

Davison Van Cleve PC

TEL (503) 241-7242 • FAX (503) 241-8160 • mail@dvclaw.com

Suite 2460
1000 SW Broadway
Portland, OR 97205

January 18, 2005

Via Facsimile and US Mail

Carol Hulse
Administrative Specialist
Oregon Public Utilities Commission
PO Box 2148
Salem, OR 97308-2148

Re: In the Matter of the PUBLIC UTILITY COMMISSION OF OREGON
Staff Request to Open an Investigation Related to Deferred Accounting
Docket No. UM 1147

Dear Ms. Hulse:

Enclosed please find the original and one copy of the Opening Comments of the Industrial Customers of Northwest Utilities in the above-captioned docket.

Please return one file-stamped copy of the document in the self-addressed, stamped envelope provided. Please call me at (503) 241-7242 if you have any questions. Thank you for your assistance.

Sincerely yours,



Ally L. Smith

Enclosures

cc: Service List

**BEFORE THE PUBLIC UTILITY COMMISSION
OF OREGON**

UM 1147

In the Matter of)	
)	
PUBLIC UTILITY COMMISSION OF)	OPENING COMMENTS OF THE
OREGON)	INDUSTRIAL CUSTOMERS OF
)	NORTHWEST UTILITIES
Staff Request to Open an Investigation)	
Related to Deferred Accounting.)	
_____)	

INTRODUCTION

Pursuant to the status conference memorandum issued in Public Utility Commission of Oregon (“OPUC” or the “Commission”) Docket No. UM 1147 on November 5, 2004, the Industrial Customers of Northwest Utilities (“ICNU”) submits the following Opening Comments regarding the OPUC’s investigation into its deferred accounting policies and practices under ORS § 757.259. Deferred accounting provides a limited exception to the rule that a utility bears the risks and reaps the rewards of cost fluctuations between rate cases. The Oregon Attorney General has found that deferred accounting would be unlawful in Oregon in the absence of specific statutory authorization because the practice would violate the rule against retroactive ratemaking. As such, the Commission should establish policies for deferred accounting that authorize the practice in only the limited circumstances contemplated in the deferred accounting statute. ICNU and its members believe that, in recent years, deferred accounting has been greatly overused in ways that far exceed the intent of the legislature. ICNU urges the Commission to adopt the following policies as part of the investigation in this Docket:

1. The Commission should limit approval of applications for deferred accounting of costs pursuant to ORS § 757.259(2)(e) to discrete expenses incurred under extraordinary and unanticipated circumstances. ICNU supports adoption of policies and revision of the OPUC administrative rules to limit deferred accounting in this manner.
2. The Commission should limit deferred accounts to the cost causing factors associated with the original application. This will help to prevent the use of deferred accounting as a general cost-recovery mechanism.
3. The Commission should adopt a policy of applying the cost of short-term debt to deferred account balances.
4. The Commission should make findings that recognize the asymmetry of risks and benefits of deferred accounting for utilities and customers. The majority of deferred accounting applications are filed to recover utility costs. Any policies adopted in this proceeding should reflect the asymmetry in the use of deferred accounting.
5. The Commission should adopt a cap on the overall amount of costs that the utility can defer in one year to prevent a deferred account balance from “ballooning” beyond the scope of the initial authorization.

The Commission’s deferred accounting policies and practices should recognize that deferred accounting was not intended to be a means for general cost recovery for utilities between rate cases. ICNU supports the Commission making findings as a matter of policy regarding these matters. ICNU also supports revisions to the Commission’s rules through a rulemaking to recognize these findings.

DISCUSSION

The status conference memorandum identified the substantive issues to be addressed by the parties in opening comments. ICNU addresses those issues in Section B of these Opening Comments. Section A provides a discussion of the history of the deferred accounting statute and how deferred accounting fits into the Commission’s overall ratemaking

authority. This discussion helps to frame the context for the Commission's consideration of its deferred accounting policies and practices.

A. Ratemaking Principles Supporting Deferred Accounting

In addressing deferred accounting policies and practices in this Docket, the Commission must consider the role that deferred accounting plays in Commission ratemaking. The Commission is charged with setting rates at a fair, just, and reasonable level and balancing the interests of the utility and the customer in doing so. ORS §§ 756.040, 757.210. Rates are set in a general rate case, in which the Commission forecasts the utility's costs for the next year and then normalizes that amount to reflect non-recurring items and known changes. American Can Co. v. Lobdell, 55 Or. App. 451, 454, 638 P.2d 1152, 1154 (1982). In this forecast, the Commission includes costs incurred to provide service and excludes costs that should be the responsibility of the utility rather than customers. Id.

The Commission sets rates on a prospective basis. See Re US West Communications, OPUC Docket No. UT 135, Order No. 97-180 (May 22, 1997). Once new rates go into effect, “[u]tilities typically bear the risk for changes in normal operating expenses between rate cases.” Re PacifiCorp, OPUC Docket Nos. UM 995/UE 121/UC 578, Order No. 01-420 at 4 (May 11, 2001). If utility costs or revenues increase between rate cases, the rule against retroactive ratemaking prevents the Commission from adjusting future rates to reflect those past costs or revenues. Re US West Communications, OPUC Docket No. UT 135, Order No. 97-180 (May 22, 1997). Retroactive ratemaking generally is prohibited in Oregon, and the rule against retroactive ratemaking prevents changing rates to include past profits or losses into future rates. Or. Op. Att’y Gen. No. Op-6076 at 2, 8 (Mar. 18, 1987). This rule allows utilities

to retain excess revenues if costs decrease or revenues increase between rate cases, but also forces those companies to bear the burden of increased costs or lower revenues between rate cases. Id. at 3.

Oregon is one of a few states that have adopted a statute that specifically provides for deferred accounting. The history of ORS § 757.259 reveals that the statute serves a basic and limited purpose. Specifically, without this statutory authorization, deferred accounting would be illegal in Oregon. Thus, the Commission should view deferred accounting as a ratemaking mechanism to be used only within the purview of the statute.

The legislature passed the deferred accounting statute in 1987, following the issuance of an Oregon Attorney General opinion that concluded that, without specific statutory authorization, deferred accounting constituted retroactive ratemaking and was prohibited in Oregon. Or. Att’y Gen. Op. No. 6076 (Mar. 18, 1987); Or. Laws Ch. 563, § 2 (1987). This opinion was issued at the request of Oregon Public Utility Commissioner Charles Davis, who was concerned about the validity of OPUC orders in which the Commission authorized collection of utility costs in a balancing account for later inclusion in rates. Or. Att’y Gen. Op. No. 6076 at 1 (Mar. 18, 1987). The Attorney General concluded that this practice was improper. Id. at 17.

ORS § 757.259(2) allows the Commission to authorize deferred accounting for the specific types of costs enumerated in subsections (a)-(d) as well as the more general category

of costs and revenues described in subsection (e).^{1/} The nature and type of costs for which the Commission may authorize deferred accounting pursuant to ORS § 757.259(2)(e) has been the subject of considerable dispute in recent years. ORS § 757.259(2)(e) provides that the Commission may authorize deferred accounting for “[i]dentifiable utility expenses or revenues, the recovery or 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.”

The Commission should adopt a policy or rule that limits deferred accounting under ORS § 757.259(2)(e) to small-scale, discrete costs incurred under extraordinary circumstances. Such a policy would be consistent with the legislative history of the deferred accounting statute. Representative Ron Eachus, who later became the Chairman of the Commission, stated during hearings on ORS § 757.259 that the purpose of the statute was to limit deferred accounting to “make sure it was applied in out-of-the-ordinary circumstances, applied on a temporary basis and applied where generally small amounts are in effect.”^{2/}

^{1/} The specific costs or revenues enumerated in subsections (a)-(d) of ORS § 757.259(2) include: (a) amounts resulting from changes in the wholesale price of natural gas or electricity approved by the Federal Energy Regulatory Commission; (b) balances resulting from administration of section 5(c) of the Northwest Electric Power Planning and Conservation Act of 1980; (c) costs arising from any purchase from BPA pursuant to ORS § 757.663; and (d) amounts accruing under a plan for protection of short-term earnings under ORS § 757.262(2).

^{2/} There is disagreement among certain stakeholders in this proceeding regarding whether the legislative history of ORS § 757.259 reflects an intent that deferred accounting be limited to extraordinary and unanticipated costs. Certain testimony in the legislative history indicates that the bill that was enacted as ORS § 757.259 did not limit the use of deferred accounting to “unanticipated” events. See OPUC Docket No. UM 1147, Opening Comments of PGE, Exhibit 1 at 6 (Oct. 7, 2004). It is ICNU’s position that the costs eligible for deferred accounting under ORS § 757.259(2)(e) were intended to be limited to those incurred in extraordinary and unanticipated circumstances between rate cases. The types of costs listed in subsection (a)-(d) of ORS § 757.259(2), however, may not necessarily be unanticipated. This may provide some explanation for the statements in the legislative history that deferred accounting was not to be limited to unanticipated events.

Minutes, Senate Committee on Business, Housing, and Finance at 11 (May 21, 1987) (remarks of Rep. Ron Eachus).

In addition, such a policy would be consistent with the Commission's own analysis of its deferred accounting authority. For example, in Docket No. UE 115, the Commission stated:

ORS 757.259 allows this Commission to authorize the deferral of certain expenses for later incorporation in rates. We have previously construed that statute narrowly, and limited its application to the recovery of discrete expenses that might affect a utility's earnings on a short-term basis. The statute cannot be used to authorize the deferral of general expenditures that a utility incurs in an ongoing and continuous manner.

Re PGE, OPUC Docket No. UE 115, Order No. 01-988 at 8 (Nov. 20, 2001) (internal citations omitted). In Docket No. UE 76, the Commission found that “[f]or the most part, deferrals under [ORS § 757.259(2)(e) are] to be of discrete items which might substantially affect a utility’s earnings on a short term basis.” Re PacifiCorp, OPUC Docket No. UE 76, Order No. 92-1128 at 8 (Aug. 4, 1992). More recently, in Docket No. UM 1071, the Commission found that the circumstances underlying Portland General Electric’s (“PGE”) request to defer hydro replacement costs for 2003 was “not extraordinary enough to justify deferred accounting.” Re PGE, OPUC Docket No. UM 1071, Order No. 04-108 at 11 (Mar. 2, 2004) (“Order No. 04-108”). Any policies or rules adopted by the Commission as a result of this investigation should reflect the limitations on deferred accounting that were recognized by the legislature at the time it enacted ORS § 757.259 and by the Commission since that time.

Deferred accounting under ORS § 757.259(2)(e) was not intended for large-scale utility costs that are generally accounted for in rates set in a general rate case. In addition,

deferred accounting was not intended to be used as a tool to improve a utility's earnings between rate cases. Any policy adopted by the Commission in this Docket should reflect that ORS § 757.259(2)(e) should be used for the limited purpose for which it was intended rather than for general cost recovery between rate cases.

B. The Commission Should Adopt a Policy or Rule that Permits Deferred Accounting in Limited Circumstances

The status conference memorandum directs the parties to address certain issues in opening comments. As described above, ICNU urges the Commission to review the parties' comments on these issues and adopt a policy or rule that affirms the Commission's previous statements limiting deferred accounting of costs under ORS § 757.259(2)(e) to discrete expenses incurred in extraordinary and unanticipated circumstances. ICNU's position on the specific issues identified in the memorandum is described below.

1. Should the requirements for a deferral request differ depending on the circumstances underlying the request, e.g. materiality requirements that differ depending on whether the costs at issue are associated with stochastic risk or scenario risk?

This issue generally relates to the framework for addressing deferred accounting requests that the Commission described in denying PGE's application for deferred accounting related to 2003 hydro replacement costs in Docket No. UM 1071. Order No. 04-108 at 8-9. In Order No. 04-108, the Commission described an analysis that it uses as a guide in analyzing deferred accounting applications. Commission Staff recommended in previous comments in this Docket that the Commission adopt this framework as its deferred accounting policy. ICNU agrees with the Commission's findings in Order No. 04-108 and urges the Commission to adopt as a policy not only the framework described in that order but also the underlying findings that

only those costs that are extraordinary in nature are appropriate for deferred accounting under ORS § 757.259(2)(e).

a. Order No. 04-108

In Order No. 04-108, the Commission set forth a framework to evaluate whether it would approve PGE's request to defer hydro replacement costs. Order No. 04-108 at 8-9. The Commission stated that it evaluates an individual deferred accounting application according to whether it: 1) warrants an exercise of the Commission's discretion to consider authorizing deferred accounting; and 2) fits within the criteria in the deferred accounting statute. Order No. 04-108 at 8. The Commission determined that an exercise of its discretion depended on consideration of two interrelated factors: 1) the type of event that caused the request for deferral; and 2) the magnitude of the event's effect. Id.

With respect to the type of event that caused the request for deferral, the Commission examined the nature of the event in terms of "stochastic" and "scenario" risks. Id. Stochastic risks, according to the Commission, are those that are subject to prediction or quantification and may be capable of being modeled in rates. Id. at 8-9. Scenario risks, on the other hand, are not subject to quantification or prediction. Id.

The Commission stated that it would consider the magnitude of the event's effect in terms of the financial impact on the utility. For stochastic risks, the Commission found that the financial impact on the utility must be "substantial." Id. at 9. For scenario risks, the Commission found that the financial impact on the utility must be "material." Id.

The Commission analyzed PGE's application using this framework and denied the Company's request. The Commission found that hydro variability had been included in the

normalization process used to establish PGE's base rates and that the hydro conditions upon which PGE based its request represented a 1 in 4.5 year hydro event. Id. The Commission treated this hydro variability as a "stochastic" risk (as opposed to a "scenario" risk) and found that the cause of PGE's request was "not extraordinary enough to justify deferred accounting." Id. In addition, the Commission found that the financial impact of the hydro conditions on PGE was "not significant enough in this case to warrant a deferral."^{3/} Id.

b. Adoption of the Framework Described in Order No. 04-108

Commission Staff proposed in comments previously submitted in this Docket that the Commission adopt, with some modifications, the framework described in Order No. 04-108 as the OPUC's deferred accounting policy. Commission Staff developed Table 1, depicted below, to depict both the framework described by the Commission and Staff's modifications.

^{3/} The actual financial impact of the hydro conditions on PGE was in dispute at the time the Commission issued Order No. 04-108.

Table 1

Financial Effect	Type of Event		
	Stochastic Risk (1)(2)	Scenario Risk (3)(4)	Commission Approved (5)(6)
Substantial	Deferral Considered (7)	Deferral Considered	Deferral Considered
Material	Deferral Not Considered	Deferral Considered	Deferral Considered
Immaterial	Deferral Not Considered	Deferral Not Considered	Deferral Considered

- (1) Stochastic risk is defined as a risk that can be predicted as part of the normal course of events; it is quantifiable and can be represented by a known statistical distribution (Order No. 04-108).
- (2) Examples of stochastic risk are hydro variability, normal plant outages, employee compensation, and weather.
- (3) Scenario risk is defined as a risk that is not susceptible to prediction and quantification; it is often represented by abrupt changes in business factors or practices (Order No. 04-108).
- (4) Examples of scenario risk are catastrophic plant outages (Trojan), environmental costs, and material unexpected changes to costs.
- (5) These events are either mandated, pursuant to Commission approval, or emerging from a rate case settlement.
- (6) Examples of these events are DSM costs, a PGA, and intervenor funding.
- (7) Event should be extraordinary.

Table 1 creates three categories for deferred accounting requests: 1) requests that relate to an event that represents a stochastic risk; 2) requests that relate to an event that represents a scenario risk; and 3) requests that are mandated, submitted pursuant to Commission approval, or emerge from a rate case settlement. According to Table 1, the Commission would consider deferred accounting applications that represent stochastic or scenario risk according to the magnitude of the financial impact on the utility. This is the analysis applied by the Commission in Order No. 04-108. To these categories, Commission Staff added the

“Commission Approved” column. Deferred accounting applications that fall under this category would be considered regardless of the financial impact on the utility.

ICNU supports a deferred accounting framework that treats applications differently depending on whether the costs at issue are subject to prediction or quantification and capable of being modeled in rates or are the result of some Commission-approval or mandate. The analytical framework described by the Commission in Order No. 04-108 provides a more objective method of evaluating the risks and impacts posed by the event behind a particular deferred accounting application. Categorizing the type of risk that a particular event represents and determining whether that risk was contemplated when rates were established will help to determine whether a particular request for deferred accounting is justified.

The test described in Order No. 04-108 and depicted in Table 1 essentially provides a means to quantify when an event is extraordinary enough to justify deferred accounting. Indeed, the ultimate finding underlying the Commission’s decision in Order No. 04-108 was that the event that precipitated PGE’s application was “not extraordinary enough to justify deferred accounting.” Order No. 04-108 at 11. Given that the Commission has applied this framework in limited circumstances, it is unclear whether it will apply to other types of costs as easily as it did to the hydro replacement costs in UM 1071. As a result, if the Commission intends to adopt the framework in Table 1 as its deferred accounting policy, it should affirm that this policy is based on the premise that only those costs that are extraordinary in nature are appropriate for deferred accounting, regardless of whether they represent a stochastic or scenario risk.

In addition, the Commission should state as its policy that evidentiary support will be necessary to justify authorization to defer costs or revenues and that unjustified applications will be denied at the deferral stage. The test announced in Order No. 04-108 will help to demonstrate such a policy. Certain deferred accounting applications have sought to have the Commission authorize deferral as merely an accounting order and postpone meaningful review until the amortization phase. See Re PGE, OPUC Docket No. UM 1071, Opening Comments of PGE at 6, 9 (Jan. 9, 2004). The Commission should adopt a policy stating that the authority to defer will not be granted on the basis that the Commission merely is issuing an “accounting order” and recovery will be determined at a later time. Authorizing a deferred account has significance beyond different accounting treatment.

First, accumulation of a deferred account balance can create a presumption of recovery. If the Commission grants deferral authority without thorough review, the accumulation of a large deferred account balance can cloud consideration in the recovery phase of whether deferred accounting was appropriate in the first place. Furthermore, accumulation of a large deferral balance can sometimes be used to justify amortization. A utility may argue that it will face financial hardship or a ratings downgrade without recovery of a deferred cost. Washington Utilities and Transportation Commission (“WUTC”) Staff recognized the significance of granting the authorization to defer in testimony in the current Puget Sound Energy rate case:

[Deferred accounts] place the Commission in a ‘no-win’ situation with investors and Wall Street when it does come to disallowances (write-offs). What I mean by that is, if deferral treatment is granted, it creates an implicit expectation by investors, debtors, and Wall Street that the deferred costs are virtually “guaranteed[.]”

Re Puget Sound Energy, WUTC Docket Nos. UE-040641, 040640, Exh. No. 421 at 22:7-11 (Testimony of James M. Russell) (Sept. 23, 2004).

Second, authorization of a deferred account is only the first phase of a deferred accounting request. The Commission still must conduct an earnings test, audit, and prudence review prior to determining recovery. Such process would be unnecessary if unjustified deferred accounting applications are denied at the deferral stage. In addition, an audit and prudence review often proves difficult and administratively burdensome, especially in the case of large deferred account balances. In the prudence review of PacifiCorp's \$259 million deferred excess net power cost balance in UM 995, Staff and intervenors faced a substantial burden in attempting to determine the various cost-causing factors at issue, identify potential areas of imprudence, and provide evidence to demonstrate that imprudence. WUTC Staff recognized in the rate case mentioned above that the burden of proof often shifts to staff to demonstrate imprudence in the case of a deferred account balance: "[Deferred accounting] creates more work through audit responsibility and shifts the burden of proof from the utility to the Commission and its Staff to find the excessive or imprudent dollars in multi-year deferrals versus the utility having to justify a normal level of expenses in a rate case." Id. at 21:18 – 22:3 (Testimony of James M. Russell). For all of these reasons, the Commission should adopt a policy that limits the authorization of deferred accounting under ORS § 757.259(2)(e) and also that encourages thorough scrutiny of an application prior to granting the authority to defer the costs at issue.

2. For what types of deferrals should the Commission apply the concept of a normal risk range? How should it determine the size of the range?

The Commission should apply the concept of the normal risk range in relation to all deferred accounting applications, unless it is obvious that the event that caused the request definitely was not considered at the time the utility's base rates were established. A number of deferred accounting applications have been submitted in recent years to recover from ratepayers costs that exceed the amount of a particular cost included in base rates—so called “excess” costs. See e.g. Re PGE, OPUC Docket UM 1040, PGE Application for Authorization to Defer Certain Advertising Costs (Oct. 1, 2004); Re PGE, OPUC Docket No. UM 1071, PGE Application for Deferral of Hydro Replacement Costs (Feb. 11, 2003). The Commission certainly should consider the normal range of risk in relation to an application to defer excess costs. The level of costs included in base rates is established upon the assumption that the utility will bear the risk and reap the reward of cost fluctuations between rate cases. The Commission grants the utility an authorized return on equity to compensate for that risk. As a result, the Commission should deny applications to defer excess costs that fall within the normal range of risk allocated to the utility between rate cases.

The Commission should determine the size of the normal range of risk on a case-by-case basis. Determining the range of risk associated with a particular utility's rates is a fact-specific decision that will depend on the circumstances surrounding both the cost at issue and the utility's last rate proceeding. Whether the cost at issue falls within the range of risk accepted by the utility should be a matter left to the Commission's discretion. The Commission should not adopt any rigid policy in this proceeding that will limit its flexibility in evaluating the evidence to make such a determination in future fact-specific proceedings.

3. Should deferrals be limited to the costs associated with the cost-causing factors identified in the original application for deferred accounting?

ICNU supports limiting deferrals to the cost causing factors identified in the original application. The deferred accounting statute provides that costs or revenues to be deferred under ORS § 757.259(2)(e) must be “identifiable.” Furthermore, in previous orders the Commission has described the types of costs that are appropriate for deferred accounting as “discrete.”^{4/} Re PacifiCorp, OPUC Docket No. UE 76, Order No. 92-1128 at 8 (Aug. 4, 1992). The references to “discrete” and “identifiable” costs does not indicate that deferred accounts should be authorized to record or recover costs that are unknown or unidentified at the time of the application.

Limiting deferred accounts to the cost causing factors identified in the application will help to prevent a deferred account from shifting into an account that includes costs other than those for which the deferral is authorized. PacifiCorp’s excess net power cost deferred account in Docket No. UM 995 provides an example of a deferred account that changed dramatically in both nature and extent from the time it was filed to the time that the Commission approved amortization. In Docket No. UM 995, PacifiCorp initially filed a request to defer approximately \$63 million in excess power costs related to high wholesale power prices during the western power crisis. Re PacifiCorp, OPUC Docket No. UM 995, Application of PacifiCorp for an Accounting Order Regarding Excess Net Power Costs (Nov. 2, 2000). By the time the Commission authorized PacifiCorp to defer the excess net power costs, it was clear that the

^{4/} The Commission noted in a subsequent order that the term “discrete” is not found specifically in the statute and there was no absolute requirement that only discrete costs are eligible for deferred accounting. Re PacifiCorp, OPUC Docket Nos. UM 995/UE 121/UC 578, Order No. 01-420 at 27-28 (May 11, 2001).

account would include certain excess costs related to the outage at PacifiCorp's Hunter 1 generating facility. When the Commission ultimately authorized PacifiCorp to recover the excess net power costs, the deferred account included \$259 million associated with high wholesale power prices, below-normal hydro conditions, wholesale power sales, and the outage of the Hunter 1 generating plant. This deferred account went far beyond the scope of the costs identified in PacifiCorp's initial application, and the prudence review of such a large and amorphous deferred account proved extremely difficult. The Commission should adopt a policy of limiting deferred accounts to the cost-causing factors identified in the initial application as a means of preventing utilities from recording in those accounts costs for which a deferral has not been explicitly authorized. Otherwise, utilities will file generic deferrals to recover any variations in cost.

The Commission also should adopt a policy or rule that requires utilities to submit a new filing requesting approval related to any cost-causing factor that was not identified in the initial application but that the utility will seek to include in the deferral balance. For example, in Docket No. UM 995, the Hunter outage and below-normal hydro conditions were not cost-causing factors identified in PacifiCorp's initial application. A policy or rule should be put in place that would have required PacifiCorp to request authorization to include the costs associated with these events in the deferral balance. This will ensure that the Commission and customers are aware of the nature and extent of the costs being included in deferred accounts. Adoption of such a rule or policy will help to discourage utilities from filing generic deferred accounting requests in the hope of recovering unknown future cost variations.

4. What interest rate should be applied to a deferral balance?

The Commission should adopt a policy of using the utility's cost of short-term debt as the interest rate to apply to deferral balances. The current practice is to allow utilities to earn interest on a deferral balance at the authorized rate of return, which allows the utility to benefit from the deferral of costs when short-term interest rates are lower than that level. In addition, many deferred accounts are recovered over a relatively short period of time for which a short-term interest rate is more appropriate. Finally, a utility's authorized rate of return includes a return on equity. It is inappropriate to allow equity returns on deferred balances.

5. What should be the filing requirements and process for deferred accounting investigations?

The OPUC rules regarding the processing of deferred accounting applications currently do not establish a definite process for applications to follow. The rules currently provide that, once an application is filed, comments may be submitted within a time period set forth in the notice that must accompany the application. OAR § 860-027-0300(6)(d). That time period may be no less than twenty-five days. *Id.* The applicant then has ten days to submit reply comments, and the rules provide that the Commission will consider the matter at a public meeting. OAR § 860-027-0300(7), (8). Nevertheless, despite this notice and comment process in the rules, the deferred accounting statute also provides that a party may request a hearing on the request. ORS § 757.259(2).

Although ICNU believes that changes could be made to this process to help facilitate the consideration of deferred accounting applications, the difficulty is fashioning changes that provide certainty to the parties involved but retain the flexibility in the current process that allows for addressing different types of deferred accounting requests. As such,

ICNU is not suggesting revisions to the filing process for deferred accounting applications at this time. The current process allows for uncontested applications to be addressed through the notice and comment process, with a decision at a public meeting, but provides a party the opportunity to request a hearing or more extensive process if warranted by the particular application. Once a party requests a hearing, then contested case procedures should apply rather than notice and comment procedures.

Difficulties have emerged in recent deferred accounting dockets when an application has been left pending before the Commission for several months prior to any action being taken. For example, a prehearing conference was not scheduled in response to PGE's application to defer 2003 hydro replacement costs in UM 1071 until eight months after the application was filed. Given that the Commission can authorize a deferred account retroactively back to the date of the application, a long delay in processing a deferred accounting request creates risk and uncertainty for all parties involved. Eliminating extended processing delays will help to minimize this risk and uncertainty in the future.

In addition, PGE argued after Order No. 04-108 was issued in UM 1071 that it was improper for the Commission to consider disputed issues of fact in the deferral authorization phase of a proceeding. Re PGE, OPUC Docket No. UM 1071, PGE's Application for Reconsideration and Rehearing of Order No. 04-108 at 9 (May 3, 2004). The Commission should make clear in this Docket that authorization of a deferred account is a factual matter about which factual findings may be made, especially in relation to contested applications. This acknowledgment, along with specific findings recognizing the nature of costs that are

appropriate for deferred accounting, will help to clarify the issues that need to be resolved in both the initial request for deferral and any request to recover deferred amounts in rates.

6. What are the alternatives to deferred accounting for recovery of excess utility costs or revenues between rate cases?

Examining the alternatives to deferred accounting is outside the scope of this proceeding. Whether an alternative to deferred accounting is appropriate for treatment of a particular cost will depend on the facts in that case.

7. Do the Commission's deferred accounting practices and procedures ensure symmetrical treatment of deferrals for excess utility costs and deferrals for excess utility revenues?

The Commission's deferred accounting policies should recognize the one-sided nature of deferred accounting as it is typically used by the utilities. The allocation of risks with respect to deferred accounting is asymmetrical because the majority of deferred accounting requests relate to utility costs. As described above, utilities typically bear the risks and reap the rewards of cost fluctuations between rate cases. Deferred accounting, however, alters that risk allocation by providing a mechanism for utilities to recover costs that are not included in rates. Although Staff and Intervenors have the ability to file a deferred accounting application to return excess utility revenues to customers, these parties do not have the resources or access to information necessary to determine if and when utility revenues increase due to declining costs, higher loads, or for other reasons. The Commission's current statutes, rules, and policies generally provide symmetrical treatment for deferred accounting of costs and revenues. However, the Commission should recognize as a policy matter that deferred accounting typically works in the utility's favor. In future deferred accounting proceedings, the Commission should

exercise its discretion in light of this policy and limit the deferral of costs by utilities accordingly.

8. Should there be an overall cap on the amount of costs that a utility can defer in one year?

ICNU supports adoption of an overall cap on the amount of costs that a utility can defer in one year. ICNU proposes that the Commission adopt a cap that would limit the deferral of costs in one year to an amount no greater than 6% of the utility's gross revenues for the previous calendar year. The Commission would have the discretion to allow deferrals above this cap in cases in which denial of the application could result in a detriment to public safety, welfare, or continuing electric service. Such a cap would provide an important limit on the use of deferred accounting. In addition, this cap parallels the 6% cap on amortization of costs in ORS § 757.259(8). As described above, deferred accounting was intended to be used in limited circumstances to recover costs related to specific events rather than as a mechanism to achieve general cost recovery between rate cases. Implementation of this cap will help to achieve this intent.

A cap on the amount that a utility could defer in any one year would help to prevent the deferral of large-scale costs that may prove unmanageable to address through the deferred accounting procedures. The difficulty of assessing the prudence of costs that were the result of a variety of diverse cost-causing factors also demonstrates that deferred accounting is not well-suited to address large-scale costs. Implementing a cap on the total amount of costs deferred in one year would help prevent the "ballooning" of a deferral balance beyond a manageable amount and would require utilities to file rate cases when large cost increases occur rather than seeking to recover those costs through deferred accounting. Review in a general rate

case is a more appropriate vehicle to examine large-scale costs of a utility and the impact of such costs on revenue requirement and return on equity. It is also important to allow ratepayers the opportunity to see if any costs are decreasing to offset the impact of a rate increase for a large deferred account.

9. What must an applicant show to demonstrate that a deferral under ORS § 757.259(2)(e) will either (a) minimize the frequency of rate changes or fluctuation of rate levels, or (b) match ratepayer benefits and costs?

As described above, much of the dispute surrounding deferred accounting relates to deferred accounts authorized pursuant to ORS § 757.259(2)(e), which provides that the Commission may authorize deferred accounting for “[i]dentifiable utility expenses or revenues, the recovery or 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.” The meaning of “minimize the frequency of rate changes or fluctuation of rate levels” and “match appropriately the costs borne by and benefits received by ratepayers” has been the subject of controversy in previous deferred accounting proceedings. ICNU suggests that the Commission adopt a policy that the requirement to “minimize the frequency of rate changes or fluctuation of rate levels” demands more than just a statement that the utility would file a general rate case in the absence of deferred accounting. In addition, with respect to the meaning of “match appropriately the costs borne by and benefits received by ratepayers,” ICNU urges the Commission to adopt as its policy the implementation of that phrase that in Docket No. UM 246. These findings are discussed in more detail below.

a. Minimizing the Frequency of Rate Changes or Fluctuation of Rate Levels

Certain deferred accounting applications have attempted to demonstrate that the request will minimize the frequency of rate changes or fluctuation of rate levels on the basis that, without deferred accounting, the utility would file a general rate case to collect the costs at issue. In PGE's request to defer excess hydro costs in UM 1071, for example, PGE stated that "[g]iven the uncertainty about hydro conditions, PGE might have been required to file new rate cases several times during 2003 to track the rate effects of changing hydro and power cost forecasts." Re PGE, OPUC Docket No. UM 1071, Opening Comments of PGE at 7 (Jan. 9, 2004). The Commission should not accept such unsupported statements as a basis to conclude that the requirements of the statute have been met. Utilities should not be permitted to justify authorization of a deferred account merely by asserting that the Commission must authorize the request in order to avoid the threatened rate case.

In UM 995, the Commission found that PacifiCorp's application for deferred accounting could proceed as a matter of law based upon the finding that PacifiCorp could have filed for interim rate relief in lieu of its deferred accounting filing. Re PacifiCorp, OPUC Docket No. UM 995, Order No. 01-085 at 12 (Jan. 9, 2001). For deferred accounting applications filed under ORS § 757.259(2)(e), ICNU urges the Commission to adopt the interim rate relief standard to guide the Commission's consideration of when a deferred accounting application legitimately will minimize the frequency of rate changes or fluctuation of rate levels by avoiding an immediate rate filing. As described above, ORS § 757.259(2)(e) is intended to address deferrals of extraordinary costs incurred in unanticipated circumstances between rate cases. Thus, if a utility seeks deferred accounting authorization in order to avoid filing a full rate case and

requesting immediate interim rate relief, it is reasonable to require the utility to make a showing of the need for interim rate relief for the application to meet the requirement in the statute.

The Commission has described its standard for granting interim rate relief as follows:

Interim rates are appropriate in some instances. Where the utility can show a compelling need for immediate rate relief, interim rate increases will be considered. However, the utility should show severe financial stress or some other such reason to gain approval of a request for interim rates. In such instances, the utility should show that its ability to serve the public at reasonable rates will be jeopardized.

Re PGE, OPUC Docket Nos. UE 47/UE 48, Order No. 87-1017 at 53 (Sept. 30, 1987) (internal citations omitted). If a utility seeks to justify a deferred accounting application on the basis that it will minimize the frequency of rate changes by avoiding an immediate rate filing, the Commission should require a showing of severe financial stress or other event that jeopardizes the utility's ability to serve the public at reasonable rates. This test will help to provide more certainty to the parties to deferred accounting dockets with respect to how the Commission will determine if the application complies with the terms of the statute.^{5/} In addition, making use of the interim rate relief standard will help to discourage attempts to justify deferred accounting applications on the basis of unsupported assertions that a rate filing would have been made in lieu of the deferred accounting application. At the same time, however, this test will not preclude relief for applications that are related to truly unanticipated and extraordinary circumstances for which deferred accounting may be warranted.

^{5/} Whether a deferred accounting application fits within the criteria in the deferred accounting statute is the second prong of the test stated by the Commission in UM 1071. Order No. 04-108 at 8.

b. Match Appropriately the Costs Borne By and Benefits Received By Ratepayers

With respect to the matching of costs and benefits, ICNU urges the Commission to adopt the meaning given to that phrase in Docket No. UM 246, in which the Commission authorized deferred accounting on the basis that the benefits to certain deferred expenses would accrue to future ratepayers. Re PGE, OPUC Docket No. UM 246, Order No. 90-311 at 1 (Mar. 5, 1990). In Docket No. UM 246, PGE requested deferred accounting treatment under the provision that is now ORS § 757.259(2)(e)^{6/} for legal costs associated with litigation concerning a coal supply contract. Id. PGE agreed in that Docket to limit its right to recover any deferred legal expenses from customers to the extent that the company could demonstrate that customers benefited from those costs. Id. The Commission authorized PGE's request in Order No. 90-311, finding:

Since any benefits from the deferred expenses will accrue to future ratepayers, and since the legal expenses associated with such litigation are likely to be substantial, the commission finds that deferral of such expenses is appropriate. PGE should maintain separately the expenses and its calculation of customer benefits so that when it applies to amortize the expense, the Commission will be able to apply the earnings review required by the statute and the further limitation that PGE has agreed upon.

Id. In a subsequent docket, the Commission described the use of deferred accounting in Docket No. UM 246 as a “good example of appropriate use of the matching provision to authorize deferral of added costs.” OPUC Docket No. UE 76, Order No. 92-1128 at 9.

The Commission should recognize its findings in Order No. 90-311 as the appropriate interpretation of when a deferred accounting application will “match appropriately

^{6/} At the time of PGE's application in Docket No. UM 246, this provision was numbered ORS § 757.259(2)(c).

the costs borne by and benefits received by ratepayers.” ORS § 757.259(2)(e). This test provides that deferred accounting is appropriate when a utility can demonstrate that the costs it is incurring at present will result in a demonstrable benefit to customers in the future. In addition, the utility should be permitted to recover costs only to the extent that it demonstrates in the amortization phase that customers actually benefited from those costs. Utilizing this test will ensure not only that costs and benefits are appropriately matched at the time any deferral is authorized but also that customers receive the benefit upon which the authorization was based.

10. What types of costs are eligible for deferred accounting (e.g. do the costs have to be extraordinary, unanticipated, nonrecurring, and/or discrete)?

As described above, ORS § 757.259(2) establishes two general categories of costs or revenues appropriate for deferral: 1) the specific costs or revenues listed in subsections (a)-(d) of ORS § 757.259(2); and 2) the costs described in ORS § 757.259(2)(e), “[i]dentifiable utility expenses or revenues, the recovery or 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.” The costs eligible for deferred accounting under ORS § 757.259(2)(e) should be limited to those that are extraordinary in nature, unanticipated, and discrete. The history of the statute and the Commission’s decisions interpreting and applying the statute reflect the limitations on the costs that can be deferred under this subsection.

In addition, “annual” deferrals for recurring costs should not be approved under the statute. In Docket No. UM 1040, PGE has been granted a deferred account related to excess advertising costs each year since 2001. This recurring deferred account was the result of a stipulation in Docket No. UE 115, which provided for “an annual deferral that continues until

new base rates are established.” Re PGE, OPUC Docket No. UE 115, Order No. 01-777, Appendix B at 7 (Aug. 31, 2001). Such an annual deferral that is automatically approved each year is inappropriate under the deferred accounting statute. If costs are recurring from year to year, the Commission should address those costs in a general rate case. Approving deferred accounting for such costs year after year amounts to an automatic cost recovery mechanism, and deferred accounting was not intended to be used in such a manner. ICNU urges the Commission to revise its rules or make specific findings in this Docket recognizing that costs that are appropriate for deferred accounting are nonrecurring and that “annual” deferrals will not be granted.

The Commission should make these findings or rule revisions regardless of whether it adopts the framework announced in Order No. 04-108. Although that framework may prove workable to address deferred accounting applications in the future, it is largely unproven at this time. The Commission should recognize the appropriate nature of the costs eligible for deferred accounting under ORS § 757.259(2)(e) in order to retain the flexibility necessary to address applications for deferred accounting that may not fit within the test described in Order No. 04-108.

CONCLUSION

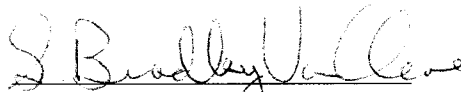
The Commission’s deferred accounting policies and practices should reflect that ORS § 757.259 was intended to provide the Commission with limited authority to make use of a ratemaking mechanism that would otherwise be unlawful in Oregon. ICNU urges the Commission to adopt the policy changes described in these Opening Comments and to identify areas in which these policy decisions can be implemented as revisions to the Commission’s

rules. Such changes will assist in protecting customers from the inclusion in rates of costs that are not appropriately recovered through deferred accounting. ICNU appreciates the Commission's review of this important ratemaking topic and appreciates the opportunity to provide these comments.

Dated this 18th day of January, 2005.

Respectfully submitted,

DAVISON VAN CLEVE, P.C.



S. Bradley Van Cleve

Matthew Perkins

Davison Van Cleve, P.C.

333 SW Taylor, Suite 400

Portland, Oregon 97204

(503) 241-7242 phone

(503) 241-8160 facsimile

mail@dvclaw.com

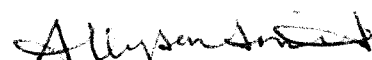
Of Attorneys for Industrial Customers of Northwest
Utilities

CERTIFICATE OF SERVICE

I hereby certify that I have this day served a copy of the foregoing Simultaneous Opening Comments on behalf of the Industrial Customers of Northwest Utilities upon the service list, shown below, by causing the same to be mailed, postage-prepaid, through the U.S. Mail.

DATED this 18th day of January, 2005.

Davison Van Cleve, P.C.


Ally L. Smith

STEPHANIE S ANDRUS DEPARTMENT OF JUSTICE REGULATED UTILITY & BUSINESS SECTION 1162 COURT ST NE SALEM OR 97301-4096 stephanie.andrus@state.or.us	KATHERINE BARNARD CASCADE NATURAL GAS PO BOX 24464 SEATTLE WA 98124 kbarnard@cngc.com
JASON EISDORFER CITIZENS' UTILITY BOARD OF OREGON 610 SW BROADWAY STE 308 PORTLAND OR 97205 jason@oregoncub.org	JAMES F FELL STOEL RIVES LLP 900 SW 5TH AVE STE 2600 PORTLAND OR 97204-1268 jffell@stoel.com
EDWARD A FINKLEA CABLE HUSTON BENEDICT HAAGENSEN & LLOYD LLP 1001 SW 5TH, SUITE 2000 PORTLAND OR 97204 efinklea@chbh.com	PATRICK G HAGER PORTLAND GENERAL ELECTRIC 121 SW SALMON ST 1WTC0702 PORTLAND OR 97204 patrick.hager@pgn.com
JUDY JOHNSON PUBLIC UTILITY COMMISSION PO BOX 2148 SALEM OR 97308-2148 judy.johnson@state.or.us	BARTON L KLINE IDAHO POWER COMPANY PO BOX 70 BOISE ID 83707-0070 bkline@idahopower.com
KATHERINE A MCDOWELL STOEL RIVES LLP 900 SW FIFTH AVE STE 1600 PORTLAND OR 97204-1268 kamcdowell@stoel.com	C. ALEX MILLER NORTHWEST NATURAL 220 NW 2ND AVE PORTLAND OR 97209 c2m@nwnatural.com.