BEFORE THE PUBLIC SERVICE COMMISSION

OF THE

STATE OF NORTH DAKOTA

PRE-FILED RESPONSIVE TESTIMONY

OF

STEVE GOODNER

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Advocacy Staff, Direct Testimony - Rate Design

Public Service Commission Advocacy Staff

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PRE-FILED RESPONSIVE TESTIMONY
OF
STEVE GOODNER

Q: Please state your name and business address.

A: My name is Steve Goodner. My business address is 2717 NW 45th Street, Oklahoma City, Oklahoma 73112.

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

A: I have been retained by Mathai & Associates Regulatory Consultants LLC to review the cost of service study, the allocation of the any rate change to customer classes and rate design recommendations.

Q: What is your educational background and experience?

A: I received a Bachelor of Science Degree in Accounting from Central State University and a Master of Business Administration from Oklahoma City University. I was employed by Oklahoma Gas & Electric Company (OG&E) for thirty-four years. My overall professional experience has been in the areas of accounting, internal audits, finance and regulation. I worked in accounting and finance from May 1974 until June of 1994. During this time I worked in all areas of accounting including the regulatory section where I prepared the accounting exhibits and assisted in preparation of testimony required in OG&E's filings in Oklahoma, Arkansas and the Federal Energy Regulatory Commission. From 1994 until December 2008, I worked in the Rates and Regulatory Department where I prepared the cost of service studies, assisted in rate design and fuel adjustment clause tariffs, and provided witness testimony in OG&E's Oklahoma and Arkansas rate filings. Since retiring from OG&E in December 2008, I currently provide consulting services on cost of service studies and revenue requirements.

Q: What is the purpose of your testimony?

A: My testimony discusses the following items:

- Discussion of my review of the Montana-Dakota Utilities Company (MDU) cost-of-service study.
- Discussion of the allocation of the proposed rate change proposed to the rate classes,
- Discussion of rate design recommendations.

Q: What is the purpose of a cost-of-service study?

A: A cost-of-service study is used to allocate the total jurisdictional revenue requirement to each customer class.

Q: Mr. Goodner, please describe the term "cost of service" in common terms.

A: The total revenue this Commission allows a public utility an opportunity to collect should be equal to the total costs the public utility incurs to provide electric service to its customers. In a cost-of-service study, particular costs are allocated or directly assigned to customer classes to determine the cost of service for each class. Because costs are generally determined from historical accounting records, this type of analysis is referred to as an "accounting" or "embedded" cost of service study. Costs are allocated to customer classes on a cost causation basis; referred to as a "fully distributed" or "fully allocated" cost-of-service study.

Q: What are the "cost" components of a cost-of-service study?

A: The cost of providing electric service generally includes: (1) Operation and Maintenance Expenses, (2) Depreciation Expenses, (3) Federal and State income taxes, (4) Taxes Other Than Income taxes, and (5) Costs of Capital (Return).

Q: What are the major steps required in the development of a fully allocated cost-of-service study?

A: The development of a fully allocated cost-of-service study consists of three major steps: (1) functionalization, (2) classification, and (3) allocation or assignment. More fully explained below:

1. First, embedded costs are categorized by operating **function** with which the costs are primarily associated. The functional categories ordinarily used in ratemaking are production, transmission, distribution and customer service.

2. These functionalized costs are then **classified** to reflect the manner in which the costs were incurred. Generally, classification further defines functional costs into demand-related (demand usage), energy-related (energy consumption), customer-related (the number of customers served) and directly assigned components.

3. Classification arranges costs into categories so that these costs may be **allocated** to customer classes based on their respective cost causative service characteristics.

The typical cost classifications associated with each functional category are summarized below:

Cost Function	Cost Classification
Production	Demand-Related Energy-Related
Transmission	Demand-Related Energy-Related

Distribution	Demand-Related Customer-Related
Customer Service	Customer-Related

Demand-related costs are generally fixed, and tend not to vary with the use of electric plant facilities or energy production or delivery. Thus, demand-related costs typically are allocated to customer classes based on their respective megawatt (MW) load, or demand, characteristics.

Energy-related costs, however, do vary with use of electric plant facilities. Fuel and variable operation and maintenance expenses are primarily energy-related costs. These costs have been allocated to customer classes based on an analysis of class energy consumption, including losses in delivery.

Customer-related costs are those expenses that are a function of the number and size of customers. Customer-related plant investment includes facilities needed to give customers access to the utility's system. Other customer-related costs include expense items such as customer accounts, customer service and information, meter operation and plant-associated O&M expenses.

Q: What does the third step - allocation or assignment - involve?

A: The final step in the process is allocation, which involves apportioning (dividing) functionalized and classified costs to jurisdictions and customer classes of service. Direct assignments are used when costs can be identified as being wholly attributable to a particular customer, customer class, or jurisdiction. Investment in a substation used solely by a customer is one example of a cost that is properly directly assigned to a specific customer class.

After all costs have been allocated or assigned to jurisdictions and customer classes, a cost to serve is calculated for each jurisdiction and customer class; the respective sum of such service costs constitutes the total company cost to provide service.

Q: What criteria should be considered in the development of the allocation factors?

A: The following criteria, although not an exhaustive list, provides an objective basis upon which to judge the appropriateness of an allocation methodology:

1. The method should reflect the operating and planning characteristics of the utility system.

2. The method should recognize the various customer class characteristics such as peak demand, energy usage, load factor, diversity characteristics, number and size of customers, points of delivery, etc.

Q: Please discuss your review of MDU's cost of service.

A: My review covered each step of MDU's cost of service study for reasonableness and the use of accepted cost causation principles. The National Association of Regulatory Utility Commissioners Electric Cost Allocation Manual (NARUCCAM) was the standard for the review. This manual provides cost causation principles that have been developed over time based on a consensus of how cost of service studies should be performed.

Q: Please discuss your review of the Functionalization step.

A: The functionalization of the cost of service components are usually straight forward since most of the rate base and cost components are already functionalized through the Federal Energy Regulatory Commission (FERC) system of accounts. The common components require that they be assigned to one of the four functions based on any direct related associations or based on plant, operation & maintenance labor or total operation & maintenance expenses.

Q: What were the results of your review of the functionalization step?

A I did not find any exceptions with MDU's functionalization of rate base or expenses. The functionalization followed cost causation principles and provided the separation needed to perform the next step which is classification. However, I did not go into any detailed analysis of tracing any individual expenses or investments as Mr. Mathai attempted in his Corporate and jurisdictional allocation analysis of the overall jurisdictional Revenue Requirement calculations.

Q: What were the results of the review of the cost of service classification step?

A: The classifications assigned by MDU followed accepted cost causation principles. Classification of costs provides a direct link between costs and the tariffs developed to collect those costs. Tariffs that are based on costs then are considered to be just and reasonable.

Q: What were the results of the review of the cost of service allocation step?

A: The allocators used in the Company's cost of service were reviewed in light of two criteria. First, verification to determine if each allocator used was consistent with the type of classification assigned to each component to be allocated. For example, if the cost of service component was classified as customer, the allocator should include the number of customers as the basis for the calculation. Second, I reviewed the inputs and structure of the allocator calculation. For example, the review considers whether the allocator should include the number of customers or weighted customers. It appears the allocators used in MDU's cost of service followed accepted guidelines and provide a reasonable allocation of costs to each class based on cost causation principles.

Q: In summary what are your recommendations or general comments related to the Company's cost of service?

A: The MDU class cost of service study provides in my judgment, results that follow established guidelines and allocates the costs that each class causes MDU to incur to

provide service. The cost of service study then provides a reasonable standard to use in the development of rates to be charged to each customer class. I also performed a review to determine if the cost of service properly matched fuel revenue with fuel costs. The fuel revenue was properly matched with fuel costs and therefore did not impact the excess or deficiency calculation.

Q: How do you propose to spread the rate change to the customer classes?

A: Mr. Mathai has proposed a reduction of $2,804,000 to the base rates. This would be a 2.5% decrease to the current projected electric retail revenues of $110,925,000. I propose to spread the reduction based on the ratio of each class's electric revenue to the total electric revenue (less contracts revenue). The allocation of the reduction is shown on Exhibit No. (SMG-1).

Q: Please discuss your rate design recommendations.

A: First, I recommend the elimination of the declining block rates in the October through May period for the Residential Electric Service Rate 10 and the Small General Electric Service rate 20. Tariffs should provide price signals that indicate the amount of resources or costs that are required to provide the customer with electric service. If costs increase with the use of energy, prices should also signal this increase. Declining block rates send a price signal to customers that when usage exceeds a certain kilo-watt hour (kwh) level that the costs decline with usage of kwhs greater than a certain level. This price signal does not encourage the efficient use of energy. A flat rate per kwh for the months of October – May will send the proper price signal to customers to help encourage their efficient use of energy.

Q: What is the second rate design recommendation?

A: The second recommendation is for the Commission to accept MDU's proposal to increase the Basic Service Charge to $10.64 per month for the Residential Electric Service Rate 10. This adjustment will move the charge closer to the actual cost shown in the class cost of service. MDU's class cost of service for the Residential class calculated a Basic Service Charge of $16.50 per month. This adjustment will move the Basic Service Charge approximately half way to the cost of service determined by the cost of service study. Gradualism is needed to minimize the impact on customers and allow them to adjust to the change in costs. Any negative customer impacts from this change should be partially or totally offset by the proposed rate reduction to this class.

Q: Are there any additional recommendations?

A: Yes. I concur with MDU's proposal to charge different fuel prices for the primary and secondary service levels. The MDU proposed projected base cost of fuel is $.02055 per kwh as shown on RAM-1. MDU is proposing to charge a fuel price of $.02024 per kwh for primary service and $.02087 per kwh for secondary service to recognize the real difference in the delivered cost of fuel at different service levels. This price change is needed to charge customers a price of fuel that better represents the actual cost of fuel cost at each service level.

Q: Please discuss MDU proposed adjustment clauses.

A: MDU is proposing to add three adjustment clauses, Load Management Tracking Adjustment Rate Schedule 54, Renewable Resource Cost Recovery Rider Rate Schedule 55 and Transmission Cost Recovery Rider Rate Schedule 56. The Renewable Resource Cost Recovery Rider is addressed by Mr. Mathai. Tariffs should be developed when a need to collect costs exists and can be supported by known and measureable facts and figures. This allows for an adequate review process needed to develop tariffs. These conditions do not currently exist; therefore, I recommend that the approval of the Load Management Tracking Adjustment and the Transmission Cost Recovery Rider be denied in this case. The Commission should consider these riders when all facts are available for analysis and determination. In Staff's opinion, these proposals are premature for current approval.

Q: Does this conclude your testimony?

A: Yes, it does.

Case No. NDPSC Case No.PU-10-124

Exhibit No. (SMG-1)

MONTANA-DAKOTA UTILITIES CO.
ADVOCACY STAFF POSITION
ELECTRIC UTILITY - NORTH DAKOTA
PROPOSED ALLOCATION OF REVENUE CHANGE

Class Name	Class Code	Projected Electric Revenues	%/1	Allocated Rate Change
Residential	R10	$ 45,802	42.3%	$ (1,187)
Small General	R20	$ 8,259	7.6%	$ (214)
Irrigation Service	R 25	$ 45	0.0%	$ (1)
Large General Service Primary	R 30-P	$ 5,278	4.9%	$ (137)
Large General Service Secondary	R 30-S	$ 41,418	38.3%	$ (1,073)
TOD Large General Service	R 31	$ 537	0.5%	$ (14)
Space Heating	R32	$ 1,854	1.7%	$ (48)
Small Municipal Service	R 40	$ 310	0.3%	$ (8)
Municipal Lighting Service Primary	R 41 P	$ 111	0.1%	$ (3)
Municipal Lighting Service Secondary	R 41 S	$ 1,302	1.2%	$ (34)
Municipal Pumping Service Primary	R 48 P	$ 418	0.4%	$ (11)
Municipal Pumping Service Secondary	R 48 S	$ 1,281	1.2%	$ (33)
Outdoor Lighting Service	R 52	$ 494	0.5%	$ (13)
Interruptible Power Service	R 39	$ 173	0.2%	$ (4)
Interruptible Demand Response	R 38	$ 911	0.8%	$ (24)
Contracts		$ 2,732	0.0%	
	Total	$ 110,925	100.0%	$ (2,804)
Electric Revenues Less Contracts		$ 108,193		

1 Projected Electric Revenues / Electric Revenues Less Contracts

Prosposed Revenue Change (Reduction) (2,804)