BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF IDAHO POWER COMPANY'S APPLICATION FOR APPROVAL OF A SPECIAL CONTRACT TO SUPPLY POWER TO HOKU MATERIALS, INC.	)	CASE NO. IPC-E-08-21

IDAHO POWER COMPANY

DIRECT TESTIMONY

OF

JOHN R. GALE

Q. Please state your name and business address.

A. My name is John R. Gale and my business address is 1221 West Idaho Street, Boise, Idaho.

Q. By whom are you employed and in what capacity?

A. I am employed by Idaho Power Company ("the Company") as the Vice President of Regulatory Affairs.

Q. Please describe your educational background and business affiliations.

A. I received a BBA in 1975 and an MBA in 1981 from Boise State University. I maintain a close affiliation with the university and serve on the College of Business and Economics' Advisory Council and on the Board of Directors of the Alumni Association. I have also attended the Public Utilities Executive Course at the University of Idaho and am now on the faculty of that program covering "Regulation and Ratemaking."

I am an active member of the Edison Electric Institute's Rates and Regulatory Affairs Committee, which is the committee that is concerned primarily with regulatory issues and ratemaking methods. I am the current Chair of this committee.

Q. Please describe your work experience.

A. From 1976 to 1983, I was employed by the State of Idaho primarily as an analyst in the Department of Employment. In October 1983, I accepted a position at Idaho Power Company as a Rate Analyst in the Rate Department. I initially worked on rate design, tariff administration, and line extension issues. In March 1990, I was assigned to the Company's Meridian District Office where I held the position of Meridian Manager, which was a one-year cross training position established to provide corporate employees with an extensive field experience. I returned to the Rate Department in March 1991 and in June, I was promoted to Manager of Rates. In July 1997, I was named General Manager of Pricing and Regulatory Services. In March 2001, I was promoted to Vice President of Regulatory Affairs, my current position.

As Vice President of Regulatory Affairs, I oversee and direct the activities of the Pricing and Regulatory Services Department. These activities include the development of jurisdictional revenue requirements, the oversight of the Company's rate adjustment mechanisms, the preparation of class cost-of-service studies, the preparation of rate design analyses, and the administration of tariffs and customer contracts. In my current position, I have the primary responsibility for policy matters

related to the economic regulation of Idaho Power Company. I have testified frequently before the Idaho Public Utilities Commission ("the Commission") on a variety of rate and regulatory matters. I have also testified before or submitted direct testimony to the regulatory commissions in Nevada and Oregon, the Federal Energy Regulatory Commission ("FERC"), the Bonneville Power Administration, and the United States Senate Committee on Energy and Natural Resources.

Q. What is the purpose of your testimony in this matter?

A. I will describe the terms and conditions of a new Special Contract consistent with the requirements of Idaho Power's Schedule 19, Large Power Service. The Special Contract is an Energy Services Agreement ("ESA") between Idaho Power Company and Hoku Materials, Inc. ("Hoku"). The accompanying new tariff sheet, Schedule 32, contains the proposed rates for service to Hoku. The ESA is Exhibit No. 1 to my testimony and Schedule 32 is Exhibit No. 2. My testimony will also describe the rationale for each.

Q. Please describe the ESA.

A. The ESA provides for an initial four-year contract term that begins on June 1, 2009, which is the

expected time that Hoku's load should exceed 25 megawatts ("MW") of capacity. The ESA includes a contract demand schedule that allows Hoku to ramp up to 82 MW, while incorporating seasonal peak constraints that Idaho Power expects to experience through 2012. The ESA provides for a hybrid approach to the rate structure for the initial contract term that incorporates both an embedded cost-based price for a 25 MW block of power and a marginal cost-based price for capacity amounts above 25 MW. Finally, the ESA provides for a transition to traditional embedded-cost retail pricing following the initial term.

Q. Is the recovery of the costs for the initial construction of substation and transmission facilities needed to serve Hoku's load addressed in the ESA?

A. No. The cost recovery of the initial construction for substation and transmission facilities needed to serve Hoku is provided for in a separate construction agreement. Through that agreement, Hoku is responsible for the construction costs of the new substation and transmission upgrades, including the income tax impact. Idaho Power retains ownership of these facilities and is responsible for ongoing operating and maintenance costs. Hoku's payment for the substation and transmission facilities was considered in the development

of the rates, the selection of the point of delivery, and the measurement of transmission losses in the ESA.

Q. Why was 25 MWs chosen to establish the pricing blocks?

A. Idaho Power provides tariff service to industrial customers under Schedule 19, Large Power Service. The Applicability Section of Schedule 19 states:

> "If the aggregate power requirement of a Customer who receives service at one or more Points of Delivery on the same Premises exceeds 25,000 kW, the Customer is ineligible for service under this schedule and is required to make special contract arrangements with the Company."

Q. What is the purpose of this provision?

A. The requirement for a Special Contract serves several purposes. First, it allows for the unique characteristics of customers of this size to be captured within the terms of an agreement. Second, special contracts allow for specific cost-of-service information for each large load to be reviewed during rate proceedings. And, third, special contracts provide protection to the Company and the other retail customers from the system impacts that some large loads could impose because of sheer size or operating characteristics.

Q. Does Idaho Power currently serve other special contract customers?

A. Yes. There are currently three: (1) Micron Technology, Inc., located in southeast Boise; (2) the United States Department of Energy's Idaho National Laboratory, located west of Idaho Falls; and (3) the J R Simplot Company's Don Plant, located directly west of Pocatello. These customers range in size from 30 to 85 MWs of load. From 1973 until 2001, Idaho Power also served FMC Corporation under a special contract for up to 250 MW.

Q. What were the regulatory goals Idaho Power was trying to achieve in developing a service plan for Hoku?

A. There were five goals:

1. Provide requested service consistent with system capability and the reliability needs of existing customers.

2. Provide options to the customer when the Company is unable to provide service as requested.

3. Mitigate the rate impact on existing customers by developing a rate structure that includes a marginal price component for an initial term of the service agreement.

4. Require upfront contributions to capital expenditures associated with facilities that specifically serve the customer.

5. Provide a means to quantify known and measurable amounts of additional load for Integrated Resource Planning.

Q. How does the ESA provide the requested service consistent with system capability and the reliability needs of existing customers?

A. Hoku originally requested 82 MW of year-round capacity. Because of supply and transmission constraints, Idaho Power was unable to serve at this level during certain summer months prior to 2012. Hoku and Idaho Power discussed the possibility of Hoku supplying self generation and/or load interruptibility as a means to address the summer difference. Neither option worked well in this particular situation. However, Hoku and Idaho Power were able to devise a seasonally shaped contract demand schedule that would allow Hoku to perform annual maintenance and help Idaho Power avoid additional loads during peak periods prior to 2012. Also, there is a contingency provision that reduces the Company's 2012 capacity obligation in case Idaho Power is not able to add additional generation and/or transmission as planned.

Q. How does the ESA provide options to Hoku when Idaho Power is unable to provide the service as requested?

A. In addition to the seasonally shaped load, there is a provision in the ESA that allows Hoku to request Idaho Power to initiate a summertime request for proposals

to determine whether some additional summertime supply can be secured at an acceptable price.

Q. How does the ESA mitigate the rate impact on existing customers through its rate structure?

A. The proposed rate structure for the Hoku ESA includes an embedded-cost rate for a 25 MW block of power and a marginal-cost rate for loads above 25 MW. The embedded block is capped at 25 MW in recognition that had Hoku limited its load to less than 25 MW, it would have been entitled to buy 25 MW under Schedule 19 at embedded-cost rates. The charges in the ESA for the embedded block are equivalent to the costs a Schedule 19 customer operating at a 90 percent load factor and served at transmission voltage would experience.

The marginal block is applicable to capacity and energy above 25 MW up to the total contracted capacity, specified in the ESA as Contract Demand. The marginal block capacity charges are reflective of transmission access and ancillary services costs, plus some operating and maintenance expenses related to the substation serving Hoku. The marginal energy cost is based on Idaho Power's published avoided cost rates as approved by the Commission, applicable to the relevant contract time period. Marginal costs could have been based on an actual purchase or market

proxy. However, because of the volatility, and perhaps subjectivity, of these methods of determining marginal costs, the avoided cost method is preferred.

Q. How are upfront capital contributions incorporated into the cost of providing service to Hoku?

A. As previously discussed, the cost recovery of the initial construction for substation and transmission facilities needed to serve Hoku is provided for in a separate construction agreement. Through that agreement, Hoku is contributing the construction costs of the new substation and transmission upgrades, including the income tax impact. Idaho Power retains ownership of these facilities and is responsible for ongoing operation and maintenance.

Q. How does the ESA provide a means to include additional load into the Company's Integrated Resource Planning?

A. The ESA provides a contractual capacity commitment from Hoku to take power that, once the Commission approves, the Company can rely upon for resource planning purposes. It is a much stronger commitment than an application for service. In the past we have relied on similar representations for planning. The most recent example of this type of explicit commitment was when Micron

Technology was ramping up to its present size.

Q. Does the hybrid embedded/marginal rate structure remain in place indefinitely?

A. No. The Company proposal is to maintain this rate structure for the initial term of the ESA, which is four years. After the initial term, it is Idaho Power's recommendation that Hoku be treated just like all other special contract customers for ratemaking purposes. The initial four years provides a transition period for Hoku to establish itself as a customer, while providing some rate mitigation for the immediate impact of its load on other customers. It also mutes an inappropriate price signal to potential new large loads that look at our existing rates and conclude that Idaho Power has an unlimited supply of three-cent power.

Q. Why is a transition period reasonable?

A. A transition period provides a balance between the new customer's interest of access to low-cost power and the current customers' interest of mitigating the impact of new loads on their energy costs.

Q. Please describe the component charges for the first or marginal block.

A. There are two "first block" component charges; one for demand and one for energy:

First Block Contract Demand Charges are based on the monthly number of kilowatts the Company has agreed to make available to Hoku in accordance with the scheduled contract demands delineated in the ESA. This Contract Demand is supplied on a "take-or-pay" basis. However, the Company's obligation to supply demand during the load period from 6/16/2012 to 9/15/2012 in excess of the 2011 summer Contract Demand levels, is contingent on the timely completion of the Company's major transmission and generation projects.

First Block Energy Charges are based on the kilowatt-hours computed by multiplying the First Block Contact Demand by the number of hours in the billing period multiplied by the Contract Load Factor of 90 percent. With adequate notice and the written consent of the Company, Hoku may request a release of all or part of its First Block Energy purchase commitment in return for credit on its First Block Energy Charges.

Q. Please describe the charges for the second or embedded block.

A. There are two "second block" component charges; one for demand and one for energy:

Second Block Contract Demand Charges are based on 25,000 kilowatts times the then-current demand charges

delineated in the Company's Schedule 19 tariff sheet applicable to transmission level service. After the Embedded Date of June 1, 2013, these demand charges will be subject to the orders of the Commission.

Second Block Energy Charges are based on the total kilowatts supplied during the billing month less the First Block Energy usage, multiplied by the then-current energy charges delineated in the Company's Schedule 19 tariff sheet applicable to transmission level service. After the Embedded Date of June 1, 2013, these energy charges will be subject to the orders of the Commission.

Q. Why are the Excess Demand Charges included on Schedule 32?

A. The availability of power in excess of the Total Contract Demand (First Block plus Second Block), is not guaranteed. Hoku will be responsible for any damages to the Company or other parties if they exceed their Total Contract Demand. However, if and when Hoku should ever exceed their contact, the Excess Demand will be subject to both daily and monthly Excess Demand Charges.

Q. Please describe the applicability of Schedule 55, Power Cost Adjustment, Schedule 91, Energy Efficiency Rider, and Schedule 95, Adjustment for Municipal Franchise Fees, to the Hoku ESA and Schedule 32.

A. The Power Cost Adjustment (Schedule 55) bill component is computed by multiplying the adjustment amount by the kilowatt-hours being charged under the Second Energy Block component *only*. The reason for only applying the PCA rate to the Second Block is discussed in greater detail later in my testimony.

The Energy Efficiency Rider (Schedule 91) charge is computed by multiplying the rider percentage times the sum of the monthly billed charge components in the Second Block, except for the Power Cost Adjustment.

The Adjustment for Municipal Franchise Fees (Schedule 95) charge is computed by multiplying the fee percentage by the sum of all the monthly billed charge components, including the Power Cost Adjustment.

Q. What PCA treatment do you propose for the new ESA?

A. I propose that all the costs of supplying power to both the First Block Energy and Second Block Energy be included in the PCA. Additionally, revenues from the First Block Energy would be treated as a surplus sale and an offset to power supply costs. Accordingly, First Block Energy - the marginal block - would not be included as Idaho retail load and the First Block Energy rate would not adjust each year with the PCA. Second Block Energy -

embedded block - would be included as an Idaho retail load and would adjust each year with the PCA. Essentially, we are treating the First Energy Block as if it were a four-year off-system sale. This PCA treatment is similar to the approach authorized when the FMC special contract was served under two blocks, one priced at embedded rates and one at market rates.

Q. Is it your opinion that the approval of the ESA between Hoku and the Company is in the public interest?

A. Yes. Idaho Power and Hoku have worked together to fashion an agreement that reflects current energy economic realities (i.e., the existing supply of low cost energy is finite, while new sources of power supply are expensive). The ESA incorporates these economics in a workable and equitable way that works for both the new customer, for the system, and for existing customers.

Q. Does this conclude your testimony?

A. Yes, it does.