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Via Electronic Filing

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Public Utility Commission of Oregon
PO Box 2148
Salem, OR 97308-2148

RE: PacifiCorp's Response to Initial Staff Analysis
Docket Nos. UM 1256, UM 1257 and UM 1259

Enclosed for filing are the original and five copies of PacifiCorp's Response to Initial Staff Analysis in the above-referenced matters. A copy of this filing was served on all parties to these proceedings as indicated on the attached certificate of service.

Sincerely,

/s/ Natalie L. Hocken

Natalie L. Hocken

Enclosure

cc: Service Lists for UM 1256, UM 1257 and UM 1259

CERTIFICATE OF SERVICE

I certify that I have on July 10, 2006 served the foregoing document in Docket Nos. UM 1256, 1257 and 1259 upon all parties of record in this proceeding by mailing a copy with first class postage prepaid, unless paper service is waived, and by electronic mail to the following person(s) at his or her last-known address(es) as indicated below and via email to said person(s) email address as indicated below:

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/s/ Natalie L. Hocken
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1 reasonable and should be included in PacifiCorp’s test year revenue requirement). Apart
2 from the ongoing expenses associated with RTO development, PacifiCorp previously made
3 loans to Grid West, which are recorded as a long-term receivable in the balance sheet. These
4 loans were made pursuant to a Funding Agreement among the RTO participants, effective as
5 of January 1, 2001, which contained the following repayment terms:

6 “Funds provided by [Transmission Owners] other than BPA shall
7 be loaned amounts that shall be repaid with interest by RTO West
8 to the [Transmission Owners] promptly when third party financing
9 is available to RTO West, but in any event, not later than the
10 commencement of transmission services by RTO West as an RTO
11 over the transmission assets of one or more [Transmission
12 Owners].”

13 *Funding Agreement, Section 1.1.* These loans, which are the subject of this deferral request,
14 are not reflected in PacifiCorp’s on-going RTO expense levels.

15 PacifiCorp provided initial funding for development of RTO West, the predecessor to
16 Grid West, in June of 2000. From that date to the present, PacifiCorp has loaned a total of
17 \$2.7 million to Grid West, including accrued interest. All other regional utilities involved in
18 the formation of Grid West have made similar loans to the organization. Grid West planned
19 to repay the loans through surcharges to customers once it became operational. When it
20 became apparent that Grid West was unlikely to function in a manner that would permit it to
21 repay PacifiCorp’s loan, PacifiCorp concluded that it could not continue to carry the Grid
22 West receivable on its books without the establishment of a reserve for the amount
23 uncollectible. The change in PacifiCorp’s accounting treatment of this loan – by establishing
24 a reserve for the uncollectible debt – was made concurrently with the filing of the
25 Application for deferred accounting in Docket UM 1257. PacifiCorp estimates that the total
26 amount of the deferred account would be approximately \$765,000, Oregon’s portion of
PacifiCorp’s \$2.7 million loan.

1 **Procedural Background**

2 PacifiCorp filed an Application on March 23, 2006 in accordance with ORS 757.259
3 and OAR 860-027-0300 for an order authorizing the Company to defer the costs of loans
4 made to Grid West. By its Application, PacifiCorp proposed to defer these loan costs as of
5 the date of the Application for later recovery in rates. ORS 757.259(2)(e) allows the deferral
6 of utility expenses or revenues where necessary to minimize the frequency of rate changes or
7 the fluctuation of rate levels or to match appropriately the costs borne by and benefits
8 received by ratepayers.

9 PacifiCorp proposes to account for these costs in the following manner: Amounts
10 currently recorded as a loan to Grid West will be transferred from Account 124, Other
11 Investments, to Account 182.3, Other Regulatory Assets. The amortization of the balance
12 would be accomplished by crediting Account 182.3 and debiting Account 560, Transmission
13 Operation Supervision and Engineering, coincident with inclusion of the amortization
14 expense in rates. PacifiCorp requested that, in accordance with ORS 757.259(3), it be
15 allowed to accrue interest on the unamortized balance at a rate equal to its weighted average
16 cost of capital most recently approved by the Commission in Docket UE 170. PacifiCorp did
17 not request a determination of ratemaking treatment of the Grid West loan costs in this
18 proceeding, but proposed to address amortization of these costs in PacifiCorp’s pending
19 Oregon rate case, Docket UE 179.

20 Similar applications seeking authorization to defer Grid West loans were filed by
21 Portland General Electric Company on March 21, 2006 and by Idaho Power Company on
22 April 4, 2006. Following interventions by Citizens’ Utility Board (“CUB”) and Industrial
23 Customers of Northwest Utilities (“ICNU”) in these dockets, Chief Administrative Law
24 Judge Michael Grant convened a conference on May 24, 2006. Pursuant to Judge Grant’s
25
26

1 Conference Memorandum, Staff filed the “Initial Staff Analysis” of the issues on June 16,
2 2006.

3 **Comments**

4 **A. PacifiCorp Concurs with the Finding in the Initial Staff Analysis That the Loan**
5 **Amounts Are Eligible for Deferral Inasmuch as the Resulting Expense Was**
6 **Incurred After the Date of the Application.**

7 An issue identified during the parties’ May 24, 2006 conference is whether the
8 utilities “seek to defer expenses incurred prior to the date of the application” (*Issue 1,*
9 *Conference Memorandum at 1*), which arguably would be barred as retroactive ratemaking.
10 ICNU had argued in its May 8, 2006 letter to the Commission that the utilities were engaging
11 in “accounting gimmicks,” and that the Commission “cannot permit the deferral of past
12 expense merely because they have been described as loans.” *Letter from Melinda J. Davison*
13 *to Commissioners, May 8, 2006 at 1*. According to ICNU, “a utility must obtain approval
14 from the Commission *prior* to the date of expending money or collecting revenues that it
15 wishes to include in a deferred account.” *Id. at 1-2 (emphasis added)*.

16 This argument disregards generally accepted accounting principles (“GAAP”), which
17 determine the point at which an expense is “incurred” for accounting purposes. As described
18 above, in contrast to ongoing expenses incurred by PacifiCorp in connection with RTO
19 development – which were recorded as expenses and are being recovered in rates – the loans
20 were recorded on PacifiCorp’s balance sheet as a long-term receivable. The character of the
21 loan amounts changed once it became clear that the loan would not be repaid. Upon the
22 imminent dissolution of Grid West – when it became likely that the loan would not be
23 repaid – PacifiCorp established a reserve for uncollectible debt.¹ Once the loan becomes
24 uncollectible, PacifiCorp will be required under GAAP to write off the cost of the loan, at

25 ¹ On April 11, 2006, the Grid West Board of Directors determined that it should begin
26 the process to dissolve Grid West. *See May 10, 2006 Letter from Chuck Durick, President of*
Grid West, to Current and Former Grid West Funding Utilities at 2.

1 which point the loan amounts become an *expense* item. Thus it is Grid West’s default under
2 the Funding Agreement which triggers the ability to treat the amounts as an expense.
3 Because this event will occur *after* the filing of the Application in these dockets, the expense
4 amounts remain eligible for deferral. In other words, the amounts were incurred as expenses
5 for accounting purposes *after* the filing of the Application.

6 The Initial Staff Analysis reaches the same conclusion on this point; it states:

7 “The loans will become an expense when the Generally Accepted
8 Accounting Principles (‘GAAP’) require the respective utilities to
9 write-off the promissory notes as uncollectible debt. As a result,
10 the applications for deferred accounting were filed before the loans
11 became an expense as determined by GAAP.”

12 *Initial Staff Analysis at 2.* Given this sequence of events, deferral of the requested amounts is
13 not prohibited by the prohibition against retroactive ratemaking. PacifiCorp supports the
14 resolution of this issue in the Initial Staff Analysis.

15 ICNU also argued that allowing the utilities to defer these “past costs” would create a
16 “huge loophole,” as “there would be no reason why any disputed cost could not be disguised
17 as a loan in order to allow a future deferral.” *Letter from Melinda J. Davison to*
18 *Commissioners, May 8, 2006 at 2.* This argument is without merit. First, it completely
19 disregards that the funds advanced to Grid West by PacifiCorp were pursuant to the Funding
20 Agreement, which contains a repayment provision under which PacifiCorp expected to be
21 repaid. There was no “disguise” of a cost as a loan; the funds were characterized as a loan at
22 the time they were advanced, pursuant to a Funding Agreement under which the loan would
23 be repaid. No such “loophole” exists for other expense items that would enable a utility to
24 make otherwise ineligible costs eligible for deferral.

25 Second, the Commission has discretion under ORS 757.259 to determine whether to
26 grant a requested deferral. ORS 757.259(2) provides that “the Commission by order *may*
authorize deferral.” (*Emphasis added.*) Claiming that the instant request creates a “huge

1 loophole” suggests that the Commission would not exercise its full discretion under the
2 statute to reject inappropriate deferral requests. The Initial Staff Analysis concurs on this
3 point, noting that “the Commission is not required to approve every application for deferred
4 accounting” but “has substantial discretion to grant or deny these applications based on
5 policy considerations.” *Initial Staff Analysis at 4.*

6 There is thus no legal impediment to the Commission granting authorization for the
7 deferrals in these dockets. As discussed in the next section, the Commission should exercise
8 its discretion to grant the requested deferrals.

9 **B. PacifiCorp Concurs with the Finding in the Initial Staff Analysis that the**
10 **Commission has the Discretion under ORS 757.259 to Grant the Requested**
Deferrals.

11 In its Application, PacifiCorp cited ORS 757.259(2)(e) as authority for granting the
12 requested deferral. ORS 757.259(2) provides in relevant part that:

13 Upon application of a utility . . . the commission by order may
14 authorize deferral of the following amounts for later incorporation
15 in rates:

16 . . .

17 (e) Identifiable utility expenses or revenues, the recovery or
18 refund of which the commission finds should be deferred in order
to minimize the frequency of rate changes or the fluctuation of rate
levels or to match appropriately the costs borne by and benefits
received by ratepayers.

19 The costs for which PacifiCorp seeks deferral meet the requirement of subsection 2(e).

20 The Initial Staff Analysis concludes that the term “identifiable utility expenses” is an
21 “inexact term” under the statutory interpretation regime set forth in *Springfield Education*
22 *Assn. v. School District*, 290 Or. 217, 223, 621 P.2d 547 (1980) (“*Springfield*”). According
23 to *Springfield*, “inexact terms” require “agency interpretation and judicial review for
24 consistency with legislative policy.” *Id.* As stated in the Initial Staff Analysis, an
25 interpretive method of statutory interpretation is used to determine the meaning of inexact
26 terms and phrases. *Initial Staff Analysis at 2, citing Portland General Electric v. Bureau of*

1 *Labor and Industries, 317 Or. 606, 859 P.2d 1143 (1993) (“PGE v. BOLI”).* The Initial
2 Staff Analysis concludes that only the first level of analysis – looking at the text and context
3 of the statute – is necessary to interpret the statute, given that the statute’s text and context
4 “unambiguously disclose the legislature’s intent.” *Initial Staff Analysis at 3.* According to
5 the Analysis, the Commission is empowered to define “identifiable utility expense” using its
6 expertise, along with the “context of the Oregon regulatory scheme.” *Id. at 3.* Applying this
7 approach, the Initial Staff Analysis concludes that the Commission “has the discretion to
8 allow the applications for deferred accounting because the applications were filed before the
9 loans became, or will become, an “identifiable utility expense.” *Id. at 3.*

10 With respect to the types of “identifiable utility expenses” the Commission has
11 authorized in the past, Order No. 05-1070 notes that deferrals have been used “for a variety
12 of reasons,” including to “address costs that are hard to forecast or arise from extraordinary
13 and unanticipated events; implement legislative mandates or unique ratemaking mechanisms;
14 and encourage utility or customer behavior consistent with regulatory policy.” *Docket*
15 *UM 1147, Order No. 05-1070, at 2.* The Initial Staff Analysis states that the expenses at
16 issue in these dockets are appropriately subject to deferral under ORS 757.259(2)(e)
17 “[b]ecause the expenses that are now likely to be incurred were a result of utility behavior
18 consistent with regulatory policy” (presumably the development of regional transmission
19 entities and the pursuit of state policies encouraging competitive electric market
20 development). *Initial Staff Analysis at 4.* The Commission retains the discretion to
21 determine whether or not the utility’s behavior is consistent with regulatory policy by its
22 actions with respect to granting the requested deferral. Given PacifiCorp’s ability to recover
23 RTO-related expenses in rates, it would appear that the Commission has previously been
24 supportive of utilities’ efforts with respect to Grid West and its predecessor entity. The
25 Initial Staff Analysis expresses the view that “the utilities’ participation was consistent with
26 regulatory policy and will benefit customers.” *Id.* Granting the deferral applications would

1 allow these benefits received by customers to be appropriately matched with the costs borne
2 by customers, as required by ORS 757.259(2)(e). *Id.*

3 ICNU previously argued for a more narrow interpretation of ORS 757.259(2)(e),
4 stating that “there is no possible way in which these costs can be matched to a time in which
5 ratepayers will receive any benefits,” given that Grid West is dissolving. *Letter from*
6 *Melinda J. Davison to Commissioners, May 8, 2006 at 3.* This same restrictive interpretation
7 of ORS 757.259(2)(e) was advanced by ICNU in Docket UM 1147, the Commission’s
8 investigation of deferred accounting. In that proceeding, ICNU urged an interpretation of
9 ORS 757.259(2)(e) that would impose a “benefit over time” requirement, *i.e.*, that deferred
10 accounting would be appropriate only if “a utility can demonstrate that the costs it is
11 incurring at present will result in a demonstrable benefit to customers in the future.” *Order*
12 *No. 05-1070 at 4.* This same restrictive interpretation was rejected by the Commission in
13 that proceeding, when the Commission declined to adopt additional standards to determine
14 whether an application meets the requirements of ORS 757.259(2)(e). According to Order
15 No. 05-1070, the Commission will continue to “adhere to the Commission’s past practice,
16 which utilizes a flexible, fact-specific approach that acknowledges the wide range of reasons
17 why deferred accounting might be beneficial to customers.” *Id.* The Commission should
18 continue to reject the inflexible approach which ICNU reiterates in this proceeding, and grant
19 the requested deferrals.

20 Order No. 05-1070 provides some guidance on the issue of when the Commission
21 should exercise its discretion to grant a deferral. The Order describes the approach as
22 follows:

23 Initially, the proper approach in analyzing an event is to examine
24 the nature of the event, its impact on the utility, the treatment in
25 ratemaking, and other factors used to evaluate whether a deferred
26 account is appropriate. The next step is to examine the magnitude
of the underlying event in terms of the potential harm. The type of
event—modeled in rates or not, foreseeable or not—will affect the

1 amount of harm that must be shown by the utility. If the event was
2 modeled or foreseen, without extenuating circumstances, the
3 magnitude of harm must be substantial to warrant the
4 Commission's exercise of discretion in opening a deferred account.
5 If the event was neither modeled nor foreseen, or if extenuating
6 circumstances were not foreseen, then the magnitude of harm that
7 would justify deferral likely would be lower.

8 *Docket UM 1147, Order No. 05-1070 at 7.* Applying this approach to the requested deferrals
9 at issue in these dockets suggests that they should be granted. The default by Grid West of
10 its obligation to repay the loans was neither modeled nor foreseen. Moreover, ratemaking
11 treatment provided no means for recovery of these costs; in contrast to the ongoing expenses
12 associated with RTO formation that were recoverable in rates, the loan amounts were carried
13 as a receivable on the balance sheet and were intended to be repaid at some time in the
14 future. Denial of deferred accounting for the loan amounts would effectively deny the ability
15 of PacifiCorp to recover these amounts.

16 The Commission should exercise its discretion under ORS 757.259(2)(e) to grant the
17 requested deferrals. Such treatment would be consistent with Commission precedent, which
18 has granted deferrals where appropriate to encourage utility behavior consistent with
19 regulatory policy. *Docket UM 1147, Order No. 05-1070, at 2.* Because deferral would
20 permit the costs to be matched with the benefits arising from the expenditures, the
21 requirements of ORS 757.259(2)(e) are satisfied. In addition, such treatment would be
22 consistent with the standards enunciated by the Commission in its Order No. 05-1070 for
23 exercising its discretion to grant a deferral, as the event leading to the cost was unforeseen
24 and traditional ratemaking treatment fails to provide an adequate means of recovering the
25 costs.

26 **Conclusion**

PacifiCorp respectfully requests that in accordance with ORS 757.259, the
Commission authorize the Company to defer, commencing as of the date of the Application

1 (March 23, 2006), the Grid West loan costs incurred by the Company as described in the
2 Application. PacifiCorp proposes that the amortization in rates of authorized deferrals will
3 be determined in its pending general rate proceeding, Docket UE 179.
4

5 DATED: July 10, 2006.

6 **PACIFICORP**

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8 */s/ Natalie L. Hocken*

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