

Rocky Mountain Power  
Docket 07-035-93  
Witness: A. Richard Walje

BEFORE THE PUBLIC SERVICE COMMISSION  
OF THE STATE OF UTAH

ROCKY MOUNTAIN POWER

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Rebuttal Testimony of A. Richard Walje  
Policy

May 2008

1 **Q. Are you the same A. Richard Walje who has previously testified in this**  
2 **proceeding?**

3 A. Yes.

4 **Purpose of Testimony**

5 **Q. What is the purpose of your rebuttal testimony?**

6 A. The purpose of my testimony is to:

- 7 • Explain the ramifications of the Utah Commission's test period order of  
8 February 14, 2008 (Test Period Order), on Rocky Mountain Power.  
9 (RMP).
- 10 • Reiterate the need for a reasonable rate increase at this time.
- 11 • Provide RMP's overall response to the revenue requirement proposals of  
12 the intervening parties in this docket, particularly the position of the  
13 Committee of Consumer Services (CCS).
- 14 • Address some of the proposed modifications to the rate case regulatory  
15 process proposed by the Division of Public Utilities (DPU) and the CCS.

16 **Impact of Test Period Order**

17 **Q. Please explain the impact of the Utah Commission's Test Period Order on**  
18 **Rocky Mountain Power.**

19 A. In the Test Period Order, the Commission shortened the Company's forecast test  
20 period, pointing to the potential impact of economic uncertainties on the  
21 Company's investments and load forecasts. Based upon the Company's  
22 experience in the first quarter of 2008 and its expectations for the balance of the  
23 year, however, there are no material changes in its projected investments or loads.

24 RMP's load continues to grow (particularly in Utah and Wyoming); RMP  
25 continues to make investments at a rate of well over \$100 million per month (on  
26 average) to maintain service; and the costs of materials, equipment and generation  
27 and wholesale power continue to increase faster than the rate of inflation.

28 Because these conditions have all remained steady and are expected to remain  
29 steady throughout the rate effective period, the Commission's Test Period Order  
30 is problematic both in terms of providing timely cost recovery to the Company  
31 and sending customers the correct price signals regarding the cost of their electric  
32 use.

33 **Q. Please provide an update on the Company's load growth in Utah.**

34 A. As compared to the first quarter of last year, Utah customer usage has increased in  
35 the first quarter of 2008 across all classes with industrial and residential showing  
36 the largest increases. As compared to the sales forecast included in this filing,  
37 actual customer usage in the first quarter of 2008 is higher than forecast for  
38 residential and industrial customers, and lower than forecast for commercial  
39 customers. Overall Utah load is above forecast.

40 **Q. Please provide an update on the Company's current investment initiatives.**

41 A. The Company remains fully committed to the system investment necessary to  
42 meet the burgeoning demand in Utah. Indeed, the size and scope of the program  
43 are such that the Company cannot readily slow it to match transitory economic or  
44 regulatory conditions and still meet its projected need for new utility  
45 infrastructure.

46 **Q. Following up on your last response, there was testimony in the test period**  
47 **hearing on how short term changes in economic outlook should be factored**  
48 **into the Company's capital budgeting and forecasting plans. Do you believe**  
49 **that the capital investment plan can or should be started and stopped based**  
50 **on the latest economic indicators?**

51 A. No. The planning, budgeting, design, procurement, property acquisitions,  
52 building and commission of our generation, distribution and transmission  
53 facilities can take from three to eight years, depending on the circumstances  
54 surrounding the investments. In many cases, the Company does not have feasible  
55 alternatives to the projects in the long term investment plan. Without these  
56 investments, the Company will be hard pressed to meet its obligation to provide  
57 safe and reliable power to its customers. For these reasons, it is unwise to expect  
58 the Company to recast its entire capital plan each time there is a national  
59 fluctuation in the Dow Jones Industrial Average, unemployment rate or consumer  
60 price index, especially when such indicia contrast with local conditions that  
61 counter such trends. The Company has a robust long term planning approach,  
62 which is intended to assure to match investments with current customers needs.  
63 The match will never be 100 percent but under the current business environment  
64 it is better to have marginal excess capacity than to have inadequate electric  
65 infrastructure in place to meet the Company's obligation to serve. Additionally,  
66 with the sky rocketing cost of our business inputs, shifting a new facility (such as  
67 a distribution substation) out a year strictly in response to a short-term economic  
68 dislocation, might very well result in higher prices to customers because of the

69 extreme cost increases of steel, concrete and electrical equipment the Company  
70 and all businesses are experiencing.

71 **Q. Has the Company's most recent rating agency report taken note of the**  
72 **Company's large capital expenditure program?**

73 A. Yes. Exhibit RMP\_\_\_(ARW-1R-RR) includes Standard & Poor's (S&P) most  
74 recent credit report on PacifiCorp, which was issued on April 17, 2008. Page 2 of  
75 the S&P report contains the following comment:

76 In 2007, the company invested \$1.5 billion in capital projects that  
77 was funded with approximately \$1.0 billion of debt...\$200 million  
78 in MEHC equity infusions, and the balance with operating cash  
79 flow. The company is embarking on a 10-year, \$20 billion capital  
80 program, of which an estimated \$14 billion will be incurred in the  
81 next five years.

82 **Q. Please provide an update on the external cost pressures the Company faces,**  
83 **particularly in power costs.**

84 A. Net power costs have increased significantly since the time of the Company's  
85 initial filing. The Company's actual power costs for the first quarter of 2008 are  
86 17 percent higher than the level projected in this case.

87 **The Company's Need for Timely Cost Recovery in Rates**

88 **Q. How has the Company responded to these circumstances?**

89 A. Because the Commission's Test Period Order does not allow RMP to avoid  
90 making investments or incurring increased costs, the limitation on the test period  
91 in this rate case has necessarily accelerated the filing schedule of the Company's  
92 next rate case. The Commission's Test Period Order recognized that "In this time  
93 of expanded utility investment, potentially increasing costs, and greater  
94 uncertainty of economic conditions, more frequent rate cases may be necessary to

95 ensure just and reasonable rates.” More frequent rate cases is one way to partially  
96 mitigate the cost recovery issues created by the Test Period Order, and this both  
97 explains and justifies the Company’s plan to now file its next rate case as soon as  
98 practicable.

99 **Q. In your opinion, are there better alternatives to serial, overlapping rate cases**  
100 **to address and ameliorate the serious lag in cost recovery now faced by the**  
101 **Company?**

102 A. Yes, both in the long term (i.e. the next rate case) and short term (i.e. this rate  
103 case). In the long-term, because the Commission’s and interveners’ concerns  
104 about loads and forecasts in this case have not been substantiated, the Company  
105 hopes the Commission will further extend the test period in its next filing to help  
106 slow the cycle of repeat, overlapping rate cases in Utah during the Company’s  
107 investment plan.

108 If the Commission’s concern is to ensure that rates and changes in costs  
109 are more closely synchronized, there are much better regulatory mechanisms to  
110 accomplish that than to revert to use of an historical or foreshortened test period.  
111 Power cost adjustment mechanisms can ensure that rates precisely track positive  
112 and negative changes in net power costs. Generation investment adjustments  
113 mechanisms, such as authorized by Utah Senate Bill 202, allow customers to  
114 receive the benefits of new generation at the same time as they begin paying the  
115 costs. The Company may explore such mechanisms in its next rate filing.

116 **Q. How can the Commission address these issues in this rate case?**

117 A. Most importantly, by approving an overall rate increase at or near the level

118 requested by the Company. As discussed in my opening testimony, Rocky  
119 Mountain Power's need for this revenue increase is primarily driven by cost  
120 increases related to new plant investment and power costs. As discussed above,  
121 the Company's investment levels remain high and its power costs are now  
122 trending at an even higher level than when the filing was made. This, coupled  
123 with the fact that the \$40 million in costs removed from this case as a result of the  
124 Test Period Order were predominantly new investment and power costs, makes a  
125 good outcome in this case critical to the Company's financial position, its  
126 opportunity to achieve its allowed rate of return, and its ability to attract new  
127 capital.

128 **Q. Are there specific issues in this case where the Commission's discretion over**  
129 **the Company's rates can be exercised in a manner that better aligns the**  
130 **Company's rates with its rapidly rising costs?**

131 A. Yes. There are several critical issues in the case where the mismatch between the  
132 Company's actual and projected costs and its rate levels is potentially relevant. I  
133 previously submitted testimony on the Company's cost of capital addressing how  
134 the Company's business risk supported its 10.75 percent return on equity  
135 recommendation. A Commission decision recognizing this business risk and  
136 adopting the Company's return on equity recommendation would help strengthen  
137 the Company's financial position in the face of its large capital investment  
138 program.

139 Additionally, the Company's rebuttal filing has reduced its requested  
140 system net power costs number to \$1.044 billion, a level that is in line with the

141 DPU's recommendation. CCS has proposed system NPC of \$986 million, which  
142 is \$57 million less than the Company and DPU recommendation. The Company's  
143 most recent actual power costs for 12 months ending March 31, 2008 were \$1.024  
144 billion; CCS's recommendation is \$38 million below this number. In reviewing  
145 the reasonableness of the Company and DPU position, on the one hand, and the  
146 CCS position, on the other, the Commission should check the positions against  
147 relevant benchmarks such as this. The Commission should set power costs in this  
148 case at a level that recognizes the realities of increasing loads and rising costs.

149 Finally, the Company has proposed recovery of its incentive compensation  
150 costs and other labor costs, pointing to the improved, more customer-oriented  
151 performance of the Company under MidAmerican Energy Holdings Company  
152 (MEHC) ownership. The Commission can support, reward and encourage these  
153 performance improvements through full allowance of the Company's labor costs.  
154 I discuss this particular issue in more detail below. As represented by the MEHC  
155 acquisition commitments the Commission and interveners have signaled their  
156 desire to take this broader view of the Company's performance.

157 **Q. Did the recent credit report from S&P note the connection between the**  
158 **Company's large capital program and its need for rate increases?**

159 A. Yes. The report states that the Company's "capital program underscores the need  
160 for what is expected to be sizable rate relief in the coming years." The report also  
161 noted that the Company has "below average regulatory protection from fuel and  
162 purchased power cost escalation," due to "an absence of PSAs in Utah,  
163 Washington and Idaho."

164 **Q. Did the S&P credit report also note the importance of the relationship**  
165 **between the Company and the Utah Commission?**

166 A. Yes. Much of the Company's load growth and the investment to serve load is  
167 incurring in Utah. The S&P report notes that "Utah will be an important state to  
168 monitor," in terms of the regulatory support the Company will receive for its  
169 capital investment program.

170 **Q. Does the Company Agree with S&P's observation in this regard?**

171 A. Yes. RMP is focused on providing reliable, reasonably priced electric service to  
172 its Utah customers. We are also dedicated to meeting increased demand from our  
173 Utah customers while maintaining high levels of customer service, a challenging  
174 proposition in today's energy markets coupled with the need to make large  
175 infrastructure investments. We need support from the Utah Commission to  
176 continue to meet this challenge and hope to receive it in this case.

177 **Q. What recommendations have certain interveners made in response to Rocky**  
178 **Mountain Power's announced intention to file another general rate case?**

179 A. Both the DPU and CCS propose modifications to the amount of required  
180 information for filing a general rate case and the time period in which a general  
181 rate case must be completed.

182 **Q. Does Rocky Mountain Power agree with their proposed modifications to the**  
183 **regulatory process?**

184 A. No. As presented, these proposed modifications to the amount of required filing  
185 information for a general rate case and the time period in which a general rate  
186 case must be completed would further delay recovery of costs, create even less

187 opportunity for the Company to achieve its authorized rate of return and provide  
188 poor price signals to customers. These modifications are inconsistent with the  
189 Utah State Legislature’s direction that the Commission use a forward looking test  
190 period when appropriate.

191 The Commission should be particularly concerned that RMP rates are not sending  
192 accurate price signals to customers. The political and popular sentiment is to  
193 criticize utilities for not doing enough to control peak demand and encourage  
194 energy efficiency; yet, it is not reasonable to expect customers to make proper  
195 economic decisions regarding electricity use when we don’t expect or ask them to  
196 pay what it actually costs to provide them with electric service.

197 **Overall Reaction to Intervening Party Recommendations**

198 **Q. As president of Rocky Mountain Power, what is your reaction to the**  
199 **recommendations of the intervening parties in this case?**

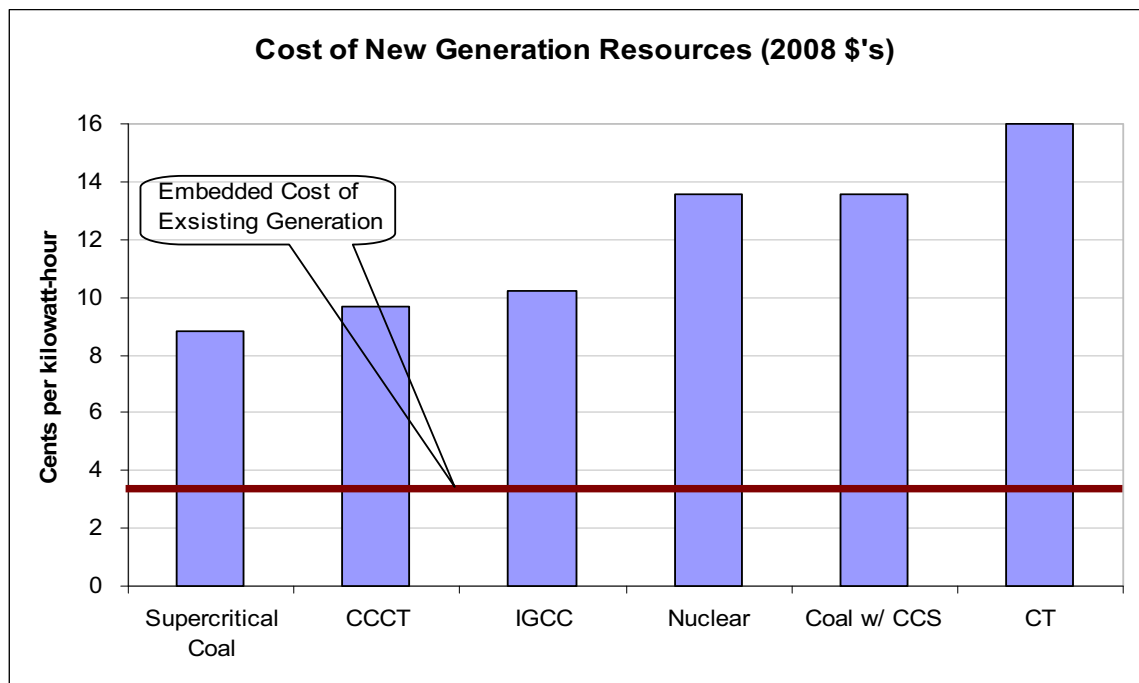
200 A. While five parties filed revenue requirement testimony, only two, the DPU and  
201 the CCS, filed full revenue requirement proposals. With a few notable  
202 exceptions, the recommendations of the DPU appear to be a good faith attempt to  
203 set a reasonable revenue requirement. Indeed, the Company accepts a number of  
204 the proposed adjustments offered by the DPU and has worked with the DPU to  
205 modify several others of their proposed adjustments. The Company does disagree  
206 with several of their proposed adjustments, and other Company witnesses will  
207 address those adjustments in their rebuttal testimony.

208 In contrast, I am disappointed with the recommendations made by the  
209 CCS. RMP has made \$420 million of investment (over \$192 million allocable to

210 Utah) in the six months since the September 2007 end of the test period in our last  
 211 settled rate case. These actual investments over a period of only six months  
 212 support an increase in revenue requirement for that item alone of over \$30  
 213 million; more than three times the total increase proposed by the CCS. Yet, the  
 214 CCS witnesses have recommended a rate increase of less than 1 percent – a result  
 215 that simply cannot be reconciled with RMP’s actual experience.

216 **Q. Please explain why the overall result CCS recommends does not make sense.**

217 A. It is common knowledge that the utility industry faces increasing operating costs  
 218 and capital investment costs. This is illustrated in the following table that  
 219 compares the cost of new resources with current embedded generation costs. The  
 220 supporting data for this table is found in Exhibit RMP\_\_\_(ARW-2R-RR).



230  
 231 (Source: Resource costs are based upon the costs used from the NWPPE region as configured in the IPM® model. The  
 232 NWPPE region includes Nevada, Utah, southeast Idaho, and western Wyoming. Updated resource costs for use in  
 233 PacifiCorp’s IRP and business plan have not yet been finalized and may differ from the costs presented in this table.)

234 I'm personally unaware of one fundamental input to our business that has  
235 increased by less than 1 percent over the past two years, let alone for the totality  
236 of our fuel, metals, concrete, wages, equipment, etc. The global demand for  
237 energy and world-wide competition for scarce resources affect supply and  
238 demand; this has driven the cost of our inputs well beyond the consumer price  
239 index. We believe we do a very good job of controlling our costs but we should  
240 not pretend that Utah is immune from what is happening in the world regarding  
241 fuel and commodity costs.

242 As a direct result of growth in the state of Utah, the Company is  
243 undertaking the most significant capital investment initiative in its history. Every  
244 new generation plant, every transmission line, and nearly every distribution  
245 facility costs significantly more than the cost of similar facilities included in  
246 current rates. In addition, the cost of fuel and purchased power is rising for both  
247 existing and future customers. It seems unreasonable that anyone could expect  
248 that in this environment the cost of serving our customers would increase by less  
249 than one percent over a period of nearly two years.

250 **Q. What is your reaction to the various labor cost disallowances the DPU and**  
251 **CCS propose?**

252 A. In some ways, these are the most distressing disallowances of all. There is a  
253 shortage of qualified utility personnel available in the market. As explained by  
254 RMP witness Wilson, the Company attempts to provide a total compensation and  
255 benefits package that is near the average for the businesses we compete against to  
256 hire and retain good employees. We have already lost several employees to other

257 businesses, especially in the Northwest. If the Commission disallows a portion of  
258 the costs of that market average package and the Company understandably  
259 responds by adjusting that package downward, we will be forced to compete for  
260 employees with a below average compensation and benefits package. I urge the  
261 Commission to recognize that in assessing the reasonableness of the Company's  
262 salary and benefits costs, it should not limit its focus to just one element of the  
263 total compensation package.

264 As a long time employee and manager of the company, I can emphatically  
265 state that now, more than ever, the performance management approach that has  
266 been instituted by MEHC is focused on encouraging and motivating outcomes  
267 that have a direct benefit for customers, including but not limited to: reliability,  
268 safety, customer service, operating efficiencies, environmental stewardship and  
269 good corporate citizenship. The performance plan for which RMP is seeking cost  
270 recovery in rates is based upon employees achieving or exceeding their individual  
271 goals; it is not based upon or contingent upon return to shareholders. MEHC has  
272 another incentive plan for executives that have that objective, and RMP is not  
273 seeking recovery of the costs of that plan.

274 Pay for performance with bonus opportunities, though rarely applied in the  
275 public sector, is common, if not pervasive, in the private sector. And since our  
276 base pay and benefits are average for similar jobs in our labor market, the cost of  
277 the total package cannot be said to be excessive.

278 It is important to note that over 2,400 of the employees affected by the  
279 DPU's and CCS's recommendation live and work in Utah. They are directly

280 affected by these penurious adjustments proposed by these interveners. The  
281 Commission's consideration should be upon the reasonableness of the cost of the  
282 total package and the package's positive impact on customers.

283 **Q. In summary, what would be the consequences of rates based on the revenue**  
284 **requirement proposed by the Committee?**

285 A. The Company has the obligation to serve its customers dependably and reliably.  
286 RMP has made significant progress to improve industrial customer service,  
287 improve reliability, enhance dedication to the communities we serve, deliver cost  
288 efficiencies, and satisfy transaction commitments to elevate local decision-  
289 making. While RMP's efforts seem to have been appreciated or at least expected,  
290 RMP is now confronted with rate proposals that would make it impossible to  
291 continue with those efforts and still maintain its credit quality. RMP cannot  
292 reasonably be expected to continue to make investments and incur costs if rates  
293 do not reflect these investments and costs.

294 **Summary**

295 **Q. Please summarize your rebuttal testimony.**

296 A. In the Company's current circumstances, absent compensating actions by the  
297 Commission, the Test Period Order will deprive RMP of the opportunity to earn  
298 anything close to its authorized return. The interveners' proposed disallowance of  
299 costs, particularly those of CCS, would further increase the shortfall. To mitigate  
300 this result, it is absolutely essential that the Commission recognize the reality of  
301 the Company's cost increases and the investments required to meet its obligation  
302 to serve an ever increasing number of customers. The Company's employees

303 have served its customers well for nearly 100 years and take pride in the  
304 opportunity to do so, as they know they provide a vital service to their friends,  
305 families and communities. We are only asking for a revenue requirement that  
306 allows us to meet growing demand, growing customer expectations and growing  
307 costs, so we can continue to deliver safe, reliable and affordable electric energy to  
308 our customers.

309 **Q. Does this conclude your rebuttal testimony?**

310 A. Yes.