Evergreen Park Drive, SW
PO Box 47250
Olympia, WA 98504-7250

Re: UE-001878
In the Matter of the Joint Application of PacifiCorp and PacifiCorp,
Washington, Inc. for Approval to Implement Restructuring

Dear Ms. Washburn:

Enclosed, for filing in this docket, are the original and 19 copies of the Testimony of Gregory N. Duvall sponsoring a proposed power sales agreement.

The power sales agreement is a critical element of PacifiCorp's proposed restructuring in that it will govern the sale of power from the proposed new generating company ("PacifiCorp Generation") to each state electric company. It is intended to afford the Company's retail customers in each state with an equitable and permanent allocation of the benefits of PacifiCorp's existing generation system. We intend to schedule a public workshop in Washington this month to provide an opportunity for the Company to provide further explanation of the proposed agreement and to begin to receive input from interested parties.

No later than May 18, 2001, PacifiCorp will file additional testimony and exhibits regarding: a) proposed interjurisdictional cost allocation principles, b) proposed corporate governance and decision-making principles, c) the Company's expectations regarding continuing state and federal regulatory oversight and d) additional information on the proposed corporate structure.

Ms. Carole J. Washburn, Secretary
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No later than June 30, 2001, PacifiCorp will file the balance of its direct case, including revenue requirement projections, power sale contract pricing elements and a proposed service company contract.

Very truly yours,

A handwritten signature in black ink, consisting of several loops and a long horizontal stroke extending to the right.

George M. Galloway

Enclosures

cc w/encls: Parties of Record
James M. Van Nostrand

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the Joint Application of
PACIFICORP and PACIFICORP,
WASHINGTON, INC. for an Order
Approving (1) the Transfer of Distribution
Property from PacifiCorp to an Affiliate,
PacifiCorp, Washington, Inc.,
(2) the Transfer by PacifiCorp of Certain
Utility Property to an Affiliate, the Service
Company, and (3) the Proposed Accounting
Treatment for Regulatory Assets and
Liabilities, and an Order Granting an
Exemption under RCW 80.08.047 for the
Issuance or Assumption of Securities and
Encumbrance of Assets by PacifiCorp,
Washington, Inc. and/or PacifiCorp

Docket No. UE-001878

PACIFICORP

DIRECT TESTIMONY OF
GREGORY N. DUVALL

April 2001

1 Q. Please state your name, address and position with PacifiCorp or the "Company".

2 A. My name is Gregory N. Duvall. My business address is 825 NE Multnomah, Suite
3 2000, Portland, Oregon 97232, and I am the Managing Director, Business
4 Strategies, Power Supply.

5 Q. Please describe your education and business experience.

6 A. I have been employed by PacifiCorp for 22 years and have held a variety of
7 positions in the Energy Trading, Resource Planning and Regulatory areas. I hold a
8 Bachelor of Arts in Mathematics from the University of Washington (1976) and a
9 Masters of Business Administration from the University of Portland (1979). From
10 July 1997 through August 2000, I managed the Energy Trading Department for
11 Powercor Australia Ltd., a former PacifiCorp subsidiary located in Melbourne,
12 Australia. In that role, I was responsible for electricity commodity trading activity,
13 retail pricing in the contestable market, trading analysis, risk management and
14 reporting, contracts and confirmations, and wholesale pool and contract settlement.
15 I have been in my current position since returning to the United States.

16 Q. Have you previously testified in regulatory proceedings?

17 A. Yes, I have previously testified in regulatory proceedings in Oregon, Utah,
18 Wyoming, Washington, Idaho and California.

19 **Overview of Testimony**

20 Q. What is the purpose of your direct testimony in this proceeding?

21 A. The purpose of my direct testimony is to present a proposed initial power supply
22 agreement between the proposed generation company ("PacifiCorp Generation")

1 and the proposed Washington state electric company (“PacifiCorp, Washington”).

2 A draft of the Company’s proposed initial power supply agreement (“Agreement”)

3 is attached as Exhibit T, GND1. In this proceeding, PacifiCorp is seeking various

4 approvals from the Washington Utilities and Transportation Commission

5 (“Commission”) necessary for it to implement its proposed corporate restructuring.

6 Under that proposal, the existing PacifiCorp would be divided into six state electric

7 companies, a generation company and a service company. Details concerning the

8 nature and reasons for this reorganization were contained in previously-filed direct

9 testimony.

10 Q. Why do you characterize this as an “initial” power supply agreement?

11 A. The Agreement provides for the supply of an amount of power at embedded-cost

12 prices from PacifiCorp’s existing power plants, purchased power contracts and

13 market purchases that is roughly equivalent to the current loads of the Company’s

14 Washington customers. Although, in theory, PacifiCorp, Washington could

15 purchase all its future requirements under the Agreement at market prices, it is

16 expected that the future load growth of such customers and resource replacement

17 will be met from other agreements entered into by PacifiCorp, Washington with

18 PacifiCorp Generation or third parties.

19 Q. Are the terms of the Agreement subject to adjustment in response to further analysis

20 by the Company and comments and concerns of the Commission Staff, customer

21 representatives and others?

1 A. Absolutely. While we have spent a great deal of time working on the Agreement,
2 we understand that it gives rise to a number of novel and challenging issues.
3 Recognizing that the Agreement will be carefully scrutinized by all stakeholders, we
4 have attempted to strike a fair balance of interests. I will note in the course of my
5 testimony particular aspects of the Agreement that the Company acknowledges
6 require further analysis and potential modification to assure that the overarching
7 goals of the Agreement (as described in the next section of my testimony) are
8 achieved.

9 We expect other parties will have comments and important perspectives
10 about the Agreement in future workshops. We would like to use those workshops
11 as a forum to develop substantial consensus on the terms of the Agreement. We
12 have proposed to delay filing the balance of our direct testimony and exhibits for
13 several months following this initial presentation of the Agreement to allow time to
14 incorporate views of interested parties in a modified version that would then be the
15 basis for the Company's detailed financial analyses contained in our final direct
16 submittal.

17 Q. What is the status of the Agreement exhibits that are included with your filing?

18 A. Only proposed Agreement Exhibits A through D are included with this filing. Even
19 these exhibits are entirely illustrative. For example, some of the exhibits will
20 ultimately list all of the Company's existing hydro-electric plants, wholesale
21 contracts or thermal plants, but the example exhibits show them on a cumulative
22 basis. Similarly, the numbers shown on the exhibits are purely illustrative.

1 Q. When will final Agreement exhibits be submitted?

2 A. They will be part of our proposed June 30, 2001 filing, along with associated
3 analyses of revenue requirement impact.

4 **Goals of Agreement**

5 Q. What are the overarching goals that guided the Company's development of the
6 Agreement?

7 A. Most importantly, the Agreement needs to provide retail customers with a
8 reasonably-priced, reliable source of power, while at the same time, providing the
9 Company's shareholders with a reasonable opportunity to earn a fair rate of return,
10 commensurate with the risks that are faced. Other important objectives are to
11 (a) encourage competition in wholesale power markets, (b) stimulate investment in
12 new generation, (c) preserve the efficiency of the Company's integrated generation
13 system and (d) provide a platform for each of the different states that regulate the
14 Company to pursue public policy initiatives that they deem appropriate without
15 burdening our customers in other states or the Company's shareholders. We
16 believe the Agreement furthers all these goals.

17 Q. Does the Agreement recognize retail customers' historic economic support of the
18 Company's existing generation?

19 A. Yes. The Agreement preserves for Washington customers their equitable portion of
20 the total "value" that is embedded in the Company's existing generation and
21 wholesale contracts. That said, we recognize that this allocation process is not an

1 exact science and that it is subject to a number of legitimate competing claims
2 among states, among customer classes and between customers and shareholders.

3 Q. How does the Agreement effect the current balancing of risks between the
4 Company's customers and shareholders?

5 A. The relative balance of risks borne by customers and shareholders is not materially
6 altered. In some respects, the Agreement changes the nature of some of the risks
7 and the associated risk-management tools that exist under our current organization
8 and form of regulation. I will highlight these changes during the course of my
9 description of the Agreement.

10 **Overview of Agreement**

11 Q. How do you describe the Agreement in the balance of your testimony?

12 A. I first provide a general overview of the key elements and then explain the intent of
13 the Agreement section-by-section.

14 Q. Please proceed with the general overview of the key elements.

15 A. The Agreement is intended to provide PacifiCorp, Washington with an ability to
16 acquire a base amount of capacity and energy from PacifiCorp Generation that is
17 roughly equivalent to current Washington loads at a price that is generally reflective
18 of the costs of owning and operating PacifiCorp's existing generation fleet. To that
19 end, the Agreement includes the following proposals:

- 20 • The Agreement contemplates that the Washington share of the Company's
21 hydro-electric facilities will be dedicated to PacifiCorp Washington for as long

1 as those plants are economic, with the actual costs and output of those facilities
2 passed through under the terms of the Agreement.

- 3 • In regard to the Company's thermal plants, the proposed contract price will
4 reflect the fixed and variable costs of those facilities at the beginning of the term
5 of the Agreement, with such costs escalated through time on the basis of
6 external cost indices that are representative of the general performance level of
7 the industry. At the end of the assumed life of each of the thermal plants, the
8 Agreement provides that the thermal plant be sold at auction with the net
9 proceeds allocated between PacifiCorp, Washington (and its customers) and
10 PacifiCorp Generation.

11 Q. What are the key billing components in the proposed Agreement?

12 A. The billing components in the Agreement consist of:

- 13 1) a charge that recovers the actual costs associated with hydro-electric and
14 wind facilities and purchased power contracts,
- 15 2) a charge that reflects the fixed costs of thermal plants,
- 16 3) a charge that recovers PacifiCorp Generation's transmission expense
17 associated with the Agreement,
- 18 4) a charge that reflects the variable costs of operating thermal plants and
19 balancing PacifiCorp Washington's loads as required with market
20 purchases and market sales,
- 21 5) a charge that recovers PacifiCorp Generation's actual environmental
22 costs, and

1 Agreement will be driven by the length of time that the Company's existing Hydro-

2 Electric Generating Plants can remain licensed to the Company and can operate in a

3 cost-effective manner. It is not possible to predict how long this will be. Finally,

4 Subsection 2.3 provides for the Agreement's review and approval by the Federal

5 Energy Regulatory Commission ("FERC").

6 Q. When do you expect to file the Agreement with the FERC?

7 A. We expect to file the Agreement with the FERC in August of 2001 after we have an

8 opportunity to receive input in regard to it from our state regulators and other

9 stakeholders.

10 **Section 3: Power Purchase**

11 Q. Please describe the purpose of Section 3 of the Agreement.

12 A. Section 3 of the Agreement summarizes the fundamental commercial arrangement

13 that is established by the Agreement. This Section obligates PacifiCorp Generation

14 to supply PacifiCorp, Washington's Net Load and obligates PacifiCorp, Washington

15 to take and pay for that Power as provided for in Subsection 3.1.

16 Q. What is meant by "Net Load"?

17 A. Net Load is a term defined in Subsection 1.43 of the Agreement. It represents the

18 amount of PacifiCorp, Washington's actual retail and wholesale load in any hour

19 that is not being served by Non-Dedicated New Resources. As defined in

20 Subsection 1.45, Non-Dedicated New Resources represent power available to

21 PacifiCorp, Washington from new power supply arrangements that PacifiCorp,

22 Washington elects not to have dispatched by PacifiCorp Generation.

- 1 Q. Does that mean that PacifiCorp, Washington has full control over the amount of
2 Power supplied by PacifiCorp Generation under the Agreement?
- 3 A. In theory, yes. PacifiCorp, Washington could supply all its requirements from Non-
4 Dedicated New Resources. However, if it pursued that strategy, it would still have
5 substantial fixed cost obligations under the Agreement. Also, we expect that as
6 PacifiCorp, Washington acquires new resources, it may be advantageous for it to
7 elect to have them categorized as Dedicated New Resources dispatched as part of
8 PacifiCorp Generation's total integrated system. For these reasons, it is likely that
9 PacifiCorp, Washington will be obtaining a substantial portion of its power supply
10 requirements under the Agreement for a long time to come.
- 11 Q. Will the Power supplied under the Agreement come from any specific resources?
12 A. No. The Power will be system power that will be delivered independent of whether
13 any particular PacifiCorp Generation resources are operating. Individual resources
14 are identified in the Agreement only for pricing purposes.
- 15 Q. Please describe the pricing provisions of the Agreement.
- 16 A. The pricing components of the Agreement are contained in Sections 4 through 9.
17 Essentially, separate "blocks" of power sold under the Agreement are priced based
18 upon the costs associated with various categories of resources. For example,
19 Section 4 describes how a quantity of power under the Agreement is to be priced
20 based upon the cost of owning and operating the Company's Hydro-Electric
21 Generating Plants (including wind facilities) and the costs incurred under existing
22 Purchased Power Contracts.

Section 4: Hydro/Contract Charge

2 Q. Please describe how Section 4 would operate.

3 A. A critical aspect of the Agreement is the allocation, for pricing purposes, of a share
4 of the output from PacifiCorp's existing generating plants and wholesale contracts
5 to PacifiCorp, Washington. In respect to Hydro-Electric Generating Plants and

6 Purchased Power Contracts, this allocation will be shown on Agreement Exhibit D.
7 The indicative Exhibit D attached to the Agreement shows Hydro-Electric

8 Generating Plants and Purchased Power Contracts on an aggregated basis because
9 we are still compiling individual Plant and contract data. The final Exhibit D will
10 be broken down by individual Plants and contracts.

11 Q. In Exhibit D, the allocation of Hydro-Electric Generating Plant output may be
12 different from month to month and between heavy and light load hours. What is the
13 reason for this?

14 A. If we were to assign, for pricing purposes, a uniform annual "slice" of our

15 resources to each state electric company, the total amount of output from all of the
16 assigned percentages would be well short of what is required to serve peak loads.
17 This is because, under current circumstances, our summer-peaking states rely on a
18 disproportionate share of our resources during the summer and our winter-peaking
19 states rely on a disproportionate share of our resources during winter months.

20 Therefore, the allocations shown on Exhibit D will be designed to give each state
21 electric company the economic benefit of our integrated system and the associated
22 seasonal diversity benefits.

1 Q. Will PacifiCorp, Washington be allocated enough resources to cover its load

2 requirements during every hour of the year?

3 A. No. Notwithstanding the seasonal diversity in the Company's system, the Company

4 currently must make substantial market purchases in hours of high demand. This

5 practice, (which along with sales of short-term surpluses, we refer to as "load

6 balancing") will be deemed to continue under the Agreement. I discuss it further in

7 connection with my testimony regarding Section 6 of the Agreement.

8 Q. When will the actual assigned percentages of resources be known?

9 A. The actual proposed percentages, as well as an analysis of their effect on generation

10 revenue requirement, will be included in our final direct submittal in June. The

11 Company intends to include in its May 2001 filing testimony concerning the

12 methods that we intend to use to develop inter-jurisdictional allocations of each of

13 our resources.

14 Q. Where are the resource shares to be reflected in Section 4 of the Agreement?

15 A. There is a defined term of "Maximum Hourly Hydro/Contract Percentage", which

16 will be found on Exhibit D to the Agreement and used as the "S" term for Hydro-

17 Electric Generating Plants and the "Q" term for Purchased Power Agreements in

18 the formula contained in Section 4. The effect of the formula is to provide for

19 PacifiCorp, Washington to pay a monthly fixed charge equal to its share of all of

20 the actual costs associated with PacifiCorp's existing Hydro-Electric Generating

21 Plants and Purchased Power Contracts.

22 Q. What does PacifiCorp, Washington receive for making this fixed monthly payment?

1 A. Through the operation of Section 6, (which I discuss later in my testimony)
2 PacifiCorp, Washington is entitled to receive an amount of Power under the
3 Agreement each month equal to the actual amount of power available to PacifiCorp
4 Generation from PacifiCorp, Washington's share of the Hydro-Electric Generating
5 Plants and Purchased Power Contracts.
6 Q. Does this mean that PacifiCorp Generation will dispatch this share of its Hydro-
7 Electric Generating Plants against PacifiCorp, Washington's load in "real time"?
8 A. No. In order to maintain existing system efficiencies, PacifiCorp Generation will
9 continue its present practice of dispatching its resources in a way that serves its total
10 load in the least-cost manner. Under the Agreement, all pricing is done on an after-
11 the-fact accounting basis that "dispatches" resources deemed allocated to
12 PacifiCorp, Washington for pricing purposes in each hour.
13 Q. How will PacifiCorp Generation's actual costs associated with Hydro-Electric
14 Generating Plants and Purchased Power Contracts be determined?
15 A. They will be based on PacifiCorp Generation's FERC Form 1.
16 Q. How will the rate of return on PacifiCorp Generation's investment in Hydro-
17 Electric Generating Plants be established?
18 A. "Rate of Return" is a defined term in the Agreement that pertains to the calculation
19 of a number of charges. Our current thinking is to establish it on the basis of a
20 formula derived from an index of long-term bond yields. It would reflect an
21 appropriate capital structure balancing both a debt and equity return. A specific
22 proposal will be included in our final direct submittal in June.

1 Q. Is the Rate of Return intended to be a pre-tax or after-tax rate?

2 A. We intend to establish the formula so that it produces an after-tax Rate of Return.

3 Q. Where is the Rate of Return reflected in the calculation of costs associated with

4 Hydro-electric Generating Plants?

5 A. It is the "R" term in the formula in Subsection 4.1.

6 Q. Will the Commission have the ability to audit the costs of Hydro-Electric

7 Generating Plants to assure that FERC accounting policies have been followed?

8 A. Yes.

9 Q. What recourse will the Commission have if costs are improperly recorded?

10 A. If PacifiCorp Generation did not voluntarily agree to remedy the matter, the

11 Commission, or any other party with standing, could file a complaint with the

12 FERC.

13 **Section 5: Thermal Charge and Transmission Charge**

14 Q. Please explain Section 5 of the Agreement.

15 A. Section 5 of the Agreement is similar to Section 4 in that it establishes a fixed

16 monthly payment derived from PacifiCorp Generation's fixed costs, but in this case,

17 those associated with PacifiCorp, Washington's share of PacifiCorp Generation's

18 existing Thermal Plants. As with Hydro-Electric Generating Plants, an allocation is

19 made for each facility for heavy and light load hours for each month of the year.

20 Q. How is Section 5 different from Section 4?

21 A. There are three important differences:

1 1. Allocation of Output: Hydro-Electric Generating Plants shares and
2 Purchased Power Contracts shares are shown on Exhibit D as *percentages* of
3 available output. In the case of Thermal Plants, the allocation is based upon a fixed
4 megawatt-hour per hour amount as shown in columns C through X of Agreement
5 Exhibit A. These amounts are referred to in the Agreement as Monthly Heavy
6 Load Hour Thermal Energy Shares and Monthly Light Load Hour Thermal Energy
7 Shares.
8 2. Duration: In the case of Hydro-Electric Generating Resources, it is
9 assumed that they will effect pricing under the Agreement more or less indefinitely.
10 In the case of Thermal Plants, the shares are reflected in the Agreement only during
11 their assumed depreciable life or until the "End Date" shown in column B of
12 Agreement Exhibit A. Prior to their End Date, Thermal Plants (or in some cases,
13 "portions" of Thermal Plants) are referred to in the Agreement as Active Thermal
14 Elements.
15 3. Actual Versus Indexed Costs: In the case of Hydro-Electric Generating
16 Plants, the monthly fixed charge is based upon PacifiCorp Generation's actual costs
17 incurred during each Year during the term of the Agreement. In regard to Thermal
18 Elements, the initial fixed charge amount (expressed as dollars per megawatt-month
19 and shown in column AA of Agreement Exhibit A) is expected to represent actual
20 fixed costs at the inception of the Agreement. Thereafter, the amount is to be
21 adjusted from month to month based upon established external indices which reflect
22 representative industry cost changes.

1 Q. Do the external indices include wholesale power market indices such as the Dow Jones Mid-Columbia or Palo Verde? 2

3 A. No. The external indices relate only to the underlying costs of the Company's Thermal Plants. Examples are shown on Agreement Exhibit C. 4

5 Q. Specifically, how is the Thermal Charge provided for in Section 5 calculated? 6

7 A. For each Active Thermal Unit, the process starts with the amount per megawatt-month shown in column AA of Agreement Exhibit A adjusted according to the relative change in a "basket" of indices, including the Rate of Return, described in the corresponding formula in column AC of Agreement Exhibit A. 9

10 Q. Please explain the depreciation amount shown for each Thermal Element. 11

12 A. For each Thermal Element, a determination will be made of the expected annual depreciation expense that will occur in the course of ordinary operation. These depreciation amounts will be set forth on a Year-by-Year basis in Exhibit A and included in the calculation of the Thermal Charge. 14

15 Q. Why is the Company proposing to establish Thermal Plant prices based upon external indices, as opposed to using actual costs as reflected in its FERC Form 1? 16

17 A. Unlike Thermal Plants, the costs and output from Hydro-Electric Generating Plants are almost entirely out of PacifiCorp Generation's control. The formula approach provides PacifiCorp, Washington with an assurance that it will pay reasonable costs in connection with Thermal Plants. We are mindful of concerns regarding the loss of Commission jurisdiction to the FERC in connection with the proposed restructuring and the Agreement. Basing Agreement prices on costs driven by 22

1 external indices should provide assurance that notwithstanding a shift of
2 Commission jurisdiction to the FERC, PacifiCorp, Washington will be protected
3 against atypical levels of costs or imprudent actions by PacifiCorp Generation. The
4 formula approach also provides PacifiCorp Generation with an added incentive to
5 operate efficiently and a benchmark against its peers.
6 Q. You indicated that some Thermal Plants might be shown as more than one Active
7 Thermal Element. Why is that the case?
8 A. There are some Thermal Plants that have "must run" characteristics for some or all
9 months of the year. During those months, all of the costs associated with the Plant,
10 including fuel, are effectively fixed because they cannot be avoided. These
11 economic realities will be reflected in the Agreement price for the months in
12 question. Similarly, some Plants have different cost characteristics associated with
13 different levels of output. For example, in the case of the Hermiston Generating
14 Plant ("Hermiston"), its natural gas supply Agreement provides for fairly
15 significant penalties if the facility is not operated approximately 80 percent of the
16 time. These penalties represent a fixed cost of operating the plant for up to 80
17 percent of its available output. Therefore, there is a different relationship between
18 the fixed and variable costs associated with operating Hermiston at different levels
19 of monthly output. We propose to deal with these differences by dividing Plants
20 such as Hermiston into separate Active Thermal Elements, with different cost
21 characteristics. The importance of having accurate variable costs associated with

1 each Active Thermal Element will become clearer when I discuss the Agreement

2 "dispatch" process contemplated by Subsection 6.3 later in my testimony.

3 Q. What benefit does PacifiCorp, Washington derive from paying the monthly Thermal

4 Charge provided for in Section 5?

5 A. For pricing purposes, PacifiCorp, Washington is deemed to have capacity available

6 to it in amounts equal to the Heavy Load Hour Thermal Energy Share and the Light

7 Load Hour Thermal Energy Share for each of the Active Thermal Elements. This

8 capacity is then deemed to be drawn on as required in exchange for the payment of

9 the Variable Charge associated with each Thermal Element as described in

10 Section 6.

11 **Section 6: Variable Charge**

12 Q. Please describe how Section 6 determines Variable Charges.

13 A. The first step in determining what Variable Charges are payable in each hour is to

14 determine which Thermal Elements must be "dispatched" to serve PacifiCorp,

15 Washington's requirements. This is the function of the formula in Subsection 6.1.

16 The starting point in this formula is PacifiCorp, Washington's Distribution Load in

17 any hour. Added to this are transmission losses and PacifiCorp, Washington's

18 allocated share of sales made under Power Sales Contracts. Subtracted from this

19 sum is the amount of energy deemed to be available in the hour from Hydro-

20 Electric Generating Plants and Purchased Power Contracts and the amount of

21 energy that was actually delivered to PacifiCorp, Washington during the hour from

1 Non-Dedicated New Resources. The result is PacifiCorp, Washington's Hourly
 2 Thermal Agreement Load.
 3 Q. Why is the starting point for this formula Distribution Load as opposed to Net
 4 Load?
 5 A. These defined terms are part of a mechanism built into the Agreement to deal with
 6 direct access affecting customers in Washington. As the terms are defined, there is
 7 only a difference between Distribution Load and Net Load to the extent that an
 8 entity other than PacifiCorp, Washington is serving some portion of the Distribution
 9 Load. When this occurs, Section 9 of the Agreement provides for a Direct Access
 10 Credit to compensate PacifiCorp, Washington for the amount of its Distribution
 11 Load that has been "freed up" by direct access initiatives. I will discuss this credit
 12 in greater detail later in my testimony.
 13 Q. Why is an allocated portion of energy sold by PacifiCorp Generation under Power
 14 Sales Contracts included in the formula for establishing the Hourly Contract
 15 Thermal Load?
 16 A. Because PacifiCorp, Washington is credited with a corresponding share of revenues
 17 derived from those Agreements pursuant to Subsection 6.5.
 18 Q. What is the next step in calculating the Thermal Variable Charge?
 19 A. The next step in the pricing process is similar to the one followed in respect to the
 20 Thermal Charge. For each Active Thermal Element, there is an initial variable cost
 21 (expressed as dollars per megawatt-hour) to be shown in column AC of Agreement
 22 Exhibit A. This amount is then adjusted each month by the relative change in a

1 basket of external indices according to the corresponding formula shown in column
2 AD of Agreement Exhibit A. This process results in an adjusted variable cost
3 associated with each Active Thermal Element that is deemed to be "dispatched"
4 against the Hourly Agreement Thermal Load in the process provided for in
5 Subsection 6.3.
6 Q. Do the external indices include wholesale power market indices such as the Dow
7 Jones Mid-Columbia or Palo Verde?
8 A. No. The external indices relate only to the underlying costs of the Company's
9 Thermal Plants. Again, examples are shown in Agreement Exhibit C.
10 Q. Is it only Active Thermal Elements that are deemed "dispatched" against the Hourly
11 Agreement Thermal Load?
12 A. No. Dedicated New Resources are also included in the deemed dispatch process.
13 Q. What is the source of variable cost data for Dedicated New Resources?
14 A. PacifiCorp, Washington will provide this information to PacifiCorp Generation
15 pursuant to Subsection 12.2 of the Agreement.
16 Q. Please describe how Subsection 6.3 is intended to operate.
17 A. The first step is to "rank order" the Active Thermal Elements and Dedicated New
18 Resources in ascending order of variable cost. They are then "dispatched" against
19 the Hourly Agreement Thermal Load. As each Active Thermal Element or
20 Dedicated New Resource is deemed to be dispatched, the Hourly Agreement
21 Thermal Load is reduced by the corresponding Monthly Heavy Load Hour Thermal
22 Energy Share or Monthly Light Load Hour Thermal Energy Share of that Active

1 Thermal Element or the Dedicated New Resource (as shown on Agreement Exhibit
2 A). This "dispatch" process continues until either:
3 a) there are no longer any Active Thermal Elements or Dedicated New
4 Resources left to dispatch or the variable cost of the next Active Thermal Element
5 or Dedicated New Resource that would be deemed to be dispatched is greater than
6 the applicable Base Supplemental Power Unit Cost for the hour or
7 b) the Hourly Thermal Agreement Load has been reduced to zero as a result
8 of the Active Thermal Elements and Dedicated New Resources that have been
9 previously dispatched.
10 Q. What is the significance of the variable cost of the next Active Thermal Element or
11 Dedicated New Resource being greater than the applicable Base Supplemental
12 Power Unit Cost?
13 A. When this occurs, it is cheaper for PacifiCorp, Washington to be deemed to be
14 served "from the market" as opposed to "dispatching" additional Agreement
15 resources.
16 Q. What is the effect on pricing if this occurs?
17 A. The balance of the Hourly Thermal Agreement Load is deemed to be "served" from
18 the market by either Base Supplemental Power or Premium Supplemental Power.
19 Q. What happens if the Hourly Thermal Agreement Load is reduced to zero before the
20 variable cost of the next Active Thermal Element or Dedicated New Resource
21 exceeds the Base Excess Power Unit Price?

1 A. Pursuant to Subsection 6.3, the "dispatch" continues until the variable cost of the
2 next Active Thermal Element or Dedicated New Resource exceeds the applicable
3 Market Sale Index. The amount of energy deemed dispatched in this way, in excess
4 of the Hourly Thermal Agreement Load, is deemed either Base Excess Power or
5 Premium Excess Power.

6 Q. What is the significance of the variable cost of the next Active Thermal Element or
7 Dedicated New Resource exceeding the applicable Base Excess Power Unit Price?
8 A. This means that the cost of "dispatching" any additional resources would exceed the
9 wholesale revenues that would be derived from doing so.

10 Q. Does Subsection 6.3 fully describe the "dispatch logic" that will have to be
11 followed?
12 A. No. Provision still needs to be made to recognize the actual limitations on
13 PacifiCorp Generation's ability to cycle Plants on and off from hour to hour and
14 dispatch the limitations arising from transmission constraints.

15 Q. Why are there distinctions between Base Supplemental Power and Premium
16 Supplemental Power and between Base Excess Power and Premium Excess Power?
17 A. Because of transmission constraints, the Company currently has a finite ability to
18 reach the most advantageous market hubs to make market purchases and market
19 sales in the course of load balancing. We propose to determine the amount of load
20 balancing that currently occurs on PacifiCorp's integrated system and to establish
21 this as the "Base" amount to be allocated among PacifiCorp, Washington and the
22 other state electric companies. This Base amount will vary as a function of the

1 Hydro/Contract Energy Amount in the hour on the basis of a table to be included in
2 Exhibit C. The allocated cost of providing this Base quantity will be established in
3 a series of formulae which will be contained in Exhibit K to the Agreement.
4 Additional quantities of load balancing (Premium Supplemental Power and Premium
5 Excess Power) are to be priced on the basis of a formula incorporating the Market
6 Purchase Index and the Market Sale Index.
7 Q. Is it possible that the Market Purchase Index will be different than the Market Sale
8 Index?
9 A. That is likely to occur. Because of transmission constraints and the location of the
10 Company's generation, the Company often is forced to purchase required energy
11 when it is deficit at different market hubs than where it is able to sell energy when it
12 is in a surplus condition. However, the entire subject of load balancing is one that
13 we believe requires substantial further consideration and will be further addressed in
14 subsequent filings in this proceeding. Under current market conditions, load
15 balancing is extremely expensive. We are concerned that as load patterns and
16 market conditions change during the term of the Agreement, it will be challenging
17 to equitably price load balancing with reference to market hub price indices. We
18 also believe that in the absence of a cap on the amount of available load balancing
19 from the system, one state electric company could unfairly impose costs on others
20 by failing to acquire new resources, thereby increasing the amount of load balancing
21 requirements of the system.

- 1 Q. Will PacifiCorp, Washington be able to avoid incurring substantial costs for load balancing above the base amount?
- 2 A. Yes. Through its integrated resource planning process, it should be able to add New Resources in a manner that keeps its load balancing requirements within the base amounts.
- 3 Q. How is the Variable Charge for each hour calculated?
- 4 A. This is described in Subsection 6.4 of the Agreement. The formula in that subsection first multiplies the variable costs of each Active Thermal Element by the amount of energy deemed to have been dispatched. Added to this amount is a charge for any Supplemental Power that was deemed to have been "purchased" and credited against it are the revenues deemed to have been received from the sale of Excess Power.
- 5 Q. Why are the variable costs of Dedicated New Resources not included in the formula?
- 6 A. Pursuant to the provisions of Subsection 12.3, both the fixed and variable costs of New Resources are to be directly paid by PacifiCorp, Washington.
- 7 Q. Why is Premium Supplemental Power priced at a premium to the Market Purchase Index while Premium Excess Power is priced at a discount to the Market Sale Index?
- 8 A. As I indicated previously, because of transmission constraints, the Company is not always able to purchase required energy at the prevailing market price at major trading hubs and is not always able to sell surplus energy at the prevailing market

1 price at major trading hubs. Also, as I indicated previously, we are very concerned
2 that changes in load patterns and market conditions will make load balancing a risky
3 endeavor for PacifiCorp Generation during the term of the Agreement. While we
4 may be prepared to have PacifiCorp Generation provide these services to
5 PacifiCorp, Washington if it requires them, we wish to provide strong incentives to
6 PacifiCorp, Washington and the other state electric companies to acquire new
7 resources in a way that does not increase system load balancing requirements and
8 unfairly burden either PacifiCorp Generation or the other state electric companies.
9 Another approach would be to somehow require each of the state electric companies
10 to acquire new resources such that their load balancing requirements are not
11 increased above the Base amount. We expect this to be a subject for future
12 workshops.
13 Q. How is the monthly Variable Charge calculated?
14 A. This is provided for in Subsection 6.5. It is the sum of the hourly Variable Charge
15 amounts, less the amount of revenues from Power Sales Agreements allocated to
16 PacifiCorp, Washington (the Power Sales Agreement Revenue Amount).
17 **Section 7: Environmental Cost Assessment**
18 Q. Please describe Section 7 of the Agreement.
19 A. Section 7 of the Agreement describes an environmental cost assessment. It provides
20 that as PacifiCorp Generation incurs Environmental Obligations associated with
21 Plants and Mines that are the source of pricing under the Agreement, the costs will
22 be accumulated in a "sinking fund" and amortized over 15 years with interest at the

1 Rate of Return. Pursuant to Section 7, PacifiCorp Washington's share of the
2 monthly amortization amount would be billed to PacifiCorp, Washington.
3 Q. What are the "Environmental Obligations" subject to Section 7?
4 A. This is a defined term at Subsection 1.22 and is intended to be inclusive of the types
5 of environmental costs that the Company is presently entitled to recover from its
6 retail customers. Section 7 will apply to costs associated with remediation of
7 ground and water contamination at the Plants and Mines, and costs of complying
8 with existing and new laws and regulations related to ground and water
9 contamination and air emissions.
10 Q. Will Environmental Obligations include costs of remediating ground and water
11 contamination that preceded the effective date of the Agreement?
12 A. Yes. These are costs that would have been borne by our retail customers in the
13 absence of the proposed restructuring and are therefore properly passed through to
14 PacifiCorp, Washington under the Agreement.
15 Q. Why are Environmental Obligations being passed through on an actual basis, rather
16 than projected at the beginning of the Agreement, as you are proposing with respect
17 to other categories of costs associated with the Company's Thermal Plants?
18 A. We believe the degree of uncertainty regarding the level of our future
19 Environmental Responsibilities precludes us from making projections that could
20 reasonably be expected to be equitable to customers and shareholders over the long
21 term.

1 Section 8: Reimbursement of New Taxes

2 Q. Please describe Section 8 of the Agreement.
3 A. Section 8 of the Agreement provides for the pass-through of "New Taxes" to
4 PacifiCorp, Washington. "New Taxes", as defined in Subsection 1.44, consist of
5 new governmental assessments that generally apply to electric generating facilities
6 that are based upon the level of output or emissions of those facilities including a
7 "carbon tax" or "generation tax".
8 Q. Why is it appropriate for PacifiCorp Generation to pass-through costs associated
9 with New Taxes?
10 A. These costs are not subject to the control of PacifiCorp Generation and would be
11 passed through to retail customers absent the proposed restructuring of the
12 Company. The purpose of these types of taxes is to send price signals that
13 encourage ultimate consumers to use electricity prudently and to encourage utilities
14 to rely less on coal-fired generation. These public purposes would be frustrated if
15 there were not a direct pass-through of New Taxes to PacifiCorp, Washington and
16 its customers.
17 Q. Would it be possible for PacifiCorp Generation, to mitigate its exposure to New
18 Taxes by limiting the emissions from its Thermal Plants?
19 A. To the extent New Taxes are aimed at carbon emissions, it is not expected that any
20 additional emission control equipment would be effective. Rather, as I previously
21 suggested, it is likely that New Taxes would be principally aimed at reducing
22 ultimate consumption, as opposed to encouraging investment in control equipment.

Section 9: Direct Access Credit

- 1 Q. What is the purpose of Section 9?
- 2 A. Section 9 provides for a "Direct Access Credit" to PacifiCorp, Washington. It
- 3 would only be operative if there is a difference between PacifiCorp, Washington's
- 4 Distribution Load and its Net Load because some of PacifiCorp, Washington's
- 5 Distribution Load is being served by entities other than PacifiCorp, Washington.
- 6 The function of Section 9 is to provide that if some of the Power that PacifiCorp,
- 7 Washington is purchasing under the Agreement is "freed-up" by direct access
- 8 initiatives, it will be deemed to have been resold in short-term wholesale markets to
- 9 the credit of PacifiCorp, Washington.
- 10 Q. How is the formula in Section 9 intended to operate?
- 11 A. To the extent, under Subsection 6.3, PacifiCorp, Washington is deemed to be
- 12 purchasing Base Supplemental Power or Premium Supplemental Power in any hour,
- 13 the energy freed up by direct access effectively cancels out the economic effect of
- 14 those purchases. The balance of the freed-up energy is deemed to be sold at the
- 15 same price that would otherwise be applicable to sales of Base Excess Power or
- 16 Premium Excess Power pursuant to Subsection 6.4.
- 17 Q. How does the Company propose that the Direct Access Credit be allocated between
- 18 cost-of-service customers and direct access customers of PacifiCorp, Washington?
- 19 A. The credit represents a return to PacifiCorp, Washington of the economic value of
- 20 the energy from PacifiCorp Generation's resources that is being freed up by direct
- 21 access in any hour. Depending upon prevailing market prices, this credit may be
- 22

1 more or less than the average cost of Power under the Agreement. That is to say,
2 there may be either "transition credits or transition charges" under the Agreement if
3 direct access is pursued by Washington consumers. We believe the determination
4 of how PacifiCorp, Washington's costs under the Agreement, including the Direct
5 Access Credit, should be allocated between cost-of-service customers and direct
6 access customers is a matter for the Commission, with guidance from the
7 Washington Legislature, to ultimately decide.

8 Q. Is PacifiCorp, Washington limited to relying on this credit in respect to obtaining
9 the economic benefit of Power freed up by direct access?

10 A. No. Pursuant to Subsection 3.2 of the Agreement, subject to stated restrictions,
11 PacifiCorp, Washington may resell Power in wholesale markets if its Retail Load is
12 reduced as a result of direct access initiatives.

13 Q. What are the restrictions?

14 A. The Wholesale Contracts must have a load factor reasonably comparable to the load
15 that was freed up and the points of delivery under the Wholesale Contracts must be
16 the same as the Points of Delivery under the Agreement. The amount sold may not
17 be appreciably greater than the amount of load freed up to direct access.

18 Q. Why are these restrictions appropriate?

19 A. While PacifiCorp, Washington should have a reasonable opportunity to mitigate
20 against load loss, it should not be permitted to do so in a way that would "game"
21 the Agreement or unreasonably increase PacifiCorp Generation's costs of providing
22 Power.

1 **Section 10: Scheduling and Redispatch**

2 Q. Please describe the provisions of Section 10 of the Agreement.

3 A. Section 10 describes how Power will be prescheduled under the Agreement.

4 Annually, PacifiCorp, Washington is to provide PacifiCorp Generation with a good-faith estimate of its expected Power requirements during each hour of the following Year. The process is repeated on a day-ahead basis pursuant to Subsection 10.2. Once PacifiCorp Generation understands PacifiCorp, Washington's expected Power requirements on a day-ahead basis, pursuant to Subsection 10.3, it will provide PacifiCorp, Washington with a schedule showing the amount of Power that will be delivered at each of the Points of Delivery that are established under the Agreement. This delivery preschedule must be consistent with Prudent Utility Practice and consistent with limits (Delivery Limits) that will be in the Agreement on the amount of Power that can be delivered at any Point of Delivery.

14 Q. What are the Points of Delivery under the Agreement?

15 A. It is expected that they will be major points of transmission interconnection at the boundaries of PacifiCorp, Washington's system.

17 Q. When will the Points of Delivery and Delivery Limits be established?

18 A. We expect to include that information in our final direct submittal in June.

19 Q. What is the purpose of Subsection 10.4?

20 A. Subsection 10.4 affords PacifiCorp Generation the right to dispatch Dedicated New Resources as part of its entire system. However, it is only permitted to do so in a manner that is not disadvantageous to PacifiCorp, Washington.

21

22

1 Q. What ancillary services is PacifiCorp Generation providing?

2 A. This is dealt with in the balance of Section 10 of the Agreement. Essentially,

3 PacifiCorp Generation is obligated to provide load following and operating reserves

4 and to maintain power quality in respect to an amount of Power equivalent to the

5 output of the generating resources that are being supported under the Agreement

6 (the Total Entitlement Amount). This is generally equivalent to the level of

7 ancillary services that the Company is currently providing in connection with its

8 service to Washington consumers. The Agreement contemplates that as PacifiCorp,

9 Washington requires additional ancillary services, it will purchase them separately

10 from PacifiCorp Generation or from the market.

11 Q. What is the difference between "load balancing," about which you previously

12 testified, and the ancillary service of "load following".

13 A. As I use the terms, "load balancing" involves shaping PacifiCorp, Washington's

14 entitlement to embedded-cost Power and market purchases and sales under the

15 Agreement against its scheduled wholesale and retail loads. "Load following"

16 means covering the difference between pre-scheduled amounts of Power and actual

17 loads within any hour.

18 Q. Is the subject of ancillary services another area of the Agreement that the Company

19 believes requires substantial additional analysis and discussion?

20 A. Yes. The subject of ancillary services is highly complex. The consideration of

21 these issues is evolving as discussions of the RTO West continue. At this point, it

22 is not possible to predict which ancillary services the RTO will provide and how it

1 will provide them. Therefore, Section 10 of the Agreement will have to evolve as
2 the issues develop.

3 **Section 11: Billing**

4 Q. What does Section 11 of the Agreement provide?

5 A. Section 11 contains the provisions for monthly billing. Subsections 11.1 and 11.2
6 reiterate the components of each monthly billing as provided for in Sections 4

7 through 9 of the Agreement. Subsection 11.3 provides mechanisms for "truing up"
8 billings to the extent that some of the components have previously been calculated
9 on an estimated basis because necessary data was not available. Subsection 11.4

10 provides that PacifiCorp, Washington will pay bills by wire transfer within 15 days
11 of receipt.

12 **Section 12: New Resources**

13 Q. Please describe the provisions of Section 12 of the Agreement.

14 A. Section 12 deals with the Dedicated and Non-Dedicated New Resources. These
15 consist of power supply contracts to be entered into by PacifiCorp, Washington,
16 other than the initial Agreement with PacifiCorp Generation. New Resources are
17 either Non-Dedicated or Dedicated depending upon whether PacifiCorp,
18 Washington elects to have PacifiCorp Generation dispatch them.

19 Q. Do New Resources have to be purchased power contracts, as opposed to new "rate-
20 based" resources?

21 A. Yes. We believe that after our proposed restructuring, it would be inefficient for
22 the separate PacifiCorp state electric companies to directly own and operate

1 generating facilities. We believe this function is best performed by entities that
2 specialize in the business including independent power producers and PacifiCorp
3 Generation.
4 Q. When must PacifiCorp, Washington decide whether New Resources are Dedicated
5 or Non-Dedicated?
6 A. Pursuant to Subsection 12.1, this election must be made at least 30 days in advance
7 of when deliveries are first expected from a New Resource. The initial election
8 may be reversed at any time with one-year advance written notice from PacifiCorp,
9 Washington to PacifiCorp Generation.
10 Q. What role will PacifiCorp Generation have with respect to Non-Dedicated New
11 Resources?
12 A. PacifiCorp Generation will need information regarding Non-Dedicated New
13 Resources for its planning purposes as described in Subsection 12.1. Otherwise, it
14 will have no involvement.
15 Q. What role will PacifiCorp Generation have with respect to Dedicated New
16 Resources?
17 A. As provided for in Subsection 10.4, PacifiCorp Generation will have the right to
18 dispatch Dedicated New Resources as part of its system. However, pursuant to
19 Subsection 12.2, PacifiCorp, Washington will have sole discretion as to what
20 variable costs are assumed by PacifiCorp Generation in making dispatch decisions.
21 PacifiCorp, Washington will have responsibility for administering all contracts
22 associated with New Resources and for paying all costs associated with those

1 contracts whether they be Dedicated or Non-Dedicated. Some or all of the

2 administration of the contracts may be delegated to the proposed service company.

3 **Section 13: Maintenance and Sale of Resources**

4 Q. What is the function of Section 13 of the Agreement?

5 A. Section 13 establishes PacifiCorp Generation's rights and responsibilities in regard

6 to its existing generating plants that were constructed to serve cost-of-service retail

7 customers.

8 Q. How does Section 13 deal with the Company's Hydro-Electric Generating Plants?

9 A. As I indicated previously, it is expected that Power priced based on the cost of

10 PacifiCorp's Hydro-Electric Generating Plants will be available under the

11 Agreement as long as those facilities are licensed to PacifiCorp and economically

12 viable. Therefore, PacifiCorp, Washington and its customers have a strong interest

13 in ensuring that the Hydro-Electric Generating Plants are well-maintained and

14 operated by PacifiCorp Generation for the balance of their useful lives. That is the

15 purpose of Subsection 13.1.

16 Q. How does Section 13 deal with the Purchased Power Contracts and Power Sales

17 Contracts?

18 A. The Agreement provides that an allocated share of the cost of all energy actually

19 available from Purchased Power Contracts will be passed through to PacifiCorp,

20 Washington for the balance of the term of those contracts. The Agreement also

21 provides that an allocated share of the cost of supplying all energy actually

22 delivered pursuant to Power Sales Contracts will be passed through to PacifiCorp,

1 Washington (along with the revenues) for the balance of the term of those contracts.
2 Therefore, PacifiCorp, Washington and its customers have a strong interest in
3 ensuring that PacifiCorp Generation adheres to the terms of those contracts and
4 requires continued compliance by counter-parties. Under the circumstances,
5 PacifiCorp Generation should not be free to assign the contracts or agree to any
6 amendment to them that increases PacifiCorp, Washington's costs. These matters
7 are all dealt with in Subsection 13.2.
8 Q. What continued rights and responsibilities are established in the Agreement with
9 respect to the Company's Thermal Plants?
10 A. Under the Agreement, PacifiCorp Generation's actual costs of owning and operating
11 its Thermal Plants do not effect the price paid for Power except as noted for
12 Environmental Obligations and New Taxes. Therefore, some of the concerns that
13 are addressed by Subsections 13.1 and 13.2 with respect to Hydro-electric
14 Generating Plants and wholesale contracts are not present. However, the
15 Company's Thermal Plants give rise to a number of different issues under the
16 Agreement which are both challenging and important. These include:
17 1. To what extent should PacifiCorp Generation be permitted to sell or
18 otherwise dispose of Thermal Plants during the term of the Agreement?
19 2. How should the net proceeds (gains and losses) of the sale of any
20 Thermal Plant be allocated between PacifiCorp Generation and PacifiCorp,
21 Washington?

1 3. What should be PacifiCorp Generation's rights and responsibilities with
2 regard to new generating plants that are built on the site of an existing Thermal
3 Plant?

4 4. What should be PacifiCorp Generation's rights and responsibilities
5 regarding life extensions, capacity additions or "repowering" at an existing Thermal
6 Plant?

7 5. What should be PacifiCorp Generation's rights and responsibilities with
8 respect to Thermal Plants that suffer catastrophic failure or are "derated" as a result
9 of environmental compliance requirements?

10 We believe issues such as these need to be resolved in a symmetrical fashion
11 between our shareholders and customers. We also believe that the resolution of
12 these issues cannot be resolved independent of the pricing impact of the Agreement.
13 We are hopeful that our planned public workshops will point the way toward a
14 balanced resolution of these issues and we have included proposals in the
15 Agreement intended to advance the discussion.

16 Q. How does the Agreement propose to resolve these issues?
17 A. Subsection 13.3 deals with the issue of a proposed sale of a Thermal Plant prior to
18 its End Date (assumed life). It requires PacifiCorp Generation to provide
19 PacifiCorp, Washington, and the other state electric companies who are parties to
20 similar power supply agreements, with 180 days' advance notice of any proposal to
21 sell a Thermal Plant that is associated with an Active Thermal Element. Within 120
22 days after such notice is given, each of the state electric companies (presumably in

1 consultation with their respective state regulatory commissions) must provide
2 PacifiCorp Generation with a Reserve Price for their respective share of the thermal
3 plant that is being sold. PacifiCorp Generation may then decide whether or not it
4 wishes to proceed with the auction.
5 If PacifiCorp Generation elects to proceed with the auction and the
6 successful bid is higher than the sum of the separate Reserve Prices: a) a percentage
7 of all net proceeds from the sale will be allocated among the state electric
8 companies relative to their respective Buyer Shares of the associated Thermal
9 Element and b) the Active Thermal Element associated with the plant that is sold
10 will no longer be an Active Thermal Element used for pricing purposes under the
11 Agreement. If the successful bid is lower than the sum of the separate Reserve
12 Prices: a) the Plant would not be sold b) the Active Thermal Element associated
13 with the Plant would no longer be used for pricing purposes under the Agreement
14 and c) the actual costs and output of the Plant would be charged to PacifiCorp,
15 Washington in the same manner that applies to Hydro-electric Generating Plants.
16 Q. How will auctions of Thermal Plants be conducted?
17 A. Subsection 13.3 anticipates that Auction Protocols will be developed and included in
18 Exhibit H to the Agreement. We assume that these Auction Protocols will assure a
19 fair auction process designed to maximize bidder participation and bid levels.
20 Q. Would PacifiCorp Generation be permitted to participate in such auctions?
21 A. Yes.

1 Q. What is the significance of the megawatt limit (now blank) at the end of Subsection 13.2?

2

3 A. We recognize that it is unlikely that the Commission would find it acceptable for PacifiCorp Generation to have the unilateral right to dispose of all or substantially all of the Thermal Plants that support the Agreement. Therefore, we would propose to cap the total amount of Thermal Plant capacity that can be sold at some reasonable level.

7

8 Q. Does this mean that PacifiCorp Generation could never propose to dispose of a greater amount of Thermal Plant capacity?

9

10 A. No. As with many issues, we anticipate that changed circumstances may well give rise to various proposals to amend the Agreement. However, we would expect that the Commission would wish to be consulted by PacifiCorp, Washington before this occurred. In this sense, the Agreement is intended to reflect the "rules of the road" that will govern until PacifiCorp Generation, PacifiCorp, Washington, the FERC and the Commission agree otherwise.

15

16 Q. What does the Company propose in respect to Thermal Plants that reach the end of their assumed lives?

17

18 A. Subsection 13.4 of the Agreement provides that during the year prior to the End Date of any Thermal Element, the associated Thermal Plant will be sold at auction.

19

20 Q. How does Subsection 13.4 resolve the issues related to new generating units that may have been built by PacifiCorp Generation on a site shared with a Thermal Plant being auctioned?

21

22

- 1 A. It provides that prior to the auction, the real property will be equitably partitioned and that a joint use-of-facilities-agreement will be put in place that equitably allocates shared costs between the two facilities. Subsection 13.4 also provides that the real property on which the new plant was constructed will be appraised on the basis of its value as bare land and that PacifiCorp, Washington will be paid its Buyer's Share of an equitable portion of such appraised value by PacifiCorp
- 7 Generation.
- 8 Q. How are the net sale proceeds from the auction to be allocated between PacifiCorp Generation and PacifiCorp, Washington?
- 9 A. Subsection 13.4 contains an allocation formula which seeks to equitably balance the interests of the Company's shareholders and customers and which recognizes any value that PacifiCorp Generation may have contributed to the facility through investments in "repowering" or capacity additions.
- 14 Q. Why is it appropriate for PacifiCorp Generation to receive benefit from such enhanced value?
- 15 A. It is appropriate for this value creation to be recognized in the sharing formula because PacifiCorp Generation's investments in such initiatives are not reflected in the Agreement pricing formula and therefore they have not been supported by PacifiCorp, Washington or its customers.
- 19 Q. Suppose the result of the sharing formula is negative?
- 20 A. This would suggest that the Plant was sold at a loss and would result in a payment from PacifiCorp, Washington to PacifiCorp Generation.
- 22

1 Section 14: Audit Rights

2 Q. What is the function of Section 14 of the Agreement?

3 A. Section 14 permits PacifiCorp, Washington to audit PacifiCorp Generation's

4 records supporting billings under the Agreement for an 18-month period following

5 any such billings. Any discrepancies found in the audit would be repaid with

6 interest.

7 Section 15: Cost Determination Changes

8 Q. Please describe the function of Section 15.

9 A. Section 15 commits both Parties to the Agreement to not unilaterally petition the

10 FERC for a modification in the Agreement terms. A provision such as this is

11 commonly found in power sales agreements in order to assure parties that they will

12 get the benefit of the bargain that was struck.

13 Section 16: Remedies

14 Q. What is the purpose of Section 16 of the Agreement?

15 A. Section 16 establishes the Parties' remedies in the event of a breach of the

16 Agreement by the other Party.

17 Q. Why is it important to specifically describe the Parties' remedies?

18 A. It is critical that a breach of the Agreement not serve as a basis for either Party to

19 contend that the Agreement should be terminated, as that would result in great

20 potential hardship for either PacifiCorp, Washington (and its customers) or

21 PacifiCorp Generation. Therefore, Section 16 of the Agreement contemplates that

22 any Agreement breaches will be remedied only with monetary damages.

- 1 Q. What damages would PacifiCorp, Washington be entitled to in the event there was an unexcused failure by PacifiCorp Generation to deliver Power?
- 2 A. Pursuant to Subsection 16.2, PacifiCorp, Washington would receive "liquidated damages" equal to 125% of the Market Purchase Index applicable to the hour or hours that the Power was not delivered.
- 3 Section 17 through 22: Typical Contract Provisions
- 4 Q. Please describe Sections 17 through 22 of the Agreement.
- 5 A. These sections contain typical contract "boiler plate" which we believe is self-explanatory and unlikely to be controversial.
- 6 Q. Under what circumstances can the Agreement be assigned?
- 7 A. Section 23 of the Agreement provides that any assignment requires the consent of the other Party, except in the event of a merger or consolidation.
- 8 Q. Does this complete your direct testimony concerning the Agreement?
- 9 A. Yes.

1 6) a charge for any new taxes based upon plant emissions.

2 To the extent that load previously served under the Agreement is freed up by direct
3 access, there is provision for a bill credit that reflects the value of the freed-up
4 power in the wholesale market.

5 **Section 1: Definitions**

6 Q. Please describe Section 1 of the Agreement.

7 A. Section 1 contains definitions of terms that are used in the Agreement. I draw

8 attention to a number of these terms as I discuss particular provisions of the

9 Agreement. Capitalized terms used hereafter in my testimony correspond to

10 defined terms in the Agreement.

11 **Section 2: Effective Date and Termination**

12 Q. Please describe the purpose of Section 2.

13 A. Subsection 2.1 establishes that the Agreement will become effective at the same

14 time that PacifiCorp's distribution assets are transferred to the separate state electric

15 companies. Of course, this will only occur after a number of regulatory approvals

16 have been obtained. Subsection 2.2 also provides for an initial Agreement term

17 through the year 2035, with a unilateral right by PacifiCorp, Washington to renew

18 for successive five-year terms. As I explain later in my testimony, when each of the

19 Company's Thermal Plants reach the end of their assumed life, the amount of

20 Power sold under the Agreement at embedded-cost prices is correspondingly

21 reduced. This will occur in respect to all of the Company's Thermal Plants well in

22 advance of 2035. Therefore, as a practical matter, the ultimate term of the