BEFORE THE PUBLIC UTILITY COMMISSION
OF THE STATE OF OREGON

In the Matter of Pacific Power & Light (d/b/a PacifiCorp) Request for a General Rate Increase in the Company's Oregon Annual Revenues	**)** **)** **)** **)** **)**	**Docket No. UE-170**

PRE HEARING BRIEF OF
THE FRED MEYER STORES

Fred Meyer purchases more than 60 million kWh annually in the PacifiCorp distribution territory in Oregon. Fred Meyer takes service from PacifiCorp under rate schedules 28, 48, and 730. Fred Meyer has been an active participant in all facets of this case including settlement negotiations. We have two primary issues which have not yet been resolved.

1. If the jurisdictional net rate increase is 6 percent or less (which is the case in this proceeding), the mitigation cap on net increases for individual rate schedules should be set by a fixed percentage differential of 3 percent, rather than "150 percent of average."

2. The per-kWh subsidy paid to any rate schedule should be subject to a ceiling of 1.5 cents/kWh in order to limit extensive subsidization from other classes and to encourage movement toward cost-of-service rates.

In determining rate spread, it is important to align rates with cost causation, to the greatest extent practicable. Properly aligning rates with the costs caused by each customer class is essential for ensuring fairness, as it minimizes cross subsidies among customers. It also sends proper price signals, which improves efficiency in resource utilization.

The Oregon Administrative Code provides important guidance in this regard, O.A.R. 860-038-0240 requires that rates for any class of consumer must be based on the unbundled costs to serve that class.

At the same time, it can be appropriate to mitigate the impact of moving immediately to cost-based rates for classes that would experience significant rate increases from doing so. This principle of ratemaking is known as "gradualism." When employing this principle, it is important to adopt a long-term strategy of moving in the direction of cost causation, and to avoid schemes that result in permanent cross-subsidies from other customers.

In PacifiCorp's Oregon tariff, rate mitigation is carried out through the Rate Mitigation Adjustment ("RMA"), Schedule 299, pursuant to which certain customer classes receive, and others pay for, inter-class subsidies.

In the UE-147 settlement, the parties agreed to pay subsidies to those customer classes whose cost-based rates would have resulted in a net increase that was greater than 150 percent of the jurisdictional average net increase.

This principle is still valid, but the formula for implementation should be refined in two ways. First, since the jurisdictional net rate increase will be 3 percent or less in this proceeding, the "150 percent of average" cap should be replaced by a fixed percentage differential. This change will better accommodate movement in the direction of cost causation, while still providing significant mitigation. An inflexible "percentage-of-average" cap on a relatively small average net increase does not provide enough opportunity for rates to move *relative to one another* to permit those classes that are paying above-cost rates (via subsidies) to move materially closer to their actual costs-of-service.

In PacifiCorp's initial filing, the Company sought a 12.5 percent base rate increase, which translated into a 6.7 percent net increase. Application of the "150 percent cap" would have meant that no class would receive more than a 10 percent net increase – or about 3.3 percentage points above average. For this magnitude of increase, the 150 percent cap is appropriate.

Now assume that PacifiCorp's revenue requirement is reduced another $26 million below the $31 million reduction reflected in the Partial Stipulation. In such a case, base rates would increase by $45 million over current rates – about 5.5 percent – but the overall *net* rate increase would be *zero*.

Algebraically, capping each class's net increase to 150 percent of system average would mean each individual class would receive an identical net increase of zero, irrespective of any relative movements in their respective costs-of-service. As a practical matter, application of a 150 percent cap in this situation would lock in future subsidy payments for classes that paid subsidies in the immediate past, in order to shield classes paying below-cost rates from incurring any impact greater than the average. This would result in no more toward cost of service.

Because of this unintended consequence of blindly applying the 150% rule, there needs to be a modification in cases where the net rate increase is small. In instances in which the jurisdictional net rate increase is 6 percent or less, the mitigation cap should be set by a fixed percentage differential, rather than a "percentage of average." Specifically, a fixed percentage differential of 3 percent should be used. This differential appropriately balances the tradeoff between gradualism and cost-of-service. Under this proposal, the decision rule for applying the rate mitigation cap would state that in the event that the overall jurisdictional net rate increase was 6 percent or less, the RMA would be applied to ensure that no class would experience a net rate increase greater than 3 percentage points greater than the jurisdictional net rate increase, subject to a maximum subsidy of 1.5 cents per kWh. Adoption of this mechanism would provide substantial rate mitigation, while allowing some meaningful movement of rates toward cost.

Fred Meyer's second issue is that a ceiling should be placed on the per-kWh subsidy paid to any rate schedule at 1.5 cents/kWh, in order to limit extensive subsidization from other classes and to encourage movement toward cost-of-service.

Under this proposal, there is only one rate schedule subject to the 1.5 cents per kWh subsidy ceiling. The subsidy payment to Agricultural Pumping (Schedule 41) reaches 1.5 cents per kWh, and is therefore capped at that level.

Currently, Schedule 41 receives a subsidy payment of 1.926 cents per-kWh, and under PacifiCorp's filed proposal, this subsidy actually would have increased to 2.472 cents per kWh. Under

the Company's proposal, the subsidy would have been paid, primarily, by Schedules 28 and 30 (and their companion Direct Access Schedules 728 and 730) – rate schedules whose generation charges are very similar to those of Schedule 41. In other words, Schedules 28 and 30 would have been called upon to pay a subsidy in excess of 2 cents/kWh to a rate schedule that otherwise paid very similar generation rates as themselves. From a ratemaking perspective, this sort of transfer is fundamentally inequitable. Therefore, a per-kWh ceiling on the magnitude of the subsidy credit is appropriate.

If Schedule 41 is awarded a subsidy of more than 1.5 cents per kWh, then the cost should be socialized. A subsidy of that magnitude would appear to me to be less governed by the principle of gradualism than by a broader social policy of subsidizing certain activities, such as irrigation. If that is the case, the cost for the social policy should be borne by society as a whole. In a ratemaking context, this would mean levying a comparable charge on each rate schedule to fund the subsidy.

Respectfully submitted,

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