

BEFORE THE PUBLIC SERVICE COMMISSION OF WYOMING

IN THE MATTER OF THE APPLICATION OF)
BLACK HILLS POWER, INC., FOR GENERAL) Docket No. 20002-75-ER-09
RATE INCREASE TOTALING \$3,819,393 PER) Record No. 12336
ANNUM)

PRE-FILED DIRECT TESTIMONY OF

Denise Kay Parrish

On Behalf of the Office of Consumer Advocate

Testimony Filed: April 9, 2010

Hearing Begins: May 10, 2010

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Denise Kay Parrish and my business address is 2515 Warren Avenue, Suite 304, Cheyenne, Wyoming 82002.

Q. WHAT IS YOUR OCCUPATION?

A. I am currently the Deputy Administrator of the Wyoming Office of Consumer Advocate (OCA). In this position, I review and provide input into the recommendations made by the OCA. I review utility applications filed with the Wyoming Public Service Commission (Commission) and provide advice to the Administrator regarding the involvement the OCA should have, if any, in the various cases. I review applications, perform analyses and provide recommendations to the Commission relative to various utility matters, including revenue requirements, tariff language, competitive issues, rules and regulations, and other items. I write and issue press releases, perform special studies, as well as provide information and research to customers, the legislature, the OCA Administrator, and others. I do other assignments and tasks, as needed and as assigned by the OCA Administrator.

Q. WHAT IS YOUR EDUCATIONAL AND PROFESSIONAL BACKGROUND?

A. In 1976, I graduated from Michigan State University with a Bachelor of Arts degree in Accounting. I have spent nearly thirty-three years as a regulator of public utilities, having been on the staff of four state utility regulatory commissions and two consumer advocate entities. More than eighteen of these years have been spent at the Wyoming Public Service Commission, some with the Rates and Pricing Section (now part of the technical advisory staff) and some with the Office of Consumer Advocate. I have taken classes related to various aspects of public utility regulation, including income taxes, regulatory accounting, capital recovery, cost-of-service, rate design, revenue requirements, separations and allocations, and other specialized topics. I have taught classes on issues of accounting standards, general ratemaking principles, affiliate transactions,

regulatory accounting, financial reporting, and other specialized topics to regulatory professionals.

Since 2002, I have been a member of the program faculty at the Michigan State University Institute of Public Utilities. I have also worked with the Nigerian Communications Commission on regulatory accounting and reporting matters and have done work for the International Telecommunications Union as a seminar leader. Furthermore, I have participated in several meetings of the Tariff and Pricing Committee of the Energy Regulators Regional Association (ERRA) and have been asked to be a permanent representative to that ERRA Committee. I was a presenter at, and participant in a workshop sponsored by the Energy Group of the Institute of International Education (IIE) regarding the development of an Electricity Distribution Indicator Toolkit. I was a panelist/presenter at a Consumer Workshop in conjunction with the World Forum on Energy Regulation III. Finally, I have been appointed by NARUC to be member of the International Confederation of Energy Regulators (ICER) Virtual Working Group on Competitiveness and Affordability.

I am the past chair and a current member of the National Association of Regulatory Utility Commissioners' Staff Subcommittee on Accounting and Finance. I am the current chair of the NARUC Staff Subcommittee on International Relations. I am a member of the National Association of State Utility Consumer Advocates' (NASUCA) Tax and Accounting Committee. Finally, I am a member of the staff of the Federal-State Joint Board on Universal Service.

Q. DO YOU HAVE EXPERIENCE AS AN EXPERT WITNESS?

A. Yes. I have testified in many cases before regulatory bodies and several years ago stopped counting the number of cases I have been involved in when the number reached one-hundred twenty five. I have testified before the Michigan Public Service Commission, the Colorado Public Utilities Commission, the Colorado

District Court, the Arizona Corporations Commission, the Wyoming Public Service Commission, the Wyoming Legislature Joint Corporations Committee, the Federal Energy Regulatory Commission, and the Federal-State Joint Board on Universal Service. I have testified in telecommunications, water, wastewater, electric, and natural gas cases. The subjects upon which I have testified include revenue requirements, rate design, cost-of-capital, nuclear decommissioning, accounting deferrals, adjustment mechanisms, income taxes, capital recovery, universal service funding, and other specialized topics.

Q. WHO DO YOU REPRESENT IN THIS PROCEEDING?

A. As a member of the Office of Consumer Advocate, I represent the interests of Wyoming citizens and all classes of utility customers in this public utility matter, as required by W.S. § 37-2-401. It is neither my intent nor my charge to represent the position of any individual, group, municipality, or corporation.

Q. WHAT COURSE OF ACTION IS AVAILABLE TO INDIVIDUAL CONSUMERS OR OTHER INTERESTED PARTIES IF THEY WISH TO PURSUE ISSUES NOT ADDRESSED BY THE OFFICE OF CONSUMER ADVOCATE, OR TAKE A DIFFERENT POSITION FROM THE OFFICE OF CONSUMER ADVOCATE?

A. Consumers and other parties may intervene in the proceedings and raise additional issues not addressed by the Office of Consumer Advocate, and may take different positions than those presented by the OCA. Consumers may also present written or oral comments at the hearing, which then become part of the record in the case and are available to the Commission as it makes its decision on any particular proposal or suggested change. The OCA encourages the participation of the public and all interested parties in cases before the Commission.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. The purpose of my testimony is to present the recommendations and concerns of the Office of Consumer Advocate relative to Black Hills Power's proposed rate increase, including matters related to its computed required revenues, its cost of service, and its rate design. My testimony is offered to the Commission in conjunction with the testimony of Mr. Bryce Freeman, Administrator of the Office of Consumer Advocate who specifically addresses issues related to the appropriate rate of return that may be authorized in this proceeding.

Q. ARE YOU SPONSORING ANY COMPUTATIONAL SCHEDULES AS PART OF YOUR DIRECT PREFILED TESTIMONY IN THIS PROCEEDING?

A. Yes. I am sponsoring OCA Schedules DKP-1 through DKP-32. These schedules have been prepared by me and will be explained throughout the remainder of my testimony below. The testimony narrative and associated schedules are an integrated package that is intended to support the OCA's position as it is offered in this proceeding.

Q. PLEASE BRIEFLY DESCRIBE THE NATURE OF THIS PROCEEDING.

A. This proceeding constitutes what is often called a rate case or a request to change the rates that Black Hills charges its customers for the provision of electrical service to its Wyoming customers. While Black Hills Power also provides electricity service to retail customers in South Dakota and Montana, the Commission's jurisdiction only extends to the rates and services provided by Black Hills to customers within Wyoming. Its service territory in Wyoming is a relatively small piece of the overall system, constituting less than 10% of its retail energy usage and system peak. That, however, does not make Black Hills Power a small company. In fact, it is a growing company in that it has recently purchased existing utility operations from Aquila and in doing so, expanded its natural gas operations throughout the middle part of America. It also owns Cheyenne Light Fuel and Power, and has unregulated operations, primarily related to constructing and operating electrical generating stations.

The fact that Black Hills is a midsize company, and perhaps approaching the status of a larger company, while providing service to a fairly small portion of the Wyoming population (a few thousand customers), creates some situations that directly impact this proceeding. Specifically, the derivation of Wyoming's portion of the overall system's costs is driven by the cost allocation process. This allocation process is delineated in great detail in the two cost allocation manuals that have been provided as exhibits to Mr. Cleberg's testimony.

Q. ARE YOU TAKING ISSUE WITH THE CORPORATE ALLOCATIONS UTILIZED IN THIS PROCEEDING?

A. No, I am not. In fact, I am very pleased with the level of detail and information that is contained within the two cost allocation manuals. (One is for Black Hills Utility Holdings, Inc. and one is for Black Hills Service Company.) The manuals are some of the more detailed cost allocation manuals that I have read and provide a reasonably clear step-by-step explanation of the corporate allocation process, thus eliminating many ambiguities that often exist when a great deal of subjectivity is left to those trying to implement less detailed policies.

This does not mean that if I were developing a cost allocation manual it would precisely mirror those provided by Black Hills. Reasonable people can differ on their views of what factor(s) best allocates a particular cost to a department or subsidiary. For instance, there was one particular allocation based on gross plant and I found this unusual, since it is much more common to see allocation factors based on utilized net plant. However, that doesn't mean that one is wrong and one is right. Often, the difference that results when a particular factor is replaced with another is insignificant, assuming that both alternatives are reasonably related to the causation of the cost.

I was comfortable that the costs that result from the use of these manuals are acceptable for purposes of this case. However, cost manuals function best when

they are so-called *living documents* that are periodically reviewed and tweaked, as necessary, to represent on-going corporate structures. Significant changes in costs allocation factors or processes, or significant changes to the underlying corporate structure would warrant further discussion between Black Hills and the Commission (and hopefully, the OCA). An example of this would be if Black Hills and Cheyenne Light were to ultimately merge their generating resources into one integrated entity that shared both service territories.

Q. PLEASE DESCRIBE HOW YOU PREPARED YOURSELF TO MAKE THE RECOMMENDATIONS THAT YOU ARE MAKING IN THIS PROCEEDING?

A. I took a multitude of actions to understand Black Hills's rate request as best as time would permit. This included spending nearly a week in Rapid City, South Dakota at Black Hills corporate headquarters to meet with some of the Black Hills witnesses and further explore some of the proposals that are being made. While in Rapid City, I obtained and examined various records of the Company and have had numerous follow-up conversations on the issues that arose during that initial visit in December 2009. I also did some research on Black Hills' past regulatory filings before the Wyoming Commission to learn from those past cases and particularly the Commission's comments regarding those past requests. I was a witness before the Commission in the proceeding where Black Hills was granted its certificate of public convenience and necessity to construct the Wygen III generating station – the most significant cost driver behind the request to increase rates. I reviewed the inquiries of the Commission Advisory Staff to Black Hills and Black Hills responses thereto and found them to be quite helpful and informative of the issues – particularly providing updates to some of the information that I had examined earlier in the process.

While I certainly don't know as much about Black Hills as do the Company's own witnesses, I have made a sincere attempt to educate myself on the matters of

the case before commenting on them and before making recommendations in this proceeding.

Q. MS. PARRISH, DOES THAT MEAN THAT YOU ARE COMFORTABLE THAT YOUR CASE IS COMPLETE AND SHOULD BE ACCEPTED IN TOTAL AS THE ULTIMATE SOLUTION TO THE ISSUES IN THIS PROCEEDING?

A. Of course not. Taking such a position would be precocious and inappropriate, in that I have already indicated that some of the matters before the Commission in this proceeding are subjective and subject to differences in positions by reasonable people. However, the OCA has attempted to provide as complete a package of recommendations as possible, in order to offer a formal alternative to some of the issues in this case to the recommendations made by Black Hills Power. This is particularly true in regard to the rate design portion of the rate case. While I am not offering formal tariff sheets and similar documentation, I am offering an alternative rate design proposal, and it includes specific rates for the Commission's consideration. However, the Commission needs to fully explore all of the issues that it has identified as concerning or curious, and be satisfied that the solutions offered are not only feasible but are also prudent and in the public interest.

Furthermore, to be quite frank, there were certain aspects of this matter that were not given the attention that I had hoped to give them in the time allotted. I simply ran out of time before I accomplished everything on my to-do list. Among the items in this category are (1) a good and complete read of the proposed changes to the tariffs and (2) a more in-depth analysis of the historical cost trends for Black Hills Power. Yet, I am comfortable that my testimony touches on the key elements of the requested rate increase and that my recommendation may be considered to be prudent and in the public interest.

Q. BEFORE DESCRIBING THEM IN MORE DEPTH, PLEASE PROVIDE A SUMMARY OVERVIEW OF THE OCA'S RECOMMENDATIONS IN THIS MATTER.

A. To cut to the chase, the OCA is recommending that Black Hills Power be granted an increase in its Wyoming retail electric service revenues of about \$3.1 per annum, instead of its requested \$3.8 million per annum. A summary of how both of these amounts are derived and the key differences between them are shown on my OCA Schedule DKP-1. One of the most significant differences is the appropriate return on assets that is recommended to be incorporated into the calculation of the rates. The remaining differences are comprised of quite a number of smaller adjustments to both the rate base and the income statement. These are found on my attached schedules and will be described below.

Q. ARE THERE ANY UNUSUAL ASPECTS OF THIS CASE THAT SHOULD BE KEPT IN MIND AS YOU DESCRIBE YOUR RECOMMENDATIONS?

A. Only one aspect of the case is unusual, and that relates to the long period that has lapsed since Black Hills' last changed its electric rates in Wyoming. It has been approximately fifteen years since Black Hills applied to the Wyoming Commission to increase its general service rates in Wyoming. This is a bit surprising given that Black Hills voluntarily gave up its commodity balancing account / pass-on mechanism as part of the settlement reached with the parties in its most immediate past rate case. In consideration of Black Hills' lack of recent Wyoming rate cases, and in light of the new power generating plant for which it seeks recovery in rates, the size of the increase in this case should not be surprising.

The other aspects of this matter are more common. The test year is primarily historic with known and measurable adjustments but is based on a *year-end* rather than *average* test period. Year-end test periods have been being used for Black Hills ratemaking for decades as well as for other Wyoming utilities. As described in a November 27, 1997 order authorizing changes in rates in Docket No. 9339,

Sub 3, “We have consistently held that the rate base should be determined on an original cost basis, and we have used end of the test year figures to minimize lag and to give cognizance to the fact that rates are made for the future.” The test year in this case follows that same pattern of including plant that is just now coming into service in anticipation of the upcoming rate effective period.

Another aspect of this rate case that is consistent with past Black Hills’ practices is the use of the *average and excess* method of making class cost of service determinations. This is a method that has been used consistently in past Black Hills’ rate cases. However, it is not without some controversy in this proceeding, as I will discuss later in my testimony. Other significant disagreements between the Company and the OCA relate to the appropriate rate design that should be used to develop tariff charges in this matter.

Q. NOW THAT YOU HAVE PROVIDED SOME CONTEXT FOR YOUR RECOMMENDATIONS, PLEASE BEGIN THE MORE DETAILED DISCUSSION OF YOUR REVENUE REQUIREMENT RECOMMENDATIONS.

A. I have already directed your attention to OCA Schedule DKP-1, my schedule that summarizes the OCA’s calculation of the required rate increase of slightly more than \$3 million per annum, or a percentage increase of about 30%.

Q. IN LIGHT OF THE SIZE OF YOUR RECOMMENDED INCREASE, DID YOU CONSIDER ANY RECOMMENDATIONS THAT COULD MITIGATE THE IMMEDIATE IMPACT OF THE RATE INCREASE?

A. Yes and no. The OCA had originally planned to offer some ideas of *levelizing* or *phasing-in* the rate increase such that current customers would see less of an immediate impact on their bills. However, after offering some similar ideas in the recent (and still pending) rate case for Montana Dakota Utilities, it was clear that there were some concerns of that Commissioners and others that needed to be reconsidered. In fact, Chairman Mimier offered the comment during the MDU

hearing that rethinking but not necessarily giving up on the OCA levelization proposal might be appropriate. However, given the schedule of filing testimony in this proceeding relative to the timing of the MDU proceeding has not allowed adequate time to fully re-address the concerns that were raised. Thus, the OCA is in the position of offering a more traditional analysis in this proceeding, with the unfortunate result of a large increase at the time that a new generating plant is included in rates for cost recovery.

Q. WHAT IS SHOWN ON OCA SCHEDULE DKP-2?

A. This schedule shows the process that was used to derive the Wyoming specific rate base that is one of the foundational elements for determining the rate that result from this case. Starting from the left side of the page and moving right, the first column shows the plant and asset values taken from the Company's records before any normalizing adjustments or other adjustments are made. The next column is simply a summary of the adjustments that Black Hills has offered in its application. Summing these first two columns results in the "as adjusted" group of assets upon which it argues it should be permitted to earn a return. However, these figures still are reflected of the total company operations for all of its jurisdictions (including what may be thought of as the FERC jurisdiction for transmission). Thus, the next step is to apply an allocation factor such that the rate base will reflect only the Wyoming jurisdictions portion of the rate base.

The allocations are detailed within the Company's application and are also shown on OCA Schedule DKP-25. This is a schedule that on a comparative basis allows one to walk through the interjurisdictional allocation methods used for determining the amount assigned to each state and comparing it to the allocator used when assigning costs to individual customer classes. Once the Wyoming portion has been determined, the last step is to incorporate further adjustments that the OCA believes is required to get to assets to the point of being reflective of the rate effective period or, at least, the beginning of the time period that the rates are first

expected to be used for determining the amount paid for service by Wyoming customers.

Q. IS OCA SCHEDULE DKP-3, THE INCOME STATEMENT, LAID OUT IN A SIMILAR MANNER?

A. Yes. It too begins with the unadjusted, total company data that is turned into data reflective of the Wyoming only operations. Together, OCA Schedules DKP-1 and DKP-2 show that once the new plant (particularly Wygen III) is added to rate base, existing authorized rates will only permit Black Hills to earn approximately a one percent rate of return on its Wyoming allocated investment and even less on the equity portion of its capital structure.

Q. DO THE NEXT FEW SCHEDULES DETAIL THE ADJUSTMENTS THAT OCA RECOMMENDS BE MADE TO THE RATE BASE TO MAKE IT MORE REFLECTIVE OF THE UPCOMING RATE EFFECTIVE TIME PERIOD?

A. Yes. These rate base adjustments are detailed on OCA Schedules DKP-4 through DKP-13. OCA Schedule DKP-4 begins with an update to the capital costs associated with the construction of Wygen III. Since an estimate of the Wygen III costs has already been included in the figures provided with the Application, the purpose of my adjustment is to update those estimates using more recent data, including actuals through March 2010. Once the more recent plant cost estimates have been provided, the Wyoming portion of that overall cost is computed. This smaller number of only \$89,618 is added to the estimate already in rate base to reflect the latest estimate of the Black Hills share of the plant used to serve Wyoming customers. The detail shows that there have been few, if any, major changes to the earlier capital cost estimates for Wygen III. This is so since, as described by Mr. Ohlmacher, the cost of many of the materials and supplies were purchased on a fixed price basis early in the planning and/or construction process.

OCA Schedule DKP-5 is also just an update of an earlier computation – this time related to what has been termed *Bonus Depreciation*. This is tied to provisions of the national economic stimulus plan passed by Congress in response to the economic crisis. The bonus depreciation provisions permit a company who invested in certain assets in 2009 to write up to one-half of those assets off as an expense for purposes of computing net taxable income when computing federal income tax liabilities. This benefits customers because the difference between that treatment for federal tax purposes and the normalized depreciation for book (and regulatory) purposes is placed into accumulated deferred income taxes and is then deducted from rate base. This all goes to reduce the asset base upon which a return is to be paid – ultimately allowing a lower rate to be billed to customers than would have occurred without the bonus depreciation. The adjustment on OCA Schedule DKP-5 merely updates the plant balance numbers that were provided in the Application.

A third Wygen III item is found on OCA Schedule DKP-6 and this time the topic is Accumulated Depreciation. In its revenue requirement calculation, the Company made the deliberate decision not to reflect any updates or adjustments to Accumulated Depreciation relative to the newly constructed Wygen III generating station. Black Hills Power did reflect in its calculation depreciation *expense* for the new power plant, but did not make the related adjustment to *accumulated depreciation*. The data on OCA Schedule DKP-6 reflects one-half of the annualized depreciation expense – based on the latest plant cost estimate – in accumulated depreciation with the effect of reducing rate base. It is common practice to make this adjustment in order to best reflect what the Company's net asset balances will look like in the early portion of the rate effective period. In fact, reflecting only one-half of the first year's depreciation expense for the new plant-in-service – rather than reflecting a full year's depreciation – makes the adjustment conservative. Without this adjustment, the full, undepreciated cost of the plant would be placed in rates and would earn a return until the next rate case.

At least the OCA adjustment recognizes the declining nature of this balance and reflects it in the rate base computation.

Consistent with our expectation that this rate case and requested revenue increase is primarily caused by the completion of the Wygen III construction project, the next adjustment (shown on OCA Schedule DKP-7) is also related to Wygen III. However, this is more than just a numeric update – it represents a difference as to what is considered *fair* and *reasonable* between the OCA and Black Hills. Schedule F-4 of Black Hills’ application contains a list of materials and supplies related to Wygen III that the Company seeks to include in rate base. However, this is the only Wygen III rate base item of which I am aware that is not shared among the joint owners. In this case, Black Hills seeks to include 100% of the supplies that will be needed to maintain a plant for which it only is claiming 52% ownership in this proceeding. To allow this full addition to the rate base for Black Hills’ customers would be unfair and would result in Black Hills’ customers paying a cost for which it only receives part of the benefit. In other words, the customers of Black Hills would be subsidizing the customers of the other owners. The OCA adjustment corrects this blatant unfairness.

Q. PLEASE DESCRIBE THE ADJUSTMENT TO ACCUMULATED DEPRECIATION SHOWN ON OCA SCHEDULE DKP-8.

A. This is an adjustment that was provided to me by Black Hills shortly before I was to file my testimony in this case. Essentially, the plant balance for the Kirk generating station has been fully depreciated yet there remains on the Company’s books and records a small amount of accumulated depreciation related to the Kirk plant. This remaining balance should be written off and eliminated from the books. While there was a suggestion that some of the other state regulators may be amortizing the remaining balance over more than one year, I saw no reason to do so. It is a small balance and removing it in one swoop in this case will have no material impact on rates.

Q. PLEASE DESCRIBE THE UNCOMPLETED CONSTRUCTION BALANCES THAT YOU SEEK TO REMOVE FROM RATE BASE WITH YOUR NEXT ADJUSTMENT.

A. As part of its inquiry into this matter, the Commission's Advisory Staff sought information from Black Hills as to the construction items that are reflected in rate base but are not likely to be completed until more than twelve months beyond the end of the test year. The response included each of the items on OCA Schedule DKP-9. While it has been the Wyoming Commission's practice to include in rate base plant that is still under construction at the end of the test period, its practice has been to do so only when the items are likely to be in-service (that is, used and useful) at the time rates become effective. While a slightly different practice has recently developed for utilities' whose test year is based on a forecast, that is not the situation here and thus, it need not be discussed here. I am recommending removal from rate base of the Wyoming portion of these projects not expected to be operational until after the rates resulting from this case become effective.

Q. IF IT HAS BEEN A COMMON PRACTICE TO USE YEAR-END RATE BASE BALANCES, WHY ARE YOU RECOMMENDING THE USE OF 12 MONTH AVERAGES FOR CERTAIN ITEMS, AS SHOWN ON OCA SCHEDULE DKP-10?

A. It is true that the majority of rate base items are based on actual incurred costs rather than averages. However, the items shown on this schedule have balances that are quite volatile month-to-month and may vary greatly depending on the last month of the test year. This can be seen by just looking at the fact that the fuel stock account varies from a total company high of more than \$7 million to a low of less than \$5 million. It is, therefore, not unusual to use an average balance for these particular items with volatile balances.

Q. PLEASE DESCRIBE THE OCA PROPOSED ADJUSTMENT ON OCA SCHEDULE DKP-11.

A. This adjustment is an alternative means of treating customer deposits within the revenue requirement calculation. Black Hills chose to use the alternative method of not reflecting either customer deposits or the associated interest expense that it must pay on those deposits anywhere in the case. The theory of the Black Hills alternative is that the utility has the use of the customers' funds during the time that the security deposit is held and can earn on those funds through some investment option. The earnings that it makes from whatever investment option it chooses should be enough to at least pay the interest cost that is due to customers at the end of the security deposit period.

I, however, believe that the utility's alternative actually disadvantages customers in that it allows the utility to earn on these customer provided funds without flowing any of those earnings back to ratepayers. The theory is this: customer deposits can be invested in new plant that is placed into rate base and earns a return as high as 8 or even 9%. Yet, the utility only has to pay, pursuant to Commission order, the customer interest at the rate of 3-6% per annum. This allows the utility to arbitrage the customer funds. Thus, I am offering an accepted alternative practice of reducing rate base by the balance of the customer deposits (essentially treating it as zero cost capital) with the understanding that the interest the utility is obligated to pay is included as net operating income. This keeps all parties whole without any side being disadvantaged.

While my shown adjustment has been commonly used, I must confess to not having all of the data that I ideally would have liked for this adjustment. Since, the balances for customer deposits can also vary month-to-month, similar to the items on the previous schedule, it would have been ideal to have the monthly balances to apply in this calculation. However, as I did not have them at the time I was making this calculation, I used the balance that I identified for Wyoming from the Black Hills' balance sheet as found on the response to Commission Staff data request 3-38.1.

Either way that this adjustment is computed, it is relatively small in the overall scheme of things in this case and will not have a material impact in the overall result.

Q. WHAT IS THE NATURE OF THE OCA ADJUSTMENT FOUND ON OCA SCHEDULE DKP-12?

A. This adjustment updates the Company's cash working capital lead-lag calculation to incorporate the OCA's adjustments to operating expenses. In other words, the lead lag study used to compute cash working capital has as inputs the Company's operating expenses. When those expenses are adjusted, it may impact the overall result of the study. OCA Schedule DKP-12 utilizes the same formula used by Black Hills but incorporates the adjustments that the OCA recommends be made to operating expenses (matters to be discussed below).

I should note that for each of the adjustments I have described, once the adjustment is made on a total company basis, I apply the relevant allocation factor to bring all the numbers down to the Wyoming jurisdictional level.

Q. PLEASE DESCRIBE THE WYODAK ACQUISITION ADJUSTMENT SHOWN ON OCA SCHEDULE DKP-13.

A. In approximately 1990, Black Hills Power filed a joint application with PacifiCorp (in Docket No. 20002-ER-90-11) requesting authority to include in rate base their respective purchase costs, including transaction costs and any acquisition adjustments, associated with their purchase of the Wyodak generating plant. The joint applicants alternatively asked for an order approving the proposed accounting treatment for the purchase. In its *Order Granting Accounting Treatment*, dated December 5, 1990, the Commission granted authority for the two utilities to record and account for their respective costs of purchasing ownership certificates of the Wyodak generating plant. While the Commission did not make a finding on the ratemaking treatment to be provided the acquisition adjustment that resulted from the purchase, it did indicate that the acquisition

adjustment was to be recorded and directed that it be amortized over the remaining life of the Wyodak plant.

This OCA adjustment does not challenge Black Hills' inclusion of the remaining unamortized portion of the acquisition adjustment in rate base – although it is clear that one would be free to make such a challenge if one were so inclined. Instead, I am concerned that the amortization rate does not appear to match the rate necessary to make sure that the acquisition adjustment is fully amortized at the time of Wyodak's expected retirement date. The amortization rate currently being used is 3.11%. At this level, it would take more than 30 years to amortize the remaining balance. This appears to be inconsistent with the fact that Mr. Loos indicates that Wyodak's expected retirement date is 2030 – or 20 years from now. The adjustment increases the amortization expense and also reflects a portion of that greater expense as an adjustment to the remaining balance in rate base.

It is also an adjustment that is relatively small as a standalone matter. But, this series of smaller adjustments add up to reflect the OCA's smaller recommended increase than that requested by the Applicant.

Q. PLEASE DESCRIBE THE TWO REVENUE ADJUSTMENTS FOUND ON OCA SCHEDULES DKP-14 AND DKP-15.

A. The first is again an adjustment provided to me by Black Hills shortly before the filing of my testimony. This adjustment corrects a mis-categorization of certain transmission revenues. These revenues were reflected in the Application as Other Revenue, when they should be recorded as transmission revenues. The overall impact of this adjustment is to reduce the Operating Revenues reflected in the Wyoming jurisdiction. While it might seem that taking from one accounting and placing into another would have a neutral impact, it does not due to the fact that the two accounts have different allocators. This is shown on the OCA's schedule. The adjusted Other Revenues are allocated to the various jurisdictions and enter into the calculation of how large the revenue increase should be. This is different

than the Transmission Revenues that are directly allocated to the FERC jurisdiction so they are not reflected in the calculation of the retail rates.

The second revenue adjustment, reflected on OCA Schedule DKP-15, begins to flow back to customers the benefits of the sales of some SO₂ allowances. The net revenues from these sales is simply sitting on Black Hills books and providing no benefit to customers. Consistent with the current treatment of this revenue in the PacifiCorp rate cases, I propose that the net revenue be treated as a revenue credit, thus reducing the required revenue increase in this case.

Once the decision is made to flow these credits back, the question is how to do so. There is a movement afoot to begin to utilize various fuel and purchased power mechanisms to flow back these types of items (including renewable energy credit sales revenues). I choose not to do that but am not philosophically opposed to such, especially since there is generally a tie between the receipt of the SO₂ allowances and the cost of generation.

Once I decided to flow back the revenue through base rates, then the question became over what period should they be amortized? Based on judgment and precedent, I chose seven years but there is no hard science behind this number. It is the amortization period that has developed in the PacifiCorp rate cases after a number of proceedings. It is also the amortization period over which I have chosen to amortize rate case expenses in this case, based on my professional opinion that Black Hills will not likely be able to continue to go fifteen years between rate cases. In making this adjustment over seven years, it provides some benefit to customers through the ratemaking process without the type of rate swings and variability that might occur were this same amount to be amortized over a twelve month period through an Energy Cost Adjustment mechanism.

The adjustment is, as with all the others described herein, adjusted to reflect only the portion appropriate to address within the Wyoming jurisdiction.

Q. PLEASE DESCRIBE THE WYGEN III RELATED DEPRECIATION ADJUSTMENT FOUND ON OCA SCHEDULE DKP-16.

A. Black Hills Power has filed its application with the assumption that Wygen III will have a depreciable life of 45 years. This is an assumption with which I disagree and am proposing a depreciable life of 50 years. Based on the life extensions that are appearing throughout the industry to make less expensive existing plants last longer to help avoid the construction of new plants, I believe Wygen III will provide service to customers for at least 50 years. However, in an abundance of caution, given the lack of current action on a climate and/or energy policy bill, I am advocating a life of 50 years. The adjustment on OCA Schedule DKP-16 is the calculation to reflect this slightly longer life in the rate calculation in this proceeding.

Q. YET ANOTHER ADJUSTMENT RELATED TO WYGEN III APPEARS ON OCA SCHEDULE DKP-17. PLEASE EXPLAIN.

A. In its Application, Black Hills Power estimated the price of coal that it thought would be in place for the 2010 operating year for Wygen III. The actual price is now available. The originally filed price, shown on Black Hills Power's Schedule H-7 was \$12.09 per ton. The updated price is \$11.60 per ton. This new price is reflected in the OCA adjustment.

The second correction to the coal price estimate relates to the number tons that will be needed. The original information contained in the Application (again, found on BHP's Schedule H-7) anticipated that total production would be 100,000 kWh per hour. However, upon reflection, this was an error. The 100,000 kWh output was net output rather than gross output (considering losses and company owned use) and thus the new figure should be 110,000 kWh per hour. This corrected number (which, by the way, is the same number used in the pending Montana Dakota Utilities rate case) is reflected in the OCA's calculation and increases the overall cost of coal because there will be more coal used.

Q. IS THE COAL ADJUSTMENT FOR GENERATING UNITS OTHER THAN WYGEN III THAT IS SHOWN ON OCA SCHEDULE DKP-18 RELATED TO THE UPDATED COST OF COAL PER TON YOU JUST DISCUSSED?

A. Yes. This is coal that is purchased from Black Hills Power's affiliate and is based on the Statement R pricing that is discussed throughout Black Hills testimony. The updated price when applied to the expected generation at the other plants reduces the overall coal costs in this case.

Q. PLEASE DESCRIBE YOUR ADJUSTMENT TO UPDATE THE ADJUSTMENT FOR NEW EMPLOYEES.

A. In his testimony, Mr. Loomis discusses the need for and expectations of hiring new employees. In response to this testimony, Black Hills proposed an adjustment to operating expense to reflect the associated costs of these potential employees. The adjustment on OCA Schedule DKP-19 updates these costs to reflect the current situation. One of the slotted positions has been removed from the adjustment based on updated circumstances, one of the slotted positions hiring date has been pushed back, and for the remaining positions the estimated costs have been updated to actual. Since a portion of wages is capitalized, and a number of these recently filled positions are field positions, I have used the average capitalization percentage in calculating this adjustment.

Q. DOES THE NEXT ADJUSTMENT YOU ARE PROPOSING ALSO ADDRESS WAGES?

A. Yes. In its application, Black Hills Power proposed an adjustment to reflect anticipated wage increases for the 2010 timeframe which is the rate effective period. In its adjustment, Black Hills assumed an average wage increase of about 3.5%. As time has passed, more current information on those wages increases is available. It is my understanding that effective April 1, 2010 non-union

employees began receiving an increase of approximately 2.58%. Thus, I recalculated the originally proposed wage adjustment using the updated increase.

Q. PLEASE EXPLAIN YOUR ADJUSTMENT TO INCLUDE AN AVERAGE LEVEL OF INJURIES AND DAMAGES EXPENSE RATHER THAN AN ACTUAL TEST YEAR AMOUNT.

A. As is shown on OCA Schedule DKP-21, the annual amount of injuries and damage expense has varied widely on an annual basis over the past few years, ranging from a total company low of around \$1 million in 2007 to a high in the test year of nearly \$3 million. This lack of a pattern and extreme volatility makes it difficult to know the level of expense that should be included in the rate setting process. So, while it is not my intention to average all costs in all instances, there are times when it is obvious that some averaging is the correct method to use, and such is the case with these accounts. In many ways, it is similar to the proposed averaging done by Black Hills in its application for generating plant maintenance. With different plants down in different years, but all plants down at some point in the cycle, averaging makes sense. As long as there is a generally consistent use of averaging for specific categories of costs from case-to-case, neither the ratepayer nor the utility should be harmed by its use.

Q. IS THE ADJUSTMENT TO ADVERTISING COSTS ONE THAT WAS ALSO PROVIDED TO YOU BY COMPANY REPRESENTATIVES?

A. Yes. This adjustment was provided to me when it was discovered that some advertising costs were inappropriately left in the case. This simply removes these costs under the theory that ratepayers should not pay for corporate or image advertising.

Q. PLEASE EXPLAIN HOW YOU ARRIVED AT THE NUMBER CONTAINED IN YOUR ADJUSTMENT TO UPDATE THE ESTIMATED RATE CASE EXPENSE FOR THIS CASE, AS SHOWN ON OCA SCHEDULE DKP-23.

- A. The updated numbers shown on the schedule have two distinct parts. First, I was provided an update of the costs that have been spent to date. Many of these costs were incurred in the preparation of the filing and the studies that are associated with it, such as the depreciation expense. Thus, I have accepted the actual without taking the time or opportunity to explore them in any sort of depth.

The second part of the estimate is based on my judgment and experience on how the case is likely to proceed from here. Black Hills Power is a company that likes to settle issues if at all possible and settlement is within reason. But, more importantly, the case has proceeded quite informally with little contention – so far – and without the need for a lot of hearings, motions, objections and expensive processes. It has also proceeded, to-date, without the need for a lot of additional interaction from the outside consultants. All of this appears to be a cost savings from the original estimate.

Another issue to be addressed is the matter of the amortization period. Black Hills indicated in its testimony that three years is a common number for amortizing these types of matters. But, that should not carry as much weight for a company that has a very sporadic history of rate cases. There was lots of rate activity in the 1970s and 1980s but very little in the 1990s and 2000s. So, seven years seemed like a middle ground number, particularly given that Black Hills is looking at the possibility of new meters from the stimulus funds, Congress is looking at energy and climate matters and there is an air of regulatory uncertainty.

The final issue has to do with whether or not the unamortized portion of the rate case expense should be permitted to earn a return. The OCA has often taken the position that rate cases can benefit both customers (e.g, reliability of service, innovative rate designs) and shareholders (e.g., more current cost recovery and additional revenues), then both share in the costs. That is the position I take in this case. The Company should be permitted to recover all of the costs that the

Commission finds reasonable relative to the rate case but shareholders should pick up the carrying charge.

Q. DOES OCA SCHEDULE DKP-24 SHOW THE TRADITIONAL INTEREST SYNCHRONIZATION?

A. Yes. It has become usual to base the interest expense used for computing taxable income on the weighted average cost of debt times the rate base. This adjustment simply recognizes that the OCA's rate base and cost of debt are different from those contained within the Company's filing.

Q. IS YOUR FINAL REVENUE REQUIREMENT ADJUSTMENT A CALCULATION THAT SIMPLY RECOGNIZES THAT AS EXPENSES AND REVENUES ARE ADJUSTED, THE AMOUNT OF INCOME TAX REQUIRED WILL ALSO NEED TO CHANGE?

A. Yes. The adjustment found on OCA Schedule DKP-25 is intended to conform the income taxes to the rest of the OCA's recommendation.

Q. DOES THE OCA WISH TO OFFER ANY COMMENT ON THE DEPRECIATION STUDY THAT HAS BEEN PROVIDED AND INCORPATED INTO THIS PROCEEDING?

A. I will offer a few remarks but not take issue with the study. Based on my review of it, I found it to be comprehensive, thorough and professionally done. But, there is one thing that the Commission may wish to note as it reviews the matter. The study incorporates interim additions in it and does so to an extent not seen in many of the other studies that have been adopted by the Commission – and I am specifically thinking of PacifiCorp's depreciation. If I am reading the Black Hills study correctly, interim additions have been incorporated for the remaining life of the plant in the analyses of each generating unit. (The exception may be for Wygen III but its rates are based on the analyses of Wygen II for which interim additions have been included.) This is different than what was seen in the last

PacifiCorp depreciation case (Docket No. 20000-257-EA-06) where I described in my testimony:

As further discussed by the Rocky Mountain Power witnesses, interim additions and retirements and their appropriate treatment were widely debated. Several parties were concerned that the cost of expected plant additions should not be incorporated into the calculation as it would be a major change in policy from the past, and would break with the *known and measurable* rule-of-thumb of ratemaking. The matter was resolved by allowing interim additions for only 2007 rather than for the upcoming 5 year period for replacement of estimated retirements originally proposed in the application.

While the OCA is not taking issue with this matter, it is clearly a change that has not heretofore been embraced by many of the parties in cases appearing before the commission. It is also a change that has a current depreciation cost associated with it.

Q. MS. PARRISH, BEFORE MOVING ON TO DISCUSS OTHER ASPECTS OF YOUR CASE, DO YOU THINK THAT THE REVENUE REQUIREMENT YOU ARE PRESENTING IS FAIR, REASONABLE, AND IN THE PUBLIC INTEREST?

A. Yes, I do. While it is a larger increase than any of us would like to see at one time, it is driven by the rate recovery of Wygen III. This plant was issued a certificate of public convenience and necessity by the Wyoming Public Service Commission and found in the Commission's Order in Docket No. 20002-69-EA-07 to be "a well conceived project capable of being successfully constructed and placed into service for the benefit of the customers of Black Hills."

Q. MOVING ON TO THE DEVELOPMENT OF YOUR CLASS COST OF SERVICE STUDY, PLEASE EXPLAIN THE STEPS YOU TOOK TO ARRIVE AT THE A SET OF COSTS FOR EACH CLASS.

A. Obviously, I first arrived at the total Wyoming jurisdictional revenue requirements as a starting point. I then reviewed the allocation factors that Black

Hills had used in the development of its class cost of service study. I charted these on OCA Schedule DKP-26 to determine whether I saw any gross inconsistencies between the allocation factors used for interjurisdictional allocations and the class allocations. Nothing jumped out at me that would make me want to change the allocators, although the entirety of the discussion earlier in my testimony about reasonable people being able to disagree also applies here when discussing the class allocators.

Since I did not intend to change any of the allocation factors, my starting point was the class allocation study found in the Application. I began with the Company's revenue requirement and made the OCA's adjustments, spread those adjustments to each class and ended up with a study that looked much like the company's but based on the OCA figures. This study is found on the first five pages of OCA Schedule DKP-27. I should also note at this point that I used the broad categories as found in the Application: Residential, Small General Service, Large General Service and Industrial, and Lighting. In the tariffs and the rate design, each of the classes is further subdivided; however, I did not have the information to provide an any more detailed type of study than that offered by the Company.

Q. WHAT WAS THE CONCLUSION OF YOUR STUDY?

A. The results of the class cost of service study are summarized on page 6 of OCA Schedule DKP-27. On this page, I have computed the revenues that must be collected from each of the broad classes in order to avoid interclass subsidies, based on the results of the study. It shows that the following increases are required, based strictly on a cost basis from the study that was done:

	Residential	Small General Service	Large General Service and Industrial	Lighting
Required Increase in Revenues	\$399,347	\$519,650	\$2,174,686	\$28,357
Required Total Sales Revenues	\$2,076,845	\$2,172,845	\$8,557,843	\$118,713
Percentage Increase	23.81%	31.43%	34.07%	31.38%

In its analysis, the Company did not appear to further utilize the results of the cost of service study. Instead, it concluded that the results showed that the current earnings of each of the classes was relatively close, and it then supported the use of an across the board increase to each of the current rates within the tariff. There was no change in the structure or design of the rates.

Q. BEFORE MOVING TO RATE DESIGN, WOULD YOU PLEASE DISCUSS YOUR ADOPTION OR USE OF THE COMPANY’S STUDY BASED THE AVERAGE AND EXCESS COST ALLOCATION METHOD?

A. Certainly. Black Hills has consistently used the *average and excess* method over the years in each of the rate cases for which I reviewed the order. Mr. White, in his testimony from Docket No. 2002-ER-95-48 explains the method this way:

First, each customer class is allocated its average kW demand during the test year. Average kW demand is determined by taking the total kilowatt hour sales for the class, plus associated energy losses, divided by the number of hours within the test period...The second component of the average and excess capacity allocation, allocate the remaining system peak demand (excess demand) not allocated by the sum of the individual class average demands. The excess demand is allocated based upon the relationship of individual class non-coincident peak demands determined for the test period. The result of this approach is that customer classes with lower load factors are responsible for a greater percentage of the excess demand, whereas the customers with the higher load factors are responsible for a greater percentage of the average demand. The approach has the tendency to recognize that systems are made up of both base load resources and peaking resources,

and that the load factors associated with each class of customer inspires system planners to acquire different mixes of resources.

Black Hills does not have the data that is needed to make all the computations required by this method, so instead, has borrowed some data from another utility. I was informed that it was the same data used in the last rate case, but was tweaked to better fit today. But, much of that process is unexplained in the testimony. Also unexplained is whether the older borrowed data still makes sense in light of the changes that have occurred in on Wyoming's system, There has been tremendous growth in energy use, far less growth in capacity, and yet even less growth in the number of customers. Some of that growth in megawatt hours is noted in the table below:

	Residential	Small General Service	Large General Service and Industrial	Lighting
Prior Rate Case	16,533	12,620	96,800	790
Current Rate Case	22,184	19,733	121,344	669
Percentage Increase	34%	56%	25%	-15%

So, I am concerned about how valid the results of the class cost of service study are. But, it is what I had, and I figured it was better than nothing. So, I took the next step of trying to set rates that had each class recover its overall costs.

Q. WHAT WAS THE NEXT STEP YOU TOOK IN FORMULATING YOUR RATE DESIGN RECOMMENDATIONS?

A. The next step I took was to try to establish an appropriate customer service charge. The current rate of \$8 for most residential customers is extremely low compared to the rate put in place by other Wyoming utilities, and I note that the Large General Service class does not even include a customer charge. So, I developed some quick analysis, found on OCA Schedule DKP-28, to try to get a

ballpark idea of the costs often used to establish customer charges. For this analysis, I looked at the recovery of the return and depreciation on distribution assets, the recovery of distribution operations and maintenance costs and the recovery of customer accounting and information costs. The analysis shows that the per bill average of these costs is about \$18.65 for residential, \$68.30 for small general service, and more than \$7,000 for large general service and industrial. Because of some lingering discomfort with the accuracy of the class cost of service, I decided to recommend moving the residential customer charge to \$15 from its current level of \$8. I am also recommending an increase in the charge for small general service (to \$46.50 for most customers) and to recommend imposing a customer charge for the larger commercial/industrial customers.

Before explaining the remainder of my recommended rates, let me just say that the OCA is not wedded to these exact number for each category in each class. Of course the whole area of price setting is art and not formulaic. Transitions must be taken into account – particularly for a company who has had its current rate design for so many years and is still uses declining block rates! But, there are some principles that I tried to incorporate in my recommendations to you. I wanted a flat, common per kWh energy rate for residential and small general service customers. The declining block rates should not continue at this time. I tried to recognize that there are some cost differences between the load factors of small and large customers and between distribution and transmission customers. But, Black Hills still has to purchase some power, and it is not long all the time every day. So, there is a cost associated with imposing demand on the system. It is important to recognize that new generating resources cost more than embedded generating resources, and thus, having every class pay a little more per unit for energy than is currently being paid makes sense with a new power plant driving the majority of the cost increases in this case. With these principles in mind, and with a class cost of service in hand, I developed a rate design to recommend to you.

As to lighting, I must admit that I am simply recommending that the rates be targeted to meet the costs for the class from the OCA's overall class cost study. My recommendation is basically one where I am fine with the proposed rate design – simply scale it down to recognize the OCA's reduced revenue increase recommendation.

All of this is summarized, as are the proposed rates for the major classes, on OCA Schedule DKP-29.

Before concluding, I should comment on the contract industrial customers and how they are incorporated into my rate recommendation. I have adopted the rates that they recently negotiated into my recommendation. OCA Schedule DKP-30 shows the prior and the current negotiated rates but is deemed by Black Hills Power to be confidential and has been submitted that way. Furthermore, even the summary number of the contract revenue has been deemed to be confidential so when that number is brought over onto OCA Schedule DKP-29, page 6 of 7, it creates a confidential situation for that page as well.

Q. MS PARRISH, ARE YOU PROVIDING SOME ADDITIONAL INFORMATION THAT MAY FURTHER HELP THE COMMISSION WITH SOME OF THE RATE DESIGN ISSUES THAT ARE ARISING IN THIS CASE?

A. Yes. The six pages of OCA Schedule DKP-31 show some of the bill distribution data that I have received in both tabular form and as a graph. This information was interesting to me and especially helped me when deciding some what-if scenarios to incorporate in my sampling of bill impacts found on OCA Schedule DKP-32. As would be expected, no matter what rate design the Commission chooses, there will be winners and losers – that is, some customers will pay more than the system average increase and some will pay less. However, the bill impact sampling may assist the Commission in determining how far and how fast it wishes to transition the rates away from their current design – if it wishes to

make such a change at all. Finally, I found the skewing and the tails on some of the bill distribution graphs to be both fascinating and distressing at the same time, as I was not sure how to incorporate them into the rate design changes that I believe should be begun in this case.

Q. DO YOU WISH TO COMMENT ON THE DEMAND SIDE MANAGEMENT STUDY THAT THE COMPANY HAS INDICATED THAT IT IS IN THE PROCESS OF CONDUCTING?

A. Not at this time, other than to say that it seems incongruous of the Company to be advocating demand side management and the continuation of declining block rates at the same time.

Q. WHAT IS THE LAST SIGNIFICANT TOPIC UPON WHICH YOU WISH TO COMMENT IN THIS MATTER?

A. The last major topic I wish to comment on is the proposed Energy Cost Adjustment. I have a number of thoughts and recommendations on Black Hills proposed mechanism; however, none of my recommendations incorporate the idea of not adopting some sort of fuel, purchased power, and/or energy cost mechanism. Other utilities that provide service in Wyoming are all permitted some sort of pass through mechanism whether they are strict purchasers of power or self generators. Not to allow Black Hills the same opportunity would seem unreasonable and perhaps anti-competitive.

So, in spite of the fact that Black Hills survived for many years without a power cost mechanism in Wyoming, and in spite of the fact that self generation was supposed to further stabilize costs, my comments are not aimed at the question of if such a tariff should be approved. Instead, I am focused on what should the mechanism look like and what safeguards could and should be incorporated to protect both shareholders and customers. Much time was spent trying to make sure that all of the pass-throughs in the state (whether it be Rocky Mountain Power's or those subject to Commission rules 249 and 250) were developed in a

way that was carefully thought out. Protections were provided that I do not see in Black Hills proposal. They need to be added.

Q. WHAT IS THE FIRST AREA YOU WISH TO ADDRESS RELATIVE TO THE ENERGY COST ADJUSTMENT?

A. The first issue that should be discussed is whether it is better to have a mechanism with a deadband, or sharing, or some of each. Black Hills' proposal includes a \$2 million total company deadband and includes some very complicated sharing relative to the revenue from power marketing sales. While there are existing models in Wyoming for this type of mechanism, it is not clear to me that they are really accomplishing all of the goals that should accompany the deadband. For instance, if the purpose of the deadband is simply to assure that the utility has a stake in the game, then this is accomplished. If the purpose is to make sure that the utility does not receive 100% of its cost changes that is also accomplished. But, does it appropriately provide incentives for to Black Hills to make sure all of its costs are as stable and operations as efficient as possible? Probably not and I will try to explain with an analogy.

Take the dreaded issue of healthcare. If I have an annual deductible, I may try to avoid any medical matters to make sure that I do not have to pay my deductible. And, I may do that even if I am sick and need medical care. A similar situation may occur with Black Hills. It may be better off shutting down a power plant and going to the market for power, but if it can limp by with an inefficient power supply rather than having to leave money on the table that it will not recover due to the deadband, it might be incented to do so. Let's continue. So, I avoid the doctor until I am hit by a bus and need surgery. At that point, I have met my deductible and what do I care about how often I go to the doctor as it is mostly paid for by the insurance company. Back to Black Hills. It is hit by a bus when the Western U.S. energy market crashes and purchased power is \$100/ MW. Now, what does it care about cutting corners or squeezing out efficiency. It can

buy \$100 / MW power and it is paid for – by customers. It no longer has a stake in the game. Where is its incentive?

I would prefer to see some variation on a straight sharing mechanism that continues no matter the size of the dollar change to make sure that there is always some incentive for the utility to take all prudent actions that are reasonable. Perhaps it is reasonable to have a small deadband, as with some of the pass-ons, to avoid the need for regulatory filings when the change is too small to warrant the regulatory and customer hassle (for example, if a change is less than x dollar amount or x percent).

Q. ARE YOU LOOKING TO INCORPORATE A STICK INTO THE MECHANISM, AND NOT ONLY A CARROT?

A. Yes. I think that many of the safeguards that are present in the Commission's rules 249 and 250 are not present with the proposed mechanism. For instance, I read the Company's proposal such that it could file an application, consistent with its tariff, to pass on a very large power cost increase to its customers regardless of the status of the rest of its operations and earnings. There is no language, such as the Commission's rule contains, that would even require a financial showing with the annual application. And, even if there were, there is nothing that would stop the burden from being shifted to an intervener or party to show that it would be completely inappropriate to pass on increasing power costs at the same time that other operating utility earnings are excessively healthy.

Similarly, there are no performance standards, operating standards or other safeguards to customers that would provide offsetting benefits for this expedited cost recovery mechanism.

Q. IS THE PROPOSED ENERGY COST ADJUSTMENT ALSO VERY COMPLICATED AND SUBJECT TO POTENTIAL INTERPRETATION AND REPORTING PROBLEMS?

- A. Yes, particularly the section of the mechanism that describes the sharing of the Power Marketing Net Income. The proposal looks to share the income from Power Marketing, even though much of the power that is being marketed is coming from Black Hills Power's arrangement to purchase excess power from the Wygen II facilities owned by Cheyenne Light with all of that facilities costs recovered from Cheyenne Light's ratepayers and from excess power at Black Hills' coal generation facilities. There is a fundamental fairness question that I have about whether the risks and rewards are being symmetrically shared between customers and shareholders.

But, setting that aside, the proposed calculation itself for determining what is a profit is complicated. The tariff discusses how the profit will be determined and includes marketers bonuses for certain aspects of the calculation and not in other places. The calculation has *nightmare* written all over it. In these types of situations simplicity should be the goal. Will the Commission and its staff and other interested parties begin having debates about what is a wage versus a bonus for the marketers. Will bad debt policies be impacted by the fact that bad debt is included in certain aspects of the revenue sharing calculation?

Q. IS THERE ONE ADDITIONAL EXAMPLE OF A PROBLEM THAT YOU WISH TO RAISE ABOUT THE LANGUAGE AS IT IS WRITTEN?

- A. Yes. In discussion with Black Hills, it believes that this mechanism would allow it to pass through carbon or environmental mitigation costs as part of the costs that are covered by this proposed Energy Cost Adjustment. I am not necessarily opposed to passing some of these costs through, once we know how much they are and what they might be mitigating. However, if this mechanism stays as it is, shareholders could be incented – particularly once the deadband is passed – to take mitigation measures that are not necessarily the most cost effective or efficient because of pass through incentives. I think that there should be some safety net for customers built into this process before we all assume that environmental mitigation costs can be passed through such a mechanism without

further discussion and appropriate showings by the utility. It would be particularly troubling to me if, for example, the cost of environmental mitigation were passed through on a 100% basis but shareholders were permitted to keep most or all of the revenue associated with selling allowances to pollute .

More thought and discussion is needed on the specifics of this mechanism.

Q. BEFORE YOU CONCLUDE YOUR WRITTEN, PREFILED DIRECT TESTIMONY, ARE THERE ANY OTHER THOUGHTS THAT YOU WISH TO SHARE?

A. Yes. I wish to publically thank the Black Hills personnel, and particularly Mr. Chris Kilpatrick, for his cooperation and positive attitude during the Office of Consumer Advocate's investigation of this proceeding. He and his staff were of tremendous assistance in responding to questions quickly and made himself available throughout the process for follow-up on a wide variety issues. With that, I conclude my prefiled, direct testimony but look forward to further discussions of this matter at the scheduled hearing.

