INDEX

REBUTTAL TESTIMONY OF

LOU ANN WESTERFIELD

Witness for the Idaho Public Utilities Commission

SUBJECT: DEEMER BALANCES AND LOOKBACK ANALYSIS

REBUTTAL TESTIMONY OF

LOU ANN WESTERFIELD

Witness for the Idaho Public Utilities Commission

SUBJECT: DEEMER BALANCES AND LOOKBACK ANALYSIS

Section 1: Introduction and Purpose of Testimony

Q. Please state your name and qualifications?

A. My name is Lou Ann Westerfield and my qualifications are described in WP-07-Q-ID-1.

Q. What is the purpose of your testimony?

A. I rebut certain direct testimony of

1. The Western Public Agencies Group ("WPAG") (WP-07-E-WA-5);
2. The Cowlitz County PUD and Clark Public Utilities (collectively, the "JP 17 Parties") (WP-07-E-JP17-1); and
3. The Association of Public Agency Customers ("APAC") (WP-07-E-AP-1).

My testimony addresses the deemer balances and the Lookback analysis offered by the parties.

Section 2: The Deemer Balances

Q. Please summarize the assertions that APAC, WPAG, and JP 17 (Cowlitz and Clark) make in their testimony about the deemer balances?

A. Without elaboration, the three parties support BPA's proposal that deemer balances should be "cleared" before the affected investor-owned utilities (IOUs) are eligible to

receive future REP payments. For example, WPAG insists "that each IOU's outstanding deemer account would have to be paid in full with interest prior to receiving their hypothetical REP payments during FY 2002-2008 period . . . make[s] some sense." WP-07-E-WA-05 at p. 47, ll.9-11, p. 48, l.14. The JP 17 Parties state: "BPA should calculate and determine deemer balances during the Lookback period just as it did under the 1984 ASCM prior to the REP settlement." WP-07-E-JP17-1 at p. 39, ll.13-16. APAC states: "I will not address the issue of deemer balances except to say that those balances should be cleared before any payments are made to utilities that have them." WP-07-E-AP-1 at p. 79, ll.17-20.

Q. Did these three parties offer any reasons why the deemer balances should be paid in full before becoming eligible to receive REP payments?

A. Not in testimony. However, WPAG offered this explanation in response to Data Request ID-WA-1: "It is generally accepted rate setting practice and business practice to repay any debts before credits are applied."

Q. Based on your experience, do you agree with this statement?

A. No, I do not. The notion of having to repay any debts before receiving revenues/credits is not part of any regulatory framework of which I am aware because it flies in the face of the fact that an electric utility business is a "going concern" operating over an extended period of time. An electric utility does not incur debt to build infrastructure and provide service over a discrete period of time, repay all its debt, and then start over in an on-again, off-again fashion because that approach would assume the number of customers, loads, resources, and technologies always

remained the same. Rather, electric utilities continuously plan for and invest in facilities needed for the provision of service to current and anticipated future consumers and finance these investments with a combination of revenues, debt, and equity. In fact, for IOUs, the elimination of all debt could increase the cost of providing utility service because equity usually costs more than debt and it would shift all investment risks to shareholders.

I am not aware of any state regulatory commission that has made the receipt of revenues/credits **contingent upon** the repayment of all debt. In fact, the contention that any debt must be repaid to receive credits is circular because the source of funds for the payment of debt lies in the receipt of credits/revenues.

Q. Do the deemer balances represent debt in a ratemaking setting?

A. I dispute their characterization as "debt" in a ratemaking setting because the purported debt has never been recorded on BPA's or the IOUs' books. Moreover, the IOUs' RPSAs provide that deemer balances "shall not be a cash obligation of the Utility" and the IOUs' Suspension Agreements provide that the deemers shall not cause the utility "to incur any cash obligation to BPA as a result of the suspension", respectively. RPSA at § 10; Suspension Agreement at § 3. Thus, WPAG's assertion that any "debt" must be repaid before credits are applied not only has no regulatory underpinning, but also assumes that unrecorded debts are valid debts.

Q. Did APAC, WPAG, or JP 17 indicate in their testimonies the specific amounts of any of the deemer balances?

A. No, they did not provide any calculations or balances regarding the individual deemer accounts. After acknowledging the integral role the deemer balances play in the Lookback analysis and in setting rates going forward, the parties do not quantify the magnitude of the deemers. They rely upon BPA to "determine the deemer balances during the Lookback period" and to extinguish those balances. WP-07-E-JP17-01, p. 39, l.14; WP-07-E-WA-05, p. 47, ll.9-12, p. 48, ll.13-14; WP-07-E-AP-1, p. 79, ll.19-20.

Q. What reasons do you have to question the accounting of the deemer balances for Idaho Power?

A. In May 1985, the Federal Energy Regulatory Commission (FERC) approved a Settlement Agreement among BPA, Idaho Power, and each direct service industry (DSI) customer regarding Idaho Power's Average System Costs (ASC) filings in several FERC dockets between 1981-1983. WP-07-E-ID-2-AT4, 31 F.E.R.C. ¶ 61240 (May 20, 1985). As indicated in the settlement agreement, BPA credited Idaho Power's deemer account a total of $6.7 million (jurisdictionally separated for Idaho, Oregon, and Nevada). *Id.* at p. 7 (p. 4 of the agreement).

Q. With this $6.7 million credit to Idaho Power's deemer account, were you able to determine the balance of its deemer account?

A. Yes. Following FERC's approval of the 1985 Settlement Agreement, Idaho Power sent a letter dated June 18, 1985 to BPA asking that the agency confirm Idaho Power's deemer balance as of May 31, 1985. WP-07-E-ID-2-AT5. The letter declares that Idaho Power's jurisdictional deemer accounts (again comprised of Idaho,

Oregon, Nevada) totaled $8,068,020.50 as of May 31, 1985. The letter asked that BPA "indicate below by signature if you agree with the [Idaho Power] balances." BPA apparently agreed because the letter was purportedly signed by BPA's representative, Harry J. Allen on July 1, 1985. WP-07-E-ID-2-AT5.

Q. Why is this cumulative deemer balance as of May 31, 1985 significant?

A. In Data Request ID-BPA-4, we asked for a "copy of the calculations or the worksheet(s) used to determine Idaho Power's monthly deemer balances from 1981 to the present." The Excel spreadsheet provided by BPA did not go back to 1981 but the first entries indicated a date of approximately January 1987. The Excel spreadsheet indicated that the deemer balances for each of Idaho Power's jurisdictions were as follows:

Idaho	$52,903,825
Oregon	$ 4,561,262
Nevada	$ 689,064
Total	$58,154,151

If this total amount in the table above is accurate, this means that Idaho Power's deemer account increased by approximately $50 million in the 18 months between May 1985 and January 1987. APAC, WPAG and JP 17 offered no explanation for why Idaho Power's deemer balance increased so dramatically – seven times greater – over so short a period of time, and BPA has offered neither documentation nor explanation for this gap. In fact, no party has offered any evidence explaining this crucial time period in the history of the deemer balances. Similarly, BPA's workpapers in this case show only a beginning balance for Avista in January 1987 and no explanation for the source of that balance.

This lack of evidence is both a recordkeeping and a ratemaking issue. The significant gap in the records of the deemer balances and the magnitude it represents undermine the parties' presumption that inclusion of the deemer balance in this rate case is appropriate. The parties did not calculate the balances, and it is unreasonable to rely on BPA's calculation given the gaps in the record. Parties cannot merely pick a number or reasonably rely on BPA's number for inclusion in the Lookback mechanism.

Q. Are there financial statements or other accounting records that support the calculation of the deemer balances?

A. No. BPA did not record the deemer balances in its financial statements. An "off the books" Excel spreadsheet is not the equivalent of a durable accounting record.

Section 2.1: Deemer Interest

Q. Do you agree with WPAG's assertion that the deemer balances should be "paid in full with interest . . . ."? (WP-07-E-WA-05, p. 47, ll.9-10.)

A. It is unclear exactly what WPAG means by "with interest." All the deemer balances already include interest calculated since 1987. For example, the BPA Excel spreadsheet provided in response to Data Request ID-BPA-4 shows the interest rates applied to Idaho Power's deemer "account." BPA workpapers in this case show similar calculations for Avista's deemer "account." Consequently, it is improper to assess additional interest on the deemer balances.

Q. Have you discovered any other irregularity with the calculation of Idaho Power's deemer account?

A. Yes, in the Excel spreadsheet for BPA's calculation of Idaho Power's deemer accounts, the spreadsheet shows an entry for January 1987 of $52,903,825. ID-BPA-4. In the BPA-Idaho Power "Suspension of Residential Purchase and Sales Agreement" (Suspension Agreement) dated August 22, 1989, paragraph 4 of that document reflects that "the parties agree that Idaho Power's accrued deemer account balance as provided in Section 10 of RPSA is $52,903,825.00, including interest, as of . . . July 31, 1988, for the Idaho jurisdiction." (WP-07-E-ID-AT6.) Both the Suspension Agreement and BPA spreadsheet contain the identical accrual balance but reflect an 18-month time difference.

Q. Did Avista and Idaho Power both suspend their 1981 RSPAs?

A. Yes. Idaho Power's Suspension Agreement (WP-07-E-ID-AT6) with BPA became effective by its terms on July 31, 1988. The Suspension Agreement was dated August 22, 1989. Avista's (then known as WWP) Suspension Agreement (WP-07-E-ID-AT7) became effective June 30, 1987.

Q. Are there significant differences between the Idaho Power and Avista Suspension Agreements?

A. Yes. In particular, there is one significant difference between the termination agreements for the two utilities. Section 4 of both agreements provides the deemer balances will accrue interest. For example, Idaho Power's Suspension Agreement states that "from an August 1, 1988, such amounts shall accrue interest, which shall be compounded quarterly, . . ." WP-07-E-ID-AT6 at p. 4, ¶ 4. In comparison, Section 4 of Avista's Suspension Agreement contains a significant difference. Avista's contract

reads in part: "from and after October 1, 1987, such amounts shall incur interest, which shall **not** be compounded at the average prime rate for each calendar quarter. . . ." *Id.* (emphasis added). In other words, Avista's Suspension Agreement specified simple interest and Idaho Power's Suspension Agreement specified compound interest.

Q. Why is the difference between applying simple and compound interest important?

A. Compound interest adds to the principal balance and assesses interest on interest. According to BPA, the deemers reflect the difference between an IOU's lower ASC and the PF Exchange rate, and that is the **principal** portion of the deemer balances. However, BPA's Excel spreadsheet indicates that, for Idaho Power's deemer balances, every three months the interest is **added** to the principal and interest is then calculated for the next three months on the "new" principal balance. On the other hand, Avista's principal deemer balance has not changed since January 1987 and includes the addition solely of monthly interest accruals.

Q. Have APAC, WPAG, JP 17 or BPA explained why some deemer balances have compound interest and other balances are subject to simple interest?

A. No party has explained why there is a different interest mechanism for some of the IOUs. In my opinion it is unreasonable for some IOUs to have compound interest and others to have simple interest applied to their deemer balances. It is inequitable to apply different interest mechanisms to individual IOUs within the group of IOUs.

Q. Has the difference in simple versus compound interest adversely affected Idaho Power?

A. Yes. Without agreeing to the correctness of BPA's calculations, the application of simple interest on Avista's deemer balance from 1987 to 2007 represents an increase of 2.5 times. Conversely, the application of compound interest for Idaho Power on its alleged deemers balance from 1987 to 2007 has increased its deemer balance 4.2 times. APAC, WPAG, and JP 17 offer no justification for the application of different interest mechanisms between Avista and Idaho Power.

Q. How do the REP benefits compare to the correct deemer balances?

A. Tthe REP benefits from FY 1982 to FY 1994 demonstrate the unreasonableness of the deemer mechanism. As indicated in a summary table prepared by BPA (WP-07-E-ID-AT16), Avista and Idaho Power received REP benefits totaling $6,550,000 and $42,342,000, respectively. In comparison, BPA calculates that Avista's deemer balance is $99.32 million as of October 2007 and Idaho Power's deemer balance is $245.36 million as of October 2007. Clearly, the benefits are over-shadowed by the negative balances in the deemer accounts.

Section 2.2: Deemer Termination

Q. Avista and Idaho Power both terminated their 1981 RSPAs in 1993. Are the companies' termination notices identical?

A. No. Avista's termination notice simply states that Avista gives notice "of its election to terminate its 1981 RSPA effective September 30, 1993. . . ." WP-07-E-ID-AT8. Avista's termination notice is silent on the issue of interest. In comparison, Idaho Power's termination notice dated September 28, 1993 notifies BPA "of its election to terminate that our RPSA effective September 30, 1993." WP-07-E-ID-AT9. Idaho

Power's termination notice goes on to ask that BPA calculate the utility's deemer balances through September 30, 1993 "so that we might then either agree to the calculations or resolve any disagreements about them." *Id.* The Idaho Power notice also states that the utility "agrees that the Company's deemer account balances accrued as of September 30, 1993, . . . shall continue to accrue interest, said interest to be compounded quarterly. . . ." *Id.*

Q. Have you uncovered any reason how Idaho Power and Avista came to have two different termination notices?

A. In a note from BPA's counsel to Avista's counsel and Idaho Power's counsel dated September 21, 1993 (six days before Idaho Power's notice), BPA suggested specific language for the parties to include in their termination notice. WP-07-E-ID-AT10. Idaho Power's termination notice is nearly identical to the language suggested by BPA, including the provision about compound interest.

Q. Did BPA accept Avista's termination notice that does not address the accrual of interest?

A. Apparently not. In a letter dated October 19, 1993, BPA responded to Avista's termination notice. WP-07-E-ID-AT11. BPA's October 19 response states that BPA "accepts the termination [notice] subject to the following conditions." In particular, one condition was that Avista's deemer "account balances accrued as of September 30, 1993 for each of its exchange jurisdiction shall continue to accrue interest, which shall be compounded quarterly, ..." *Id.* (emphasis added). BPA subsequently sent a correction the following day on October 20, 1993 correcting Avista's deemer account

balances as "$41,664,455 for its Washington Jurisdiction and $18,271,996 for its Idaho Jurisdiction." WP-07-E-ID-AT12.

Q. Did Avista notify FERC of the termination of its RPSA?

A. Yes. On September 30, 1993, Avista filed a "notice of termination of rate schedule FERC Electric Tariff No. 1 between WWP and Bonneville Power Administration." WP-07-E-ID-AT13. In a Letter Order dated December 6, 1993, FERC accepted the termination notice effective September 30, 1993. WP-07-E-ID-AT14. FERC's Letter Order also observed that no "comments, protests, or interventions were filed." *Id.*

Q. Did Avista ever agree with BPA's interest accrual condition (WP-07-E-ID-AT11)?

A. Apparently not. In a September 9, 1998 letter to BPA's Administrator, the senior vice president of WWP (now Avista) stated that the utility "*expressly did not agree* with Bonneville's position" that the deemer balance would be carried over to a new contract. WP-07-E-ID-AT15 (emphasis original). Attached to the Avista vice president's September 1998 letter was a position paper prepared by the utility's attorney. The position paper recites that when "WWP terminated the exchange in 1993, WWP expressly did not agree with Bonneville's position that the deemer balance resulting from the change methodology would be carried over to a new contract. WWP's notice of termination contains no such language. While Bonneville sent a confirmation of the termination with its position stated, WWP has never agreed with [BPA's] position." *Id.* at p. 4 of 4.

Section 3: Lookback Analysis

Q. Please summarize the assertions that the APAC, WPAG, and the JP 17 Parties make in their testimonies about the Lookback Analysis?

A. APAC opines that there is no assurance of repayment of the overpayments made to the IOUs through the REP program. WPAG asserts that overpayments to the IOUs should be assessed compound interest. The JP 17 Parties assert that the Lookback Analysis should include the calculation of deemer balances for the time period and the use of the IOUs' ASC filings under the 1984 ASC methodology.

Q. Do you agree with any of these assertions?

A. No.

Q. What risks does APAC identify regarding repayments?

A. APAC states: ". . . in summary the risks are that the victims of the over-collection have no assurance of repayment." WP-07-E-AP-1, p.82, ll.19-21.

Q. Are there actions APAC could have taken to mitigate these risks?

A. APAC could have requested a stay of the WP-02 rates from BPA, FERC, or the Ninth Circuit Court. A stay would have minimized the risk of non-repayment or partial repayment and of mismatching benefits between past and future consumers. The opportunity for mitigation of this risk of repayment has passed, and future residential and small farm customer should not have to suffer for the erroneous WP-02 rates set by BPA. APAC recognizes these "intergenerational equity problems" – "where one set of [COU] customers has suffered the loss while another [set] enjoys the repayment." *Id.* at p. 86, ll.8-9.

Q. Does WPAG provide justification for charging compound interest on over-payments to the IOUs (*Id.* at p. 49, ll.10-12)?

A. WPAG fails to support why compound, rather than simple, interest is appropriate, but, rather, presumes an entitlement to compound interest. Compound interest results in a penalty on a penalty because it assesses interest on both principal and interest. WPAG's self-serving, unsupported assertion that compound interest is appropriate in this case should be rejected. As with the deemer balances as discussed above, compound interest would lead to an unjustifiably punitive result if applied as WPAG recommends.

Q. Do the JP 17 Parties explain how the deemer balances could be calculated for the Lookback period?

A. No. They offer no explanation of how these calculations could be made, except that they should be made just as they were "under the 1984 ASCM prior to the REP settlement." WP-07-E-JP17-1, p. 38, ll.13-16. As discussed above, calculations of the deemer **principal** have not occurred since the late 1980s. So the JP 17 Parties' assertion that deemer balances were calculated on a regular basis in some prior time is false. The only additions to the deemer balance since the late 1980s have been interest (Avista) or interest and interest on interest (Idaho Power).

Q. How do the JP 17 Parties propose to calculate ASC for the Lookback Analysis?

A. They state that the IOUs must submit ASC filings for review pursuant to the 1984 ASCM in order to calculate an "accurate" Lookback. *Id.* at p. 40, ll.9-13. The fact is that the IOUs did not make ASC filings with BPA from 2002-2008 because of the

administrative burden of the preparation and review of such filings. If the ASC filings were made now, a long, drawn out review process would ensue that would unreasonably delay the resolution of this case and would not be any more "accurate" than BPA's use of FERC Form 1 data for the Lookback Analysis.

Additionally, the JP 17 Parties state that "if a utility is not willing to produce these filings, there should be a full forfeiture of any REP settlement payments provided to that entity." *Id.* at p. 37, ll.19-20. Given the number of rate change filings occurring during the Lookback period and the 210-day review for each one under the 1984 ASC Methodology, the JP 17 Parties' view is punitive, if not Draconian, and would serve no purpose other than to obfuscate the process of resolving this rate case and moving forward. Thus, I recommend rejecting this approach.

Q. Do the JP 17 Parties offer any alternatives to the Appendix 1 filings under the 1984 ASC methodology?

A. Yes, in spite of the finality of the above recommendation, the JP 17 Parties, using PacifiCorp's Idaho service territory as an example, suggest that "there are several benchmarks that come to mind to test the reasonableness of this result . . . (1) the actual rate paid by the residential customers in this jurisdiction; (2) the rate charged to large power customers in the jurisdiction; and (3) regular reports filed with utility commissions." *Id.* at p. 32, ll.17-30 and p. 32-33. However, using retail residential or retail industrial rates or reports filed with state commissions for purposes other than setting retail rates seems just as arbitrary and inappropriate as strict adherence to the

1984 ASC filings is rigid. As the Parties are well aware, state rate case decisions and the setting of retail rates reflect a myriad of considerations. As with adherence to the ASC filings under the 1984 methodology, benchmarking is subject to timing and complexity issues not created by the transparency, timeliness, and availability of FERC Form 1 data. Thus, I recommend that a benchmarking approach to evaluating ASCs be rejected.

Q. Does this conclude your testimony?

A. Yes, it does.