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Q. Please state your name and business address for the record.

A. My name is Stephanie Miller. My business address is 472 West Washington Street, Boise, Idaho.

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

A. I am employed by the Idaho Public Utilities Commission as Director of the Utilities Division.

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

A. The general purpose of my testimony is to address the two alternatives Idaho Power Company has proposed in this case. Specifically, I will recommend that the Commission issue a certificate for the present convenience and necessity for the Milner Project. I will also address the proposed certificate of exemption alternative in the event the Commission should consider this option.

Q. Did Idaho Power express a preference for one alternative over the other in its application?

A. No, it did not. It did not state which alternative the Company would prefer. Neither did it explain why either alternative would be a benefit to

1 Idaho ratepayers or whether one alternative was better
2 for ratepayers than the other.

3 Q. Did the Staff investigate the reasonable-
4 ness of Idaho Power's commitment estimate for the
5 Milner Project?

6 A. Yes. Staff auditor Jack Taylor reviewed
7 the information upon which the Company relied for its
8 commitment estimate. He concluded that the manner in
9 which the estimate was made was reasonable and that
10 with careful management, the Company should be able to
11 bring the project on line at or below the \$63,350,600
12 commitment.

13 Q. Mr. Faull has tested the cost-effective-
14 ness of the Milner Project by comparing its cost to
15 avoided cost rates offered to cogenerators and small
16 power producers. How do the rates customers would pay
17 if the plant is rate based at \$63,350,600 compare to
18 the hypothetical avoided cost rates calculated by
19 Mr. Faull?

20 A. Over the 46-year life of the project
21 ratepayers would pay only slightly more for power from
22 the Milner Project than for comparable power from
23 cogenerators or small power producers as estimated by
24 Mr. Faull. However, under rate of return regulation
25 customers would pay considerably more in the early

1 years of the plant's life than with an avoided-cost-
2 based contract.

3 There are some basic differences between
4 the way costs are recovered from customers through
5 traditional ratemaking and through contracts using
6 avoided cost rates. Avoided cost rates are levelized
7 over the life of the power contract and increase only
8 slightly as operating and maintenance expenses increase
9 (or, theoretically, decrease slightly as O&M expenses
10 decrease. The capital costs associated with a rate-
11 based plant are not levelized; they are higher in early
12 years and lower in later years as the plant is
13 depreciated. This is especially true for hydroelectric
14 facilities with their high construction costs and
15 relatively lower operating and maintenance expenses
16 over the life of the plant.

17 Mr. Faull has calculated a levelized
18 cost for the Milner Project of 62.73 mills per kwh.
19 Using Mr. Faull's assumptions, first year costs of the
20 project under traditional regulation would be 74.14
21 mills per kwh.

22 If the power generated at the Milner
23 Project could be sold at an average rate of 33 mills
24 per kwh, the Company would need a rate increase from
25 its customers of \$7.7 million, or approximately 1.9%,

1 as a result of including the project in rate base. If
2 the Company were to buy a comparable amount of power at
3 the hypothetical contract rate calculated by Mr. Faull
4 of 61.35 mills per kwh from a cogenerator or small
5 power producer and receive the same 33 mills for the
6 power, the net increase to ratepayers would be \$5.3
7 million, or approximately 1.3%. If the power were not
8 needed and had to be sold strictly on the secondary
9 market, the increase experienced by ratepayers would be
10 larger. At a secondary sales price of 20 mills, the
11 increase would be 2.4% with rate basing and 1.9% with a
12 power supply contract.

13 After 7 years, the average cost of the
14 power would be less with the plant in rate base (64.50
15 mills per kwh) than with a levelized power supply
16 contract including an adjustable portion that had
17 escalated, increasing the rate to 65.03 mills per kwh.

18 Q. How firm are these numbers?

19 A. These numbers are estimates to help the
20 Commission make a decision on whether it is reasonable
21 to grant Idaho Power a Certificate of Convenience and
22 Necessity. The Company's commitment estimate is just
23 that, an estimate. Mr. Faull's hypothetical avoided
24 cost rate is his estimate of a 46-year avoided cost
25 rate. The Commission has not approved such a rate.

1 Q. Based on this information, should the
2 Commission grant Idaho Power a Certificate of
3 Convenience and Necessity for the Milner Project?

4 A. Based on this showing that the cost of
5 the Milner Project is approximately the same as avoided
6 cost rates and other policy considerations discussed by
7 Mr. Eastlake, I believe the Commission should grant a
8 certificate for the present convenience and necessity.

9 Q. Does your recommendation to the
10 Commission mean that the Milner Project should
11 inevitably be included in rate base at \$63,350,600 or
12 more if escalation and scope changes occur?

13 A. No, it does not. If the Company is able
14 to construct the project for less than the commitment
15 estimate it would enter rate base at the lower amount.
16 Also, whether the cost is \$63,350,000 or a number lower
17 or higher, only construction costs found prudent by the
18 Commission will enter rate base.

19 The granting of a certificate simply
20 means that the Company may proceed with construction
21 with the understanding that the plant will ordinarily
22 be included in rate base if major changes in either the
23 cost of the project or the environment in which the
24 Company operates do not occur between granting the
25 certificate and the completion of the project.

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Idaho Power should be reminded that a Certificate of Convenience and Necessity is not an order to complete a project. It is authority to proceed with a project or a guarantee it will be rate based. If major project scope or escalation changes do occur, or if the Company's projected power needs change, the Company should use its good management judgment to decide whether to proceed. The filing of quarterly construction reports will keep the Commission and Staff generally informed about progress on the project, but the Commission is not in the business of managing the Company's construction program. The Company is. Neither should the Commission be in the business of prospectively insulating the Company from charges of mismanagement if the Company completes a certificated plant under circumstances that have changed since the certificate was issued when those circumstances would have counseled against the plant had they been known earlier.

By the same token, the Commission and other parties should recognize that the Company is proceeding with the project under the assumption that it will be used to serve its utility customers. The Company should not be asked to bear all costs of the

1 plant on its own if there are changed circumstances,
2 provided it reacts prudently to those changes.

3 Q. Idaho Power has presented an alternative
4 to including Milner in its regulated rate base. Would
5 you describe your understanding of what has been
6 proposed?

7 A. If the Commission determines that it is
8 not reasonable for the Company to construct the Milner
9 Project for its regulated utility customers at this
10 time, Idaho Power requests the Commission issue a
11 Certificate of Exemption that would allow the Company
12 to operate the facility on an unregulated basis through
13 an affiliate for a 20-year period. At the end of the
14 20-year period, the Company would be obligated to offer
15 the project to the Commission for service to its
16 regulated utility customers at that time. The Company
17 asks the Commission to agree to allow the plant to
18 enter rate base at that time at "reproduction cost new,
19 less depreciation".

20 Q. Is this a reasonable proposal?

21 A. I think it is a new and innovative
22 regulatory approach. It would give Idaho ratepayers an
23 option on resources that may not be needed now, but may
24 very well be desirable in the future. There are prime
25 hydroelectric sites in the Idaho Power service area

1 that are very attractive to utilities serving areas
2 outside Idaho. A surplus on the Idaho Power system
3 would preclude Idaho Power under current regulatory
4 practices from developing the sites for its customers.
5 If development is delayed until power is needed, the
6 site may no longer be available. For example, in the
7 early 1980s, Idaho Power was interested in building
8 generating facilities at Lucky Peak Dam, but it did not
9 need the power. Seattle City Light is now generating
10 power at Lucky Peak for use by its customers in
11 Washington.

12 Mr. Eastlake has addressed policy issues
13 important to the development of hydroelectric generation
14 in Idaho. As Mr. Eastlake points out hydropower
15 resources in the state have resulted over the years in
16 Idaho Power customers paying some of the lowest rates
17 for power in the country. Idaho Power's proposal would
18 give Idaho ratepayers an option on such facilities in
19 the future, even if they were not needed today.

20 Although I like the concept proposed by
21 the Company, I have some concern about how it would
22 actually work.

23 Q. What are those concerns?

24 A. My first concern is the detail in which
25 the application spells out reproduction cost new, less

1 depreciation. At first blush, it sounds reasonable.
2 The utility should be compensated for the gain in the
3 value of the plant during the time it was used for
4 contract sales. The Idaho Commission has generally
5 subscribed to the "original cost" theory of ratemaking,
6 allowing plant into rate base at the value (ordinarily
7 the reasonable investment) at which it was originally
8 devoted to public service. Under Idaho Power's
9 alternative proposal, that would be the value 20 years
10 from now.

11 I am concerned that by specifically
12 prescribing how reproduction cost new, less depreciation
13 will be determined, the Company has offered an option
14 that may very well be no option at all. The method
15 described by the Company will in all likelihood produce
16 a "price" that will not reflect the true value of the
17 plant to be "acquired" by ratepayers when it is
18 dedicated to public service and, therefore, will be
19 rejected.

20 Idaho Power proposes to determine the
21 cost to "duplicate" the Milner Project at future costs
22 for all materials, supplies, labor, land and land
23 rights, transportation, etc. This would ignore contem-
24 porary products and new technologies that would be
25 available 20 years from now. Not only might the

1 physical plant be quite different, but labor and
2 construction methods used to construct a plant might
3 also have changed significantly.

4 The Company would then reduce the cost
5 of the duplicate plant by an amount representing the
6 straight-line accumulation of depreciation of the
7 reproduction costs. Once again it would ignore the
8 fact that the plant had become to a certain extent
9 obsolete, requiring increased maintenance expense, and
10 would not be the most valuable plant for generating
11 power because technological improvements had resulted
12 in reduced costs, better designs, and enhanced ability
13 to provide service.

14 I am also concerned about the practical
15 matter of determining reproduction costs. It will be
16 no easy matter. The Commission will be faced with a
17 variety of cost estimates made by thoroughly reputable
18 engineers who will disagree on what the reproduction
19 cost of the facility would be. The following is an
20 excerpt from an Iowa State Commerce Commission Order:

21 The most serious defect of reproduction
22 cost, and, therefore, of the "fair
23 value" method, is that it has no
24 kinship with fact or reality. It is a
25 mass of assumptions, estimates having
no sound foundations in fact,
speculations, and conjecture. (We do
not condemn reproduction cost because
estimates are involved. Estimates are

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often involved in rate making and in many business matters. But there is a difference between estimates having a solid foundation of fact and estimates derived from hypothesis and assumptions. Such estimates are involved in reproduction cost. They are built on foundations of sand and have no probative force.) Subjective judgments of the engineers preparing the reproduction cost regarding the methods of pricing to be used, the assumptions as to construction, and other elements involved in the construction of utility properties, are so vital to the process that no two valuation engineers arrive at the same result and differ so widely as to cast grave doubt on the results of each. Reproduction cost departs from the solid ground of fact and embarks upon guesswork. Scores of items are involved on which equally competent judgments might produce widely divergent results. Final figures appear to be so painfully precise, yet they are built upon an hypothesis so unreal as to make the exactness ludicrous.

Re Davenport Water Co., Iowa State Commerce Commission, September 27, 1968 76PUR3d 220.

No doubt, reproduction costing has also experienced technological changes since the Iowa Order was issued in 1968. This may make decision-making easier, and then again may make it more difficult if the Commission is deluged with computer models all professing to estimate the same thing and arriving at a different result. I include this quotation from the Iowa Order because it illustrates a Commission's

1 frustration when faced with a case that revolves
2 around conflicting subjective judgments of a number of
3 highly qualified expert witnesses.

4 Q. Do you have a recommendation as to how
5 the plant might be valued 20 years in the future?

6 A. I think the most sensible thing to do
7 would be to replace the reproduction cost language
8 with a general statement that the Commission would
9 determine the value of the plant at that time for rate
10 making purposes. The Commission is not now restricted
11 to book cost, but may ascertain the value of utility
12 property "and every fact which, in its judgment, may
13 or does have any [b]earing on such value." Idaho
14 Code, §61-523.

15 If the Commission and the Company are
16 uncomfortable with the uncertainty that such a general
17 provision would provide, I have an alternative. That
18 alternative would be to bring the plant into rate base
19 at original cost less depreciation accrued using the
20 annuity method. The annuity method levelizes the
21 capital costs of a project over the project life by
22 applying low depreciation rates in early years when
23 required return is high and high depreciation in later
24 years when required return is lower. This method was
25 used in the past for hydroelectric projects like the

1 Hells Canyon Complex of three dams. This approach
2 would have the advantage of relying on verifiable
3 booked costs but would recognize that any power sale
4 made by the Company would probably be based on the
5 levelized cost of the project. Using the 11.447%
6 return from the Idaho Power Avoided Cost Order No.
7 23357 assumed depreciation using this method over 20
8 years would be \$3,374,140 on an original cost of
9 \$63,350,600. The assumed depreciated value of
10 \$59,976,500 would be the price at which the plant was
11 transferred from the affiliate to the utility.

12 Q. If neither of these changes is accepted,
13 would you recommend accepting Idaho Power's proposal?

14 A. If a project is clearly not currently
15 cost effective to Idaho Power's customers, but appears
16 to be a good long-term resource, I would recommend
17 approval. If someone other than Idaho Power builds
18 the plant, ratepayers would have no option on the
19 facility, and any option is better than no option at
20 all. It should be understood, however, that if
21 restricted to the Company's proposed use of reproduc-
22 tion cost, the value of the option to ratepayers may
23 not be high.

24 Q. Is the use of reproduction cost as
25 defined in the Company's application your only concern?

1 A. No, it is not. Idaho Power proposes to
2 operate an exempted plant through a subsidiary that
3 would contract with a third party for a long-term sale
4 of the power. I am also concerned about the ability
5 of Staff to insure that there is no subsidization of
6 the affiliate by the utility and its ratepayers.

7 At a minimum, the Staff would have to
8 have access to the power sales contracts signed by the
9 affiliate to determine exactly what the conditions of
10 the power sales contracts are. The staff would also
11 require access to the books of the subsidiary so that
12 transactions between the utility and affiliate could
13 be traced. In the case of Milner, which is located in
14 the heart of the Idaho Power service area, the staff
15 would also need to see load and dispatch data to
16 ensure that system power was not being used to supply
17 the third party purchaser unless the utility was
18 explicitly compensated for the power. Even with
19 careful segregation of costs and cost allocations
20 between the affiliate and utility, there would still
21 be aspects of the relationship between utility and
22 affiliate that would be unquantifiable, but that might
23 very well result in higher prices obtainable by the
24 affiliate for its power.
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Q. Do you consider your concerns about cost allocation and monitoring the activities of the power supply affiliate to be insurmountable barriers to the alternative proposed by the Company?

A. No, I do not. I do consider them to be important issues that would have to be worked out between the Commission and the Company before final approval could be given.

Q. Do you have a final comment on Idaho Power's second alternative, the proposed certificate of exemption?

A. Yes. The legal staff advises me there is no statutory basis for such a certificate. The Commission may, however, authorize construction of the project for the **future** convenience and necessity, not merely for the **present** convenience and necessity. This certificate could incorporate the terms of the Company's proposed certificate of exemption.

Q. Does this complete your testimony?

A. Yes, it does.

CERTIFICATE OF SERVICE

I HEREBY CERTIFY THAT I HAVE THIS 9th DAY OF NOVEMBER, 1990, SERVED THE FOREGOING **DIRECT TESTIMONY OF STEPHANIE MILLER**, CASE NO. IPC-E-90-8, ON ALL PARTIES OF RECORD BY MAILING A COPY THEREOF, POSTAGE PREPAID, TO THE FOLLOWING:

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