STATE OF SOUTH DAKOTA

SOUTH DAKOTA PUBLIC UTILITIES COMMISSION

MIDAMERICAN ENERGY COMPANY	)	
	)	
Proposed general increase in electric rates.	)	**DOCKET NO. EL14-___**
	)	
	)	

DIRECT TESTIMONY
OF
RICK R. TUNNING

Q. Please state your name and business address.

A. My name is Rick R. Tunning. My business address is 666 Grand Avenue, Des Moines, Iowa 50309.

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

A. I am employed by MidAmerican Energy Company ("MidAmerican" or "Company") as Manager – Corporate Accounting.

Q. Please describe the responsibilities of your current position.

A. As Manager of Corporate Accounting, I am responsible for the preparation of shareholder, U.S. Securities and Exchange Commission, and state/federal regulatory financial reports and financial planning and budgeting for MidAmerican and MidAmerican Funding, LLC.

Q. Please describe your education and business experience.

A. I graduated from Northwest Missouri State University in 1980 with a Bachelor of Science degree in accounting. I received a Master of Business Administration degree from the University of South Dakota in 1989. I worked in the audit division of Arthur Andersen & Co. until 1982. At that time I started working for Iowa Power Inc., a MidAmerican predecessor company, as an internal auditor. I have worked in a number of audit and accounting management capacities since that time. I was appointed to my present position in 1995. I am a member of the Edison Electric Institute Accounting Standards Committee.

Q. Have you testified previously before the South Dakota Public Utilities Commission?

A. Yes. I have testified on behalf of MidAmerican in other gas proceedings before the South Dakota Public Utilities Commission (Commission) and in a number of similar electric and gas proceedings in Iowa and Illinois.

Purpose of Testimony

Q. What is the purpose of your testimony?

A. The purpose of my prepared direct testimony is to support MidAmerican's South Dakota jurisdictional electric rate filing in the following areas:

- South Dakota jurisdictional electric revenue requirement
- South Dakota jurisdictional electric test year operating income
- Capital structure and weighted average cost of capital

Q. Are you sponsoring any exhibits?

A. Yes, I am sponsoring MidAmerican Exhibit RRT 1.1 comprised of numerous schedules that are discussed in more detail below.

Revenue Requirement

Q. Please describe MidAmerican Exhibit RRT 1.1 Schedule 1.

A. MidAmerican Exhibit RRT 1.1 Schedule 1 summarizes the South Dakota jurisdictional electric revenue requirement. It reflects a revenue deficiency of $1,602,000. The adjusted test year rate base amount shown on line 1 is discussed by MidAmerican witness Mary Jo Anderson. The cost of capital amount shown on line 2 is summarized on MidAmerican Exhibit RRT 1.1 Schedule 25 and is discussed later in my testimony. The adjusted test year operating income amount shown on line 4 is summarized on MidAmerican Exhibit RRT 1.1 Schedule 2 and is discussed in more detail below.

Q. Have MidAmerican's 2013 books and records been audited by independent auditors?

A. Yes, Deloitte and Touche annually audits MidAmerican's financial statements, including those for 2013.

<u>**Operating Income**</u>

Q. Please describe MidAmerican Exhibit RRT 1.1 Schedule 2.

A. MidAmerican Exhibit RRT 1.1 Schedule 2 summarizes the test period and pro forma South Dakota jurisdictional electric operating income. Column (b) of this schedule presents actual South Dakota jurisdictional electric amounts, as reflected in MidAmerican's books and records, for the year ended December 31, 2013. Column (c) presents adjustments to test year actual amounts as summarized on MidAmerican Exhibit RRT 1.1 Schedule 3. Column (d) presents adjusted test year operating income. Column (e) presents the revenue adjustment supported by this filing.

Q. Does MidAmerican offer unregulated gas and electricity for sale to unregulated customers within and outside of its South Dakota service territory?

A. Yes. During 2013 a division of MidAmerican Energy Company made competitive retail gas sales both within and outside of South Dakota and competitive retail electric sales in states other than South Dakota.

Q. Do any amounts presented on RRT Schedule 2 pertain to such unregulated activities?

A. No. All amounts on RRT Schedule 2 pertain to MidAmerican's South Dakota regulated electric operations and no amounts are attributable to its nonregulated operations. MidAmerican's accounting system segregates revenues and costs of its regulated operations from those of its nonregulated operations. Controls over this accounting separation are reviewed annually by MidAmerican's internal audit department.

Pro Forma Adjustments

Q. Please describe MidAmerican Exhibit RRT 1.1 Schedule 3.

A. MidAmerican Exhibit RRT 1.1 Schedule 3 summarizes 18 adjustments to test period South Dakota jurisdictional electric operating income. Individual adjustments, with references to supporting workpapers, are presented in RRT Schedules 4 through 21.

Q. Please describe the interest synchronization adjustment on MidAmerican Exhibit RRT 1.1 Schedule 4.

A. This adjustment decreases income tax expense and is required in order to match, or "synchronize", the long-term interest deduction for purposes of the current income tax calculation with the interest expense included in the revenue requirement. MidAmerican records in its books estimates for the interest synchronization adjustment throughout the year and this pro forma adjustment merely updates those estimates for the rate base and cost of debt values supported in this case.

Q. Please discuss the property tax expense adjustment summarized on RRT Schedule 5.

A. Under Iowa law, wind facilities are specifically assessed based on original cost and such assessments are 100% abated in the first year of operation. After the first year of operation, the taxable portion of the turbines increases 5% annually until reaching the maximum 30% of taxability in year seven. This adjustment recognizes the scheduled increment of taxability for turbines that were in service prior to 2013. This adjustment thus increases property tax expense for the scheduled increased assessments for MidAmerican's wind projects.

Q. Please describe the payroll adjustment on MidAmerican Exhibit RRT 1.1 Schedule 6.

A. This adjustment increases test year labor expense for known and measurable pay increases. The adjustment includes the annualization of pay increases that were effective during 2013 for employees represented by two union locals and the annualized 2014 pay increases for all employees, including the mid-2014 increases for those two locals and the January 1, 2014 increases for salaried employees. The adjustment also includes increases for benefit costs that are directly impacted by base pay increases, including payroll taxes and Company 401(k) match. Finally, this adjustment removes the effect of pay increases associated with labor charged to production maintenance and distribution maintenance to avoid duplication with normalization adjustments for these costs summarized on RRT Schedules 14 and 15 and discussed in more detail below.

Q. Please describe the retirement plan cost adjustment on MidAmerican Exhibit RRT 1.1 Schedule 7.

A. This adjustment increases cost of service for changes in expense for post-employment benefits. The adjustment is based on the difference between a 2012-2014 three-year average of such expenses and amounts included in the test year for these plans. Amounts recorded for these plan expenses result from actuarial calculations pursuant to the requirements of Accounting Standards Codification Topic (ASC) 715 (formerly Statement of Financial Accounting Standard (SFAS) Nos. 87 and 106).

Q. Please explain why the adjustment is based on a three-year average of plan costs.

A. Expense amounts for these plans are subject to significant volatility, due in part to changes from year to year in the actuarial assumptions required by the ASC 715 calculations performed by the actuaries, and in part to changes in the value of plan assets. The interest rate movements normally experienced in the markets and the significant drop in investment values during 2008 and subsequent recovery are evidence of the volatility that impacts the ASC 715 calculations. Lower interest rates generally have the effect of increasing plan expense and higher interest rates generally have the effect of decreasing plan expense. Similarly, lower plan asset values increase plan costs. Use of a three-year average recognizes this volatility and adjusts benefit plan costs to a more reasonable level.

Q. Please describe the adjustment for depreciation on rate base pro forma adjustments on MidAmerican Exhibit RRT 1.1 Schedule 8.

A. This adjustment increases depreciation expense for the depreciation associated with the rate base adjustments net of lower depreciation expense associated with 2013 and 2014 depreciation rate adjustments and scheduled retirement of certain coal generation facilities. This adjustment is supported by MidAmerican witness Anderson.

Q. Please discuss the Wind VIII adjustment summarized on RRT Schedule 9.

A. This adjustment annualizes estimated amounts for revenue, operations and maintenance expense, property tax expense and production tax credits associated with wind turbines placed in service during 2013-2015 for the Vienna II, Wellsburg, Macksburg, Lundgren and Highland projects, which are expected to favorably impact jurisdictional operating income. MidAmerican witness Anderson addresses comparable adjustments to update rate base and depreciation expense for these additions.

Q. At what price was revenue from the annualized production of these projects calculated?

A. Since the generation from these wind turbines will have a zero incremental cost, it will be assigned to retail customers. However, it will initially enable greater wholesale sales at market prices. Those sales have been priced using the average annual 2013 price received from the Midcontinent Independent System Operator, Inc. ("MISO") for wind generation.

Q. What do you mean by the term "annualized"?

A. That term means the expected amount (production, expense, etc.) for each project in the first full calendar year of service. With respect to property taxes, the expense is the first year in which property taxes are owed on the project, or in the second calendar year of service.

Q. Please discuss the test year sales growth adjustment summarized on RRT Schedule 10.

A. This adjustment estimates increased revenue that would result from sales reflective of period-ending residential and commercial customer counts compared to average customer counts for those classes, less displaced wholesale revenue, and is consistent with the annualization of rate base associated with major project additions during the test year. Additionally, this adjustment results in increased depreciation expense for distribution plant used to serve these new customers that is not included in the adjustment for major project additions. MidAmerican witness Anderson supports the depreciation portion of this adjustment. A similar sales growth adjustment has not been proposed for industrial or other customers because of the lack of homogeneity in usage patterns among customers within these other classes.

Q. Please describe the coal plant retirements adjustment summarized on MidAmerican Exhibit RRT 1.1 Schedule 11.

A. MidAmerican anticipates the retirement of Walter Scott Energy Center Units 1 and 2 and Neal Units 1 and 2, and the operation of Riverside Generating Station solely on natural gas by 2015. This adjustment removes estimated test year wholesale margins lost from these units, reduces operation and maintenance ("O&M") expense to ongoing levels expected post-closure and removes test year property tax expense for each of the units.

Q. Why are test year O&M costs associated with these units not completely removed?

A. Certain costs will not be changed by unit retirements. The units are allocated a portion of costs that are common to multiple units at their respective locations. For example, Neal 1 and 2 share certain costs such as maintenance of grounds and common structures with Neal 3. With the retirements, these costs would be largely unchanged in total, but would be assigned to Neal 3 solely (less amounts charged to Neal 3's partners) instead of being assigned partially to Neal 1 and 2. In addition, there will be a need for a minimal amount of O&M for security and other matters related to the retired units.

Q. **Please describe the scrubber consumables adjustment summarized on RRT Schedule 12.**

A. This adjustment increases test year operations expense for the estimated cost of chemicals to be consumed in the operation of environmental equipment that was or is being installed at Neal Unit 3, Neal Unit 4 and Ottumwa Generating Station ("Ottumwa") for which rate base adjustments are supported by MidAmerican witness Anderson. The chemicals include lime, urea and activated carbon. The adjustment applies the actual 2013 cost per megawatt hour generated for such chemicals at Walter Scott Unit 4 to the 2013 megawatt hours generated at Neal 3 and 4 and Ottumwa.

Q. Why was Walter Scott Unit 4 used as the basis for the calculation?

A. It is the only MidAmerican-operated plant that has comparable equipment to that being installed at the other three plants.

Q. Please describe the adjustment for long-term incentive partnership costs on MidAmerican Exhibit RRT 1.1 Schedule 13.

A. This adjustment decreases test year operating expenses for costs accrued for the long-term incentive partnership ("LTIP") plan. This plan, administered by Berkshire Hathaway Energy Company, provides incentive payments to selected participants based, in large part, on financial performance factors. MidAmerican is not seeking recovery for these costs at this time due to the fact that the award for such pay is predominantly driven by achieving net income targets and removal of these costs is consistent with past treatment of such costs in South Dakota.

Q. You mention the LTIP incentive compensation program. Does MidAmerican maintain any other incentive compensation programs for its employees?

A. Yes. A portion of the total compensation of each non-represented MidAmerican employee is paid through MidAmerican's Performance Incentive Plan ("PIP"), which has been in place since 1997. During the test period, the amount of South Dakota electric compensation paid under the PIP and included in test year cost of service was $71,812.

Q. Why is PIP included in cost of service but LTIP excluded?

A. As noted above, LTIP awards are predominantly driven by financial results to a limited group of employees. The PIP plan, on the other hand, is an integral part of the compensation plan for all non-represented employees that is merely a mechanism to deliver market-based total compensation to such employees. The "incentive" nature of the plan pertains to the administration of the PIP as it relates to individual employees. Total-company payouts are targeted to provide market-based compensation, although individual employees experience varying results depending upon performance relative to their individual goals (i.e. "performance").

Q. So there are no financial triggers for the PIP?

A. Correct. A number of corporate goals are considered in the context of the decision on what the PIP award should be on a total company basis. However, the PIP award is not triggered or sized by the level of MidAmerican's earnings.

Q. How does the PIP impact MidAmerican's total compensation?

A. PIP is designed to have no net impact on total MidAmerican compensation costs. Under PIP, a portion of base salary to each employee is, in effect, at risk. The PIP compensation is distributed to employees based upon their performance, but does not have the impact of increasing overall compensation costs, which remain at market levels.

Q. Please describe the steam maintenance expense adjustment on MidAmerican Exhibit RRT 1.1 Schedule 14.

A. This adjustment normalizes maintenance costs for MidAmerican's coal units by adjusting test year values to five-year average values. Maintenance costs for MidAmerican's coal generation facilities can vary significantly from year to year depending upon where each of the units is with respect to its major maintenance cycle and the extensiveness of the maintenance performed. Five years was selected as the normalization period since these units are generally on a five-year cycle for major overhaul work.

Q. Why is an inflation factor included in the calculation?

A. While an average of the five years of actual costs reflects changes in the level of work activity, it ignores changes in cost levels for the work being performed over that period of time. The Handy-Whitman index is a well-established measure of historical change in prices for various utility industry activities. The index used in this calculation is pertinent to the costs being averaged. Additionally, since the calculation was an average, the change in the index over the five years was averaged as well.

Q. Please describe the distribution maintenance expense adjustment on MidAmerican Exhibit RRT 1.1 Schedule 15.

A. This adjustment normalizes maintenance costs for MidAmerican's electric distribution system by adjusting test year values to five-year average values. Distribution costs can vary significantly from year to year due to the occurrence of storms, flooding or other unpredictable circumstances. A multi-year average of such costs smooths the impact of such occurrences. Five years was used to be consistent with the approach used with steam maintenance. A distribution plant inflation index was used in the calculation for the same reasons outlined above for steam maintenance.

Q. Please describe the adjustment for Ottumwa capacity increase on MidAmerican Exhibit RRT 1.1 Schedule 16.

A. This adjustment increases operating revenue for capacity increases associated with an Ottumwa turbine upgrade project to be implemented in conjunction with the scrubber/baghouse project at Ottumwa. The increased revenue is based on the test year capacity factor, average locational marginal price and average fuel cost and on expected 2014 capacity prices for Ottumwa.

Q. Please describe the adjustment for weather normalization on MidAmerican Exhibit RRT 1.1 Schedule 17.

A. This adjustment decreases test year operating revenue for the impact of weather variations from normal during the test year. MidAmerican witness Charles Rea supports this adjustment.

Q. Please describe the late payment charge adjustment summarized on MidAmerican Exhibit RRT 1.1 Schedule 18.

A. This adjustment eliminates late payment revenue recorded during the test year. This rate treatment is in lieu of using actual payment collection days in MidAmerican's working capital calculation, where a 20-day period is used instead. This adjustment is consistent with the ratemaking treatment of this item in a number of MidAmerican's previous rate proceedings before the Commission.

Q. Please describe the adjustment for energy efficiency revenue and costs on MidAmerican Exhibit RRT 1.1 Schedule 19.

A. This adjustment removes from the revenue requirement all revenue and operation and maintenance expense amounts relating to energy efficiency programs. These costs and related recoveries are accounted for in a separate rider.

Q. Please describe the adjustment for out of period income tax adjustments on MidAmerican Exhibit RRT 1.1 Schedule 20.

A. This adjustment increases income tax expense through the reversal of entries made during 2013 that modified income tax expense for periods prior to 2013, and therefore are not representative of ongoing expense relative to test year activity. The tax adjustments recorded in 2013 reconciled income tax expense booked during 2012 to the amounts reflected in the 2012 tax return that was filed in late 2013, and included more refined estimates for various issues relative to those that were originally contemplated at the time the books were closed for 2012. Since these adjustments pertain to 2012, and not 2013, they are not appropriate to include in the test year for this case.

Q. Please describe the adjustment for rate case expense on MidAmerican Exhibit RRT 1.1 Schedule 21.

A. This adjustment normalizes the estimated incremental, out-of-pocket costs of preparing and litigating this case by amortizing such costs over five years. Five years is a reasonable normalization period. MidAmerican witness Kutsunis supports the estimated costs used in this adjustment.

Capital Structure and Cost of Capital

Q. Please discuss MidAmerican's cost of capital, as summarized on RRT Schedule 25.

A. The weighted average cost of capital summarized on RRT Schedule 25 presents MidAmerican Energy's pro forma average costs for long-term debt and common equity for the twelve months ended May 31, 2014. The weighted average cost of capital is 7.60%.

Q. Why was the twelve months ended May 31, 2014 used to measure the cost of capital?

A. May 31, 2014 was chosen over the calendar year 2013 for several reasons. First, a sizable amount of long-term debt was issued in April 2014 that impacts the cost of capital. Second, notes with scheduled maturity in October 2014 were redeemed early in May 2014. Third, significant time has elapsed since the end of 2013 and the calculation as of May 31, 2014 reasonably updates the calculation with more current values. Fourth, a number of rate base pro forma adjustments are included in MidAmerican's case, and an updated cost of capital more consistently matches the pro forma rate base.

Q. Were any adjustments to actual values made?

A. Generally not, although gains and losses, and associated amortizations, on past early redemptions of debt that were not deferred for book purposes are included in the cost of long-term debt calculation consistent with what has been done in past South Dakota gas rate cases.

Q. Please discuss the determination of the cost of MidAmerican's long-term debt component on RRT Schedule 26.

A. The sum of the interest costs and amortization of long-term debt discount, issuance expense and loss on reacquired debt less the amortization of gains on reacquired debt was divided by the 12-point average outstanding long-term debt balance. The 12-point outstanding balance was determined by calculating the average actual balances from June 2013 through May 2014 for the following components:

a. Each issue of long-term debt,
b. Unamortized long-term debt premium,
c. Unamortized gain on reacquired long-term debt,
d. Unamortized debt discount,
e. Unamortized issuance expense, and,
f. Unamortized loss on reacquired long-term debt.

Q. Please discuss the determination of MidAmerican's cost of common equity.

A. MidAmerican's cost of common equity is 10.7%. MidAmerican witness Vander Weide supports this amount.

Q. Does that conclude your prepared direct testimony?

A. Yes, it does.