BEFORE THE

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IDAHO PUBLIC
UTILITIES COMMISSION

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IN THE MATTER OF THE APPLICATION OF IDAHO POWER COMPANY FOR AUTHORITY TO INCREASE ITS RATES AND CHARGES FOR ELECTRIC SERVICE TO ELECTRIC CUSTOMERS IN THE STATE OF IDAHO.

CASE NO. IPC-E-08-10

DIRECT TESTIMONY OF RANDY LOBB

IDAHO PUBLIC UTILITIES COMMISSION

OCTOBER 24, 2008

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

A. My name is Randy Lobb and my business address is 472 West Washington Street, Boise, Idaho.

Q. By whom are you employed?

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

Q. What is your educational and professional background?

A. I received a Bachelor of Science Degree in Agricultural Engineering from the University of Idaho in 1980 and worked for the Idaho Department of Water Resources from June of 1980 to November of 1987. I received my Idaho license as a registered professional Civil Engineer in 1985 and began work at the Idaho Public Utilities Commission in December of 1987. My duties at the Commission currently include case management and oversight of all technical Staff assigned to Commission filings. I have conducted analysis of utility rate applications, rate design, tariff analysis and customer petitions. I have testified in numerous proceedings before the Commission including cases dealing with rate structure, cost of service, power supply, line extensions, regulatory policy and facility acquisitions.

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

A. The purpose of my testimony is to introduce Staff witnesses, identify issues addressed by each and discuss the various policy issues associated with this case.

Q. Could you please describe Staff's filing in this case?

A. Yes. Staff Auditor Cecily Vaughn begins with actual audited cost data for the historical 12-month base period of January 1, 2007 through December 31, 2007. She then updates the historical data to reflect changes in investment and expense levels through December 31, 2008. The resulting annual revenue requirement increase proposed by Staff is approximately $9.68 million for an overall increase of 1.44%.

The revenue requirement proposal is based on her recommendations for expense adjustments, the rate base additions and expense adjustments of Staff accounting witness Leckie, the various expense adjustments of Staff accounting witness Nobbs, the power supply expense adjustment of Staff Engineering witness Sterling and the cost of capital recommendations of Staff accounting witness Carlock.

Ms. Vaughn is responsible for summarizing all revenue requirement adjustments in the jurisdictional separations study model showing accounting and allocation of Company costs. In addition, Ms. Vaughn specifically discusses the Company's proposed treatment of Adjustment for Funds Used During Construction (AFUDC) associated with Hells Canyon relicensing construction work in progress (CWIP). Ms. Vaughn recommends an adjustment of $2.9 million to reflect a more accurate recovery in rates of annual AFUDC accruals. Ms Vaughn also discusses her recommended reduction of $885,000 in annual P-card expenditures and her $653,000 pass through to customers of the Federal Energy Regulatory Commission (FERC) credit. Finally, Ms. Vaughn addresses the Company proposal to increase various 2007 capital and expense accounts using a compound annual growth rate (CAGR) escalator. Ms. Vaughn recommends reducing the Company's proposed increase in expense accounts from $15.9 million to $1.75 million and reducing materials/supplies related ratebase for an additional revenue requirement decrease of $780,000.

Senior Staff Auditor Joe Leckie discusses various adjustments to O&M expenses and verifies the Company's rate base calculation. Mr. Leckie accepts the Company's calculation of rate base using the 13-month average, including Company proposed plant additions through December 31, 2008, annualizing of major plant additions and escalation in plant accounts under $2 million to arrive at a recommended rate base level of approximately $2.1

billion.

Mr. Leckie also proposes to limit salary expense to known and measureable changes through 2008 resulting in a reduction in Company proposed revenue requirement of $2.9 million. Mr. Leckie further recommends reductions in incentive payments ($3.2 million) and removes the 2009 Structured Salary adjustment (SSA) ($3.0 million). Additionally, he recommends adjustments in miscellaneous revenue, depreciation expense, legal fees and interest paid on deferred director fees to further reduce the Company's request by $2.1 million. Finally, Mr. Leckie discusses the Company's limited application of cost containment and the need to improve cost reduction programs.

Staff Auditor John Nobbs addresses various 900 Series account expense adjustments to reflect the extraordinary level of expenses incurred in the historic base year. Mr. Nobb's adjustments reduce the Company's recommended test year revenue requirement by $667,000.

Senior Staff Engineer Rick Sterling is responsible for review of the Company's Aurora power supply model used to calculate annual net power supply costs. Mr. Sterling proposes an adjustment in the natural gas price forecast used by the Company in its modeling. The results of the forecast modification are increases in fuel expenses, purchase power costs and opportunity sales for an overall decrease in Company proposed annual net power supply expenses of $11.2 million.

Deputy Administrator and Audit Section Supervisor Terri Carlock addresses cost of capital and return on equity. Ms. Carlock recommends a return on equity of 10.25% and a capital structure of approximately 51% debt and 49% equity for an overall recommended rate of return of 8.057%.

Senior Staff Engineer Keith Hessing addresses class cost of service (COS) methodology, class revenue spread and the power cost adjustment (PCA) load growth adjustment component. Mr. Hessing recommends that the Commission accept the 3cp/12cp cost of service methodology proposed by the Company. Using the jurisdictional allocation study modified to reflect Staff's proposed adjustments, Mr. Hessing applies the cost of service (COS) study results to recommend class revenue requirement changes ranging from no change for some classes where COS suggests declines are warranted to a 4.9% cap on the increase for the other classes where larger increases are suggested by the COS. Mr. Hessing's recommendation of no increase for the residential class, when combined with his revenue recommendations for the other classes, generates Staff's recommended overall revenue requirement increase of 1.44 percent. Mr. Hessing further recommends that the load growth adjustment in the PCA remain unchanged from that approved by settlement in Case No. IPC-E-07-08 until the Commission decides the issue in Case No. IPC-E-08-19.

Staff Economist Bryan Lanspery addresses issues associated with residential rate design. After a review of potential rate design alternatives and the Company's proposal, Mr. Lanspery recommends that the Commission adopt a three block tiered rate design with block breaks at 1000 and 2000 kWh per month in winter months and 1000 kWh and 3000 kWh in summer months. Mr. Lanspery determines that the current customer charge of $4.0 per month combined with revenue generated under his summer and winter three tiered energy rate proposal will provide the current annual revenue requirement for the residential class as recommended by Staff. Mr. Lanspery also supports the Company's recommendation to adopt a load factor based rate design for irrigation customers.

Staff economist Matt Elam addresses rate design for all non residential customer classes except irrigation. Mr. Elam evaluates and accepts the rate design proposals of the Company for Schedules 7, 9 and 19 as adjusted for Staff recommended class revenue requirement. While Mr. Elam recommends no change in the Schedule 7 customer charge, he specifically supports the Company recommendation for a year round two tiered energy rate. He also specifically supports the Company recommendation to implement time-of-use (TOU) rates for Schedule 9 commercial customers. Finally, Mr. Elam evaluates the effects of TOU rates on large industrial Schedule 19 customers and supports the Company proposal to increase TOU energy rate differentials.

Staff Economist Lynn Anderson addresses the demand side management (DSM) expenditures made by the Company over the last two years. Mr. Anderson recommends that the Commission defer approval of the Company's DSM program expenditures from the DSM tariff rider for calendar years 2003 through 2007 until sufficient information is provided to evaluate prudency. Mr. Anderson specifies what information should be provided in terms of program specific DSM expenditures and resultant energy savings for presentation in future DSM or general rate proceedings.

Finally, Consumer Investigators Marilyn Parker and Curtis Thaden address a broad range of consumer issues. Ms. Parker concludes that the Company has done a reasonable job of reducing overall customer complaints and improving overall customer service. She specifically recommends that the Company be directed to re-evaluate the convenience fees it charges for electronic payments.

Mr. Thaden provides information on customer income levels and employment levels and evaluates the low income programs provided by the Company.

Q. What has been your role in this case?

A. My role as Staff Administrator has been to oversee the preparation of the Staff case with respect to identification of issues, coordination of positions on those issues and development of Staff policy.

Q. What are the important policy issues in this case?

A. In my opinion, the most important policy issues include establishing the rate case test year, identifying revenue requirement adjustments, assigning cost of service responsibility and applying appropriate rate design.

TEST YEAR

Q. What is the Company's proposed test year in this case?

A. The Company proposes to use a 12-month test year ending December 31, 2008.

Q. Does this represent a change from test year proposals made by the Company in past cases?

A. Yes, it does represent a change in terms of the methods used to establish test year levels for revenues, expenses, investment totals and determine annual revenue requirement.

Q. Please explain.

A. In past rate cases, the Company has used a variety of approaches to establish what it believes to be a representative annual revenue requirement recoverable through rates. It has used 12 months of actual historic cost data updated for known and measurable changes. It has proposed a split test year that utilizes 6 months of actual booked costs and 6 months of forecasted or budgeted costs, with actual cost provided before hearing, to establish annual revenue requirement and set rates. In its last case, the Company proposed a 12-month test period using fully budgeted costs.

In this case, the Company has proposed to start with 12 months of actual 2007 booked costs and then update those costs by including known and measurable expense changes, annualizing for partial year expenditures, annualizing for major plant additions as if they were in service for the entire year and finally, inflating a variety of expense and capital accounts based on the annual growth rate in those accounts over prior years.

Q. Why has the Company continually changed the method by which it determines annual revenue requirement?

A. The Company argues that the methodology changes are necessary to reduce the effects of "regulatory lag" and improve the Company's ability to earn its authorized return.

Q. What is "regulatory lag"?

A. Regulatory lag generally refers to the delay between when the Company actually requests cost recovery and when new Commission approved rates become effective to recover those costs.

Q. How does the Company proposed test year in this case address "regulatory lag"?

A. The Company's proposed test year addresses regulatory lag in the following ways:

1) It updates actual account expenditures incurred during a historical base test period to reflect known and measurable future changes through year-end 2008. Salaries are escalated through 2009.

2) It annualizes partial year test period expenditures to reflect the fact that costs will be incurred in the future for the entire year.

3) It includes forecasted plant additions to be completed before December 31, 2008.

4) It annualizes major plant additions (over $2 million) completed before December 31, 2008 as if they were in service for the entire year.

5) It escalates various expense and capital accounts by a compound annual growth rate (CAGR) based on the growth in that account in prior years.

6) It forecasts variable power supply costs based on estimated 2008 average customer totals.

Q. What is Staff's position with respect to the

Company's proposed test year and adjustments?

A. Staff generally accepts the Company proposed 2008 test year that begins with actual 2007 calendar year costs updated through December 31, 2008. There are notable exceptions associated with forecast methodology. Items 1 and 2 listed above dealing with traditional known and measurable changes and annualization of existing partial year costs have been accepted in the past by the Commission and are supported by Staff in this case. Staff has recommended that salary changes be limited to year-end 2008.

Staff also supports the inclusion of major plant additions (in excess of $2 million) expected to be completed prior to December 31, 2008 and annualizing such plant as if it were in service for the entire year. While this adjustment has been allowed by the Commission in the past on a project by project basis for very large plant additions, it has not been approved across the board for projects as small as $2 million. The Commission has historically required expense reducing or revenue producing offsets to match project cost recovery in rates. Although the Company has included a revenue producing impact for some plant in this case, it has not included any impact for others.

Staff supports some but not all of the Company's proposed escalation of expense and capital accounts on the basis of a CAGR. Staff witness Vaughn addresses the Company's proposal and recommends that escalation be limited to select accounts with more reasonable increases. The effect of this recommendation is an annual revenue requirement that is $15.01 million less than that proposed by the Company.

Q. Company witness Gale states in testimony that the methodology used by the Company to escalate historic expense and capital account totals was consistent with input received by Staff and others in workshops addressing forecasted test years. Why then does Staff oppose the Company's full application of this methodology?

A. Staff agrees that the methodology used by the Company in this case, an escalator applied to historic account totals, is superior to the fully budgeted future test year proposed by the Company in its last general rate case. The impact of the forecast in this case can at least be evaluated. However, Staff does not believe that the Company's choice of escalator or the accounts chosen for escalation reasonably meet the "known and measureable" cost standards.

Q. Can any forecasted increase meet the "known and measurable" cost standard?

A. I believe it is very difficult to meet the known and measurable standard using any budget projection, forecast or estimate of future costs. However, Staff has tried to balance the need for timely cost recovery with the Commission's obligation to audit and verify that costs have been or will be reasonably incurred. That is why Staff has agreed to support including major capital investment in rates before some of the costs are actually incurred and before the plant is actually in service. These major investments are scheduled to be online by December 31, 2008, to be used and useful when rates are effective. Staff has also agreed to go beyond the 13 month average rate base for major plant additions to include plant in rate base as if it had been in service for the entire year. Furthermore, Staff has agreed to use forecasted 2008 customer totals to establish annual variable power supply costs. Finally, Staff has agreed to escalate capital accounts and some expense accounts using the Company proposed CAGR. While Staff does not agree with all of the recommended forecasted increases, it has agreed to cautiously move beyond the strict interpretation of what has traditionally been "known and measurable".

Q. Why does Staff agree with the Company's proposal to account for 2008 capital expenditures?

A. Staff recognizes the impact of growing load on Company expenditures and the need to include major plant additions in rates on a more timely basis. Consequently, Staff supports the Company's proposal for treatment of 2008 plant additions in excess of $2 million. The expected expenditures and the timeline for these additions are generally known and measureable.

Staff has also agreed in this case to accept the Company's proposal to escalate (at 6%) 2008 plant additions with the exception of Staff witness Vaugh's recommended reduction for escalated materials and supplies in ratebase, of less than $2 million. Staff does not believe that this adjustment necessarily reaches the same level of need nor is it as justified from a known and measurable standpoint. Nevertheless, Staff recognizes the smaller capital requirements associated with growing load and will continue to evaluate the merits of escalating these capital accounts in future rate cases. Staff witness Leckie addresses this issue further in his testimony.

STAFF ADJUSTMENTS

Q. Staff has recommended a reduction of $56.9 million in the annual revenue requirement proposed by Idaho Power Company. In what areas were the adjustments made?

A. The annual revenue requirement adjustments were primarily made in the following areas.

1) A decrease of $16.9 million due to a recommended reduction in return on equity from

11.25% to 10.25%.

2) A decrease of $15.01 million due to reductions in the Company's proposed CAGR O&M/materials supplies account escalation.

3) A decrease of $11.2 million in proposed variable power supply cost.

4) A $7.3 million adjustment that includes an increase in miscellaneous revenues, a reduction in legal fees, miscellaneous expenses and P-card expenses, a reduction in depreciation expense, a reduction in annual AFUDC recovery associated with Hells Canyon relicensing and spreading of a prior FERC credit.

5) A decrease of $4.6 million due to reductions in 2008 salary adjustments, a reduction in anticipated 2008 employee and executive salary incentives and elimination of forecasted 2009 salary increases.

Q. You mention above a reduction in the Company proposed adjustment for funds used during construction (AFUDC) associated with Hells' Canyon relicensing. Does Staff oppose the recovery of Hell's Canyon AFUDC in this case?

A. No. In fact Staff agrees that AFUDC recovery through rates is justified in this case. While Staff would not normally recommend recovery of any project cost before the project is completed and expenditures appropriately reviewed, the magnitude of deferred construction work in progress (CWIP) costs, the magnitude of AFUDC associated with those costs and the length of the relicensing process make it necessary in this instance.

Staff agrees with the Company that the current AFUDC accrual on an annual basis should be recovered through rates as an expense rather than allowed to accrue in the deferred account for later recovery through rates as a capital investment. The AFUDC adjustment proposed by Staff simply reflects what Staff believes is a more accurate estimate of annual AFUDC accrual. Staff also believes that AFUDC accrual on Hells Canyon relicensing CWIP should cease after 2009 with a filing by the Company to incorporate all project costs in rates. Staff witness Vaughn discusses the AFUDC adjustment further in her testimony.

Q. How were the areas and magnitude of other Staff adjustments determined?

A. The areas for adjustment were identified as a result of extensive Staff audit of Company books and an evaluation of the methodology and justification used by the Company to update actual 2007 booked costs to the 2008 test year levels.

Staff's overall approach in developing revenue requirement is to identify expenses and investment that are inappropriate or otherwise excessive and should not be subject to recovery from customers. Additionally, Staff evaluated the methodology used by the Company to increase or adjust actual costs to reflect future costs that are expected to be incurred. Staff has tried to balance the need for timely cost recovery with the need to assure that costs are appropriately incurred, and capital investments are both used and useful in providing utility service and known and measurable for recovery through rates.

The specific rationale and justification for each adjustment is further addressed in the testimony of individual Staff witnesses.

Q. Do you believe the Staff recommendation for a 1.44% revenue requirement increase in this case balances the needs of the Company with the needs of its customers?

A. Yes, I do. While Staff has taken a critical look at all underlying Company expenses, the proposed adjustments have been limited almost entirely to return on equity and forecasted increases in expenses for 2008. In fact, except for the CAGR adjustment in materials and supplies addressed by Staff witness Vaughn, Staff recommended no adjustments to Company proposed capital additions. At the same time, Staff has agreed to a broad range of adjustments to the historical base year in developing the 2008 test year designed to allow more timely recovery of capital investment and expenses. These previously discussed adjustments include annualized capital additions forecasted for completion in 2008, CAGR escalation of capital plant additions of less than $2 million, CAGR escalation of O&M expense accounts, the use of variable power supply costs using forecasted 2008 loads and recovery of annually accumulated AFUDC associated with Hell's Canyon relicensing.

I believe Staff's recommendations serve customers by limiting rate recovery to a reasonable level of Company costs. While not moving to a fully forecasted test year as recommended by the Company, Staff has agreed to cautiously move from the traditional definition of known and measureable adjustments of historical data to allow test year adjustments based on estimates and forecasts.

COST OF SERVICE

Q. What other policy positions has the Staff taken in this case?

A. The remaining policy issues deal primarily with class cost of service allocation methodology, rate spread among the classes and rate design. Staff's positions on these issues were developed in conjunction with the technical Staff who address those issues in testimony filed in this case and are discussed by those witnesses. Generally, it is the Staff's policy to maintain consistency between rate cases with regard to power supply, jurisdictional allocations and class cost of service methodologies. Staff believes its methodologies in this case for these functions adhere to that policy.

With respect to cost of service, Staff believes that the 3cp/12cp methodology proposed by the Company reasonably allocates costs to the various classes. Staff believes, and Mr. Hessing explains in his testimony, that the small changes in this methodology over that last approved by the Commission in Case No. IPC-E-03-13 is justified by more accurately assigning cost based on causation. Specifically, the recommended cost of service study provides a more accurate allocation of production costs based on how production plant is used, when it is used and the value of the plant at the time it is used.

With respect to revenue spread among the classes, Staff believes that cost of service is an inexact science to be used as a guide in setting class revenue requirement. That is why Staff witness Hessing uses cost of service in his proposal to move toward, but not all the way to, cost of service as indicated by the study. Mr. Hessing's proposal provides rate stability by limiting revenue requirement changes within each class to a relatively small range. Although cost of service in conjunction with Staff's proposed revenue requirement could have justified a reduction in residential rates, it was determined that no increase was most appropriate. This approach recognizes the potential bill reducing impact on residential customers of the tiered rate design and the moderating effect on other classes of no change in the residential revenue requirement.

RATE DESIGN

Q. What is Staff's policy with respect to rate design within the customer classes?

A. Staff's policy with respect to rate design is to balance the need to send appropriate price signals with the need to have relatively stable rates and appropriate revenue recovery.

Q. What is Staff's position with respect to the rate design recommendations of the Company?

A. Staff believes the Company has done a good job of proposing customer rates that meet the Staff objectives described above. In fact, the Company proposal to establish residential tiered rates year round and increase the first energy block from 300 to 600 kWh per month was quite reasonable. Staff also agrees with the Company's rate design proposals based on irrigation load factor and the Time of Use (TOU) rate proposed for large commercial customers. These rate design proposals recognize the principal that rates should follow costs without sacrificing rate stability. With adjustments for its revenue requirement recommendation, Staff supports all of the rate design recommendations of the Company with the exception of the Schedule 1 residential rate and customer charges for Schedule 7.

Q. Why has Staff proposed a different rate structure for the residential customer class?

A. Staff simply believes that we can and should do more to send the most appropriate price signal to as many residential customers as possible. That is why Staff has made the three tiered inverted block rate proposal to provide at least two break points where rates change to reflect higher production costs. Certainly, time of use (TOU) rates made available with the installation of automated meters will allow the Company to send a broad range of price signals to customers that better reflect cost of service. The multiple tiered rate structure serves a similar role until TOU rates are implemented. Staff witness Lanspery provides greater detail on Staff's residential rate design recommendation.

Q. Does this conclude your direct testimony in this proceeding?

A. Yes, it does.

CERTIFICATE OF SERVICE

I HEREBY CERTIFY THAT I HAVE THIS 24TH DAY OF OCTOBER 2008, SERVED THE FOREGOING **DIRECT TESTIMONY OF RANDY LOBB,** IN CASE NO. IPC-E-08-10, BY MAILING A COPY THEREOF, POSTAGE PREPAID, TO THE FOLLOWING:

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