BEFORE THE

WYOMING PUBLIC SERVICE COMMISSION

DIRECT TESTIMONY

OF

MICHAEL E. EASLEY

POWDER RIVER ENERGY CORPORATION

Docket No. 10014-168-CR-16

Q. Please state your name and address.

A. My name is Michael E. Easley and my business address is Powder River Energy Corporation, P.O. Box 930, Sundance, WY 82729.

Q. What is your present occupation?

A. I am employed as Chief Executive Officer of Powder River Energy Corporation ("PRECorp" or "the Cooperative").

Q. What are your duties as Chief Executive Officer of Powder River Energy Corporation?

A. My duties are to supervise the operations of the Cooperative; to make recommendations to the Board of Directors with respect to strategy, policy and to administer the policies adopted by the Board of Directors; to provide both short-term and long range plans for the operation, construction, and financing of the Cooperative; to maintain an adequate and suitable work force; and to keep the Board informed in all aspects of the management of the Cooperative.

Q. Please state your educational background and professional qualifications.

A. I have a BS degree in Electrical Engineering from Oklahoma State University and I am a graduate of the Ken Blanchard Executive MBA program at Grand Canyon University. I am also a graduate of the National Rural Electric Cooperative Association Management Internship Program at the University of Nebraska-Lincoln. I have held various positions of increasing responsibility in the cooperative utility industry and have been the CEO of PRECorp since October of 2000.

Q. Does Exhibit ME-1 accurately reflect your professional background and qualifications?

A. Yes.

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to provide a high level view of PRECorp's current operating environment and a historical look back including information regarding the notable trends and future projections. I will explain the overall objectives of this rate application, and briefly discuss its significant elements.

Q. Will PRECorp present additional witnesses?

A. Yes. Mr. David Hedrick of C.H. Guernsey and Company will provide the detailed technical testimony regarding the Cost of Service Study ("COSS") and rate analysis that supports this general rate case and objectives stated above. Mr. Curtis Mock will provide an analysis of key operating ratios that are requirements of our lenders.

Q. What are the specific objectives of this rate filing?

A. The specific objectives of this rate filing are: (a) increase the system revenue requirement by approximately $11.5 million to address a revenue shortfall; (b) rebase our rates and reset our Cost of Power Adjustment ("COPA") to zero; (c) move all rate classes closer to cost of service; (d) increase the monthly basic charge for several classes to better recover fixed costs as identified in the Cost of Service Study and increase the per horsepower charge for the Irrigation class to the same end.

Q. Please explain the guiding criteria used in developing this general rate filing.

A. PRECorp's mission is to deliver high quality, competitively priced power and services to our member-owners, while enhancing the quality of life by providing leadership and service in our communities. This rate filing was developed with the goal of ensuring PRECorp's operational and financial stability in a declining sales environment. This declining sales environment has led to a revenue shortfall for PRECorp. This shortfall is the driving need behind this application.

Q. Can you describe PRECorp's service territory?

A. PRECorp provides electric power to Crook, Weston, Campbell, Johnson and Sheridan Counties in northeast Wyoming, in addition to a small area of southern Montana. Our service area includes the bulk of the Powder River Basin, and our service area in Montana includes two large coal mines, Decker and Spring Creek.

Q. What has changed in PRECorp's approach to financial management and rates in this application?

A. The events creating PRECorp's revenue shortfall are the product of forces beyond our control as were the events leading into the CBM boom that began in early 2000. Historically the PRECorp Board has requested Commission authority for rates that would produce the minimal financial ratios required to meet our mortgage requirements. We depended upon system growth, and our various risk management strategies, to produce or support margins and ratios in excess of minimum requirements. Also, PRECorp relied on capital credit retirements from its power supplier Basin Electric Power Cooperative (BEPC) to augment the Rural Utilities Service (RUS), Operating TIER (OTIER) ratio, but Basin has been unable to retire capital credits due to its equity position and financial covenant requirements. The approach has served us well during times of growth and is workable for short duration in times of stability. However, this approach does not work during periods of declining sales, as we are currently experiencing. In this application, PRECorp is requesting rates that produce the margin necessary to maintain a mid-level RUS OTIER of 1.5.

PRECorp's CFO will provide testimony explaining the importance of this RUS OTIER level. In the opinion of PRECorp's Board of Directors, this 1.5 RUS OTIER level, along with our other risk management strategies, provides some room for things to be worse than we would hope without overreacting to the currently anticipated factors and situation we find ourselves in.

Q. Please provide a high level view of your current operating environment and compare and contrast it to historical conditions.

A. The best analogy would be to say that PRECorp has gone through a boom and bust cycle beginning in early 2000 when PRECorp was responding to the development boom of the Coal Bed Methane (CBM) industry. We experienced near exponential growth with our load doubling in a 10-year period.

We are currently experiencing a significant downturn with a declining sales environment and the natural resource extraction industry being stressed by low commodity prices and increasing regulatory pressures. CBM has been in decline since 2010 due to competition with other more profitable production areas in the U.S. and increasingly difficult environmental regulations in the Powder River Basin (PRB) area. From 2010-2013 PRECorp's overall system sales were kept relatively stable, in spite of declines in CBM sales, with increasing oil related loads and stable sales to the coal mine industry. However, CBM declines continued through 2014 and rapidly accelerated and began to impact the entire system in 2015 due to low global oil prices, continued low gas prices, and market uncertainty created by the EPA's Clean Power Plan. Please see Exhibit ME-2 for a comparison of PRECorp's sales since 2000.

The impacts that PRECorp is feeling are not isolated and are, in fact, being seen across Wyoming and beginning to show up in reports issued by the State of Wyoming. The Economic Summary 3Q2015, prepared by the Economic Analysis Division, indicates how these factors are impacting the

Global, US, and Wyoming economies. This report is included as Exhibit ME-3. The downturn is not isolated to PRECorp, but the immense energy reserves in the Powder River Basin, the heart of PRECorp's five-county, 16,200 square mile service territory, place PRECorp at ground zero for these impacts.

Q. What does PRECorp need to do to manage effectively through this these impacts and the current downturn?

A. The impacts of this bust cycle, or downturn, have been exacerbated by the combination of low natural gas prices, low oil prices, and a shrinking demand for Wyoming coal.

There are three main things that we need to do in order to manage effectively through this downturn. First, we must reduce the chance of revenue loss due to nonpayment of monthly electric bills. Then, we must ensure that PRECorp remains financially healthy and is able to maintain appropriate service levels to our member owners. Finally, PRECorp must step back and look at the bigger picture to assess the entire landscape of risk and then develop a portfolio of risk management strategies and related initiatives to manage through this bust cycle.

This application is focused on ensuring that PRECorp remains financially healthy by increasing revenues in order to address a revenue shortfall. In late 2015, PRECorp was able to secure Commission authority through revisions to our Security Deposit tariff, thus reducing the chance of revenue loss due to nonpayment of monthly electric bills. During 2016 we will be working on a risk management assessment that we anticipate will include the development of various initiatives to manage the risks that we identify through this process.

Q. Would you explain the major events that occurred in 2015 relating to the downturn you are describing?

A. It is important to recognize that PRECorp's service area includes the vast majority of coal lands within Wyoming, including the Powder River Basin. Therefore, any decline in coal or coal bed methane production has a direct impact on PRECorp's revenues. In 2015 we experienced four significant events. A CBM Company named Storm Cat Energy ceased operations and left the system without paying a $1.1 million power bill. Alpha Natural Resources, a coal mining company, declared Chapter 11 Bankruptcy and left PRECorp with $560,000 in pre-petition debt.

Additionally, in 2015 two major players, Anadarko and Williams divested their CBM assets to a new entity called Carbon Creek. Carbon Creek now owns and operates 703 CBM wells and represents approximately 43% of sales to the CBM class. Carbon Creek has yet to establish acceptable credit with PRECorp and is operating with a very large security deposit in place.

In December of 2015, Arch Coal, one of the largest mining operators in the PRB, missed a debt service payment and entered a 30-day period in which to cure the default. On January 11, 2016 Arch filed for bankruptcy relief under Chapter 11.

The impacts of these events are not directly addressed in the cost of service filing, but they certainly are helpful in understanding the stress the energy industry is experiencing and how those stresses can impact PRECorp's routine operations.

Q. Please describe how PRECorp has attempted to manage through these challenges.

A. During the beginning of the CBM boom PRECorp was focused on managing risk related to stranded investment and the ultimate retirement of the CBM facilities that would no longer be considered used and useful. During the middle portion of the growth cycle we were focused on limiting our member investment in facilities dedicated to serving CBM loads. As we began to see the end of the CBM buildout we started to focus on ensuring proper alignment between our human resources and work load. We began shedding our contract labor forces and began the process to make sure our in-house labor forces were properly aligned for the work ahead of us. We refocused on system maintenance as much of that was deferred during the boom years due to resource limitations.

We expected the CBM decline to be a more linear curve. However, in reality, it has been non-linear, disruptive and hard to predict. We did not anticipate the multiple and compounding impacts that we would see related to the low natural gas prices, the low global oil price and the regulatory uncertainty created by the build up and approval of the EPA's Clean Power Plan. This has manifested itself in business failure, bankruptcy, and an ongoing, and increasingly negative impact to our state and local economy.

The implementation of PRECorp's CBM retirement fund, our CBM risk management fund, the use of accelerated depreciation, the line share process for our line extension policy, and our Revenue Deferral Plan have all been very helpful in managing risks. Additionally, in late 2015 PRECorp was able to revise its Security Deposit regulations in order to be better positioned to require deposits from existing members who may be experiencing financial difficulties, but still managing to pay monthly power bills on time as was the case in the recent coal mine bankruptcies.

Q. Has the Cooperative been able to reduce costs?

A. PRECorp's efforts in anticipating the decline of the CBM sales resulted in the implementation of various initiatives to increase productivity and reduce costs for several years. PRECorp has decreased employee headcount through attrition in the last several years. Staffing levels reached a high of 177 full and part-time employees in 2009 as the CBM exploration and extraction reached a peak. As of June 2013, the total was 157, and as of November 2015 is 149. We also maintain an employee program where employees are encouraged to propose revenue enhancement and expense reduction ideas for the cooperative to implement. PRECorp tracks the impacts of these initiatives each year and since 2010 the PRECorp team has delivered $5,728,181.84 in value to the members through cost savings and revenue enhancements; see Exhibit ME-4.

Q. Are there increased labor and benefit costs in the adjusted test year used to determine cost of service?

A. Labor costs have been increased 3% as of October 2015 to reflect increases needed to keep PRECorp's compensation plan competitive with other cooperatives on a national benchmark for our non-union employees and to comply with terms negotiated in our union contract.

Wages and benefits are a significant portion of PRECorp's operational costs and the Board is actively engaged in reviewing the size of the work force and its wage and benefit levels. We have focused on using normal attrition to keep our workforce aligned with our desired service levels and required activities, and we continued to shift a higher percentage of healthcare costs to the employees.

In 2015 the average increase in health care premium cost to the employee was offset by the wage increase. While the cost to the company was almost neutral, the higher premiums for the employees are designed to reduce overall usage and ultimately overall premium costs to both the employer and the employee.

David Hedrick will provide additional details of increased operational costs included in the Cost of Service Study.

Q. Please expand upon the Revenue Deferral Plan mentioned previously as being helpful in managing risks.

A. In 2009, the Cooperative put into place a Revenue Deferral Plan, with approval from RUS to manage the risks related to unforeseen and extraordinary expenses related to the 2008 Economic Crisis and its impact on the capitalization of retirement plan PRECorp participates in. At that time there was real risk of PRECorp, and other cooperatives, being required to make a Deficit Reduction Contribution to provide additional capital into the RUS plan to make up for losses. As the risk abated, PRECorp realized the value of the Revenue Deferral Plan as a means to help stabilize end of year financials and associated revenues without placing any addition burden on members.

This Revenue Deferral Plan was part of the last two general rate filings PRECorp made in 2010 (Docket No. 10014-118-CR-10) and 2013 (Docket No. 10014-145-CR-13), and was created to provide a degree of planning flexibility and a cushion against unexpected revenue and expense impacts. The current balance of the Revenue Deferral Plan is $7.22 million, though we anticipate that we will utilize an amount as necessary in our 2015 final financial results in order to meet our minimum RUS OTIER requirement. Exhibit ME-5 includes copies of the current Revenue Deferral Plan, the Board resolution adopting the plan, and the RUS approval letter. A new Plan will be developed after the results of 2015 are known and an amount of deferred revenue is applied from the Plan.

Q. Do the proposed rates reflect the utilization of revenue from the Deferred Revenue Plan?

A. The 2015 operating budget was projected to utilize $2,350,000 of revenues from the Plan in order to produce a positive operating margin that meets the Cooperative's financial ratio requirements. However, the Board determined that this rate case should develop sufficient revenues without the use of the Revenue Deferral Plan to produce adequate margins and RUS OTIER results in the future to fully support PRECorp's financial stability without the use of revenue deferral. Any remaining amount of revenue in the Plan would then continue to be available for unexpected or one time events that impact the Cooperative and ultimately its financial ratios.

Q. With respect to the CBM Line Extension Policy, please explain what other policies and procedures were adopted to reduce the Cooperative's exposure to capital investment risks.

A. The previous version of our CBM Line Extension Policy, applicable to our CBM customers, included a three (3) mill per kWh surcharge which created a Cost of Retirement Fund to pay for the eventual retirement of infrastructure built solely to serve CBM customers. This fund protected the rest of the membership from bearing the significant cost to retire plant built for the benefit of one group of customers. In the revised CBM Line Extension Policy, effective June 2009, the three (3) mill surcharge was suspended and a five (5) mill surcharge instituted. The five (5) mill surcharge funded the construction of substations, transmission lines and system improvements necessary to serve the CBM customer class, not specific line extensions. Through the five (5) mill surcharge, CBM customers provided funding necessary to build plant which only benefits the class, and further relieves the other rate classes of some of the risks inherent in serving the CBM industry. Individual CBM customers still provided the capital to build line extensions to provide power to their well locations. The 5 mill surcharge was ended in September 2012, in response to the fact that the industry was no longer asking for new loads and additional capital investment. The surcharge financed $18,221,268 of capital infrastructure before it ended.

Q. Can you elaborate on the CBM Risk Management Fund?

A. In some past years, PRECorp has received bill credits from Basin Electric Power Cooperative. PRECorp handled these credits, when available, in different ways. In one year, the entire amount of the credit was retained and added additional operating margins. On other occasions the credit was extended to the membership through bill credits or checks. In 2007, PRECorp received a credit of$4,769,945.32 from Basin. The credit was allocated to the customer classes, and the amount allocated to the CBM classes, $1,596,284.02, was retained and used to establish the CBM Risk Management Fund, while the remainder was distributed to the non-CBM rate classes. The Risk Management Fund is intended to offset any stranded investment the Cooperative might have related to the CBM industry. In 2008, PRECorp again received a credit from Basin of $4,879,178.97, which was treated the same way, as a refund to the non-CBM classes and as an addition to the CBM Risk Management Fund in the amount of $2,030,098.40. The last addition to the CBM Risk Management Fund of $2,788,751.37 was made in 2009, from a total Basin credit of $8,446,198.25. The CBM Risk Management funds earns interest, which is accrued to the benefit of the fund, and the total value of the fund was over $6.6 million as of November 30, 2015.

Q. Are the year to date operating results consistent with the projected results in the 2015 operating budget?

A. Projected PRECorp year to date sales and expenses through the end of 2015 are all under budget. The 2015 Budget projected a decline in total sales as of 2015 year end of approximately 0.2% system wide. The year to date actual and project December 2015 decline for the system is 4.2%. The combined CBM rate classes are projected to be down by 11.2%, against a 2015 budgeted decrease of 11.6%. The LPT-Coal class sales were budgeted to have declined 0.6% through year end, and in fact are down 4.2%. The energy industry continues to face significant economic and political headwinds. For example, one member of the LPT-Coal class declared bankruptcy this summer, and has a prepetition debt of $560,000 outstanding. The CBM classes were singularly impacted this year by the disconnection of 488 services in the LP-CBM and GS-CBM classes, all held by one member, which was accompanied by an uncollected account balance of almost $1.1 million. The loss of the sales related to those 488 services certainly will continue to impact the actual to budget performance of the CBM rate classes through year end. PRECorp is and will continue to monitor its total sales in relation to its actual sales as this rate case progresses, and is prepared to amend its filing as the sales data develops for the entirety of 2015.

Q. Why does PRECorp propose to rebase its rates and reset its COPA at this time?

A. The Cooperative uses the COPA to pass through changes in PRECorp's wholesale power costs to its customers. The COPA amount expected for 2016 is $11,308,464. The COPA derives revenues to offset power costs through a per kWh rate adder. Members who have a higher than average load factor in a class may pay a percentage of the wholesale power cost increases when both demand and energy cost increases are collected on the basis of kWh sales. Rebasing the rates and zeroing out the COPA factor is a way to keep members' rates closer to cost of service. The Board therefore decided it would be appropriate to reset our COPA to zero and rebase our base rates to reflect Basin's 2016 wholesale rates.

Q. Were any specific Commission directives taken into account when developing this rate case?

In the Commission's Order in Docket No. 10014-82-CR-05, issued July 17, 2006, PRECorp was directed to "develop a plan to bring all customers to cost of service, particularly seasonal and irrigation customers." The rate case contemplates an increase for the irrigation class that is consistent with this directive. In addition to that directive, in the Commission's order in Docket No. 10014-145-CR-13, issued June 19, 2014, the Commissioners stated that the Cooperative was expected to propose more movement between customer charges, demand charges and energy charges. The distribution of the recovery of costs between these charges was a substantial topic during the proceedings of that docket. This filing continues to adjust those charges consistent with Commission guidance and is more fully explained by David Hedrick.

Additionally, the LPT General filing to create the LPT General Rate was docket number 100012-156-CT-14 and the order stated "PRECorp is directed to file its cost of service studies upon completion, whether or not the Cooperative files a general rate case." This filing also addresses that order with the filing of the cost of service study.

Q. Does Mr. Hedrick provide a detailed examination of the rate design used to move the rates of return of the customer classes toward cost of service, in addition to describing changes to basic charges, horsepower charges for the irrigation rate and other changes?

A. Yes.

Q. Has this filing been approved by PRECorp's Board of Directors?

A. Yes, the Board approved the rate filing on November 17, 2015.

Q. When does PRECorp request the rates proposed in this filing become effective?

A. PRECorp is requesting the rates proposed in this filing be approved and placed into effect for all customer billing dates no later than January 10, 2017.

Q. Does this conclude your testimony?

A. Yes, it does.