



Portland General Electric Company
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PortlandGeneral.com

April 15, 2016

Via electronic filing

Puc.filingcenter@state.or.us

Re: UM 1623 – Application for Deferral Accounting of Excess Pension Costs and Carrying Costs on Cash Contributions.

Attention Filing Center:

Enclosed for filing in Docket UM 1623 please find the **Reply Brief** of Portland General Electric Company.

If you have any questions regarding this filing, please contact me. Thank you for your assistance with this matter.

Sincerely,

A handwritten signature in blue ink, consisting of a large, stylized 'J' followed by a horizontal line and a loop.

JAMES R. BEAN
Legal Assistant

Enclosures

**BEFORE THE PUBLIC UTILITY COMMISSION
OF OREGON**

UM 1623

In the Matter of

PORTLAND GENERAL ELECTRIC
COMPANY

Application for Deferral Accounting of Excess
Pension Costs and Carrying Costs on Cash
Contributions.

REPLY BRIEF OF PORTLAND GENERAL
ELECTRIC COMPANY

I. INTRODUCTION

Pursuant to the procedural schedule set in this docket, Portland General Electric Company (“PGE”) submits this Reply Brief.

PGE’s application and testimony in this matter demonstrate that the excess pension costs at issue were unforeseen, significant, and meet the requirements for deferral. Other parties have made various arguments, some of which are in essence opposition to any deferral. Some of their arguments about this specific deferral attempt to mischaracterize the expense incurred by PGE.

II. BACKGROUND

PGE’s testimony and prior brief set out the background to this deferral application. In short, the application was filed when the combination of new legal requirements and much lower than expected market returns on pension plan investments caused PGE’s FAS 87 pension expense to increase dramatically. The prior rate case had included \$5.1 million for FAS 87 expense. 2012 actual net FAS 87 expense was \$13.2 million, and 2013 net FAS 87 expense was \$18.6 million. This deferral covers less than 4 ½ months of 2012, with excess expense on a prorated basis of \$2.9 million, and all of calendar year 2013, with excess expense of \$13.5 million. PGE has responded to the arguments of the other parties, and will address those included in their opening briefs below. The ultimate question for the Commission is whether a diversion from forecast expenses of this magnitude, in this situation, and caused by legal and market forces out of PGE’s control, meets the requirements for deferral.

III. ARGUMENTS

Oregon Revised Statutes §757.259 states, in part:

(2) Upon application of a utility or ratepayer or upon the commission’s own motion and after public notice, opportunity for comment and a hearing if any party requests a

hearing, the commission by order may authorize deferral of the following amounts for later incorporation in rates:

....

(e) Identifiable 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 explained, in Order 05-1070, that a deferral application may meet either of two tests: that the “proposed deferred account must either minimize the frequency or fluctuations of rate changes or match the costs and benefits received by ratepayers.” Order 05-1070, p.5.

In UM 1147, the Commission also stated:

The Commission will look to whether the event was modeled in rates, and, if so, whether extenuating circumstances were involved that were not foreseeable during the rate case, or whether the event fell within a foreseen range of risk when rates were last set. If the event was not modeled, we will consider whether it was foreseeable as happening in the normal course of events, or not likely to have been capable of forecast. The Commission will examine whether or not the “risks are reasonably predictable and quantifiable.

....

If the event was modeled or foreseen, without extenuating circumstances, the magnitude of harm must be substantial to warrant the Commission’s exercise of discretion in opening a deferred account. If the event was neither modeled nor foreseen, or if extenuating circumstances were not foreseen, then the magnitude of harm that would justify deferral likely would be lower.

Order 05-1070, p. 7.

While parties to this docket have attempted to impose impossible requirements to meet the statutory test that should not be adopted, PGE’s testimony shows that its application meets both of the criteria laid out in Order 05-1070.

Minimize rate changes: Here, Staff and CUB attempt to impose a requirement that would be impossible to meet. In Staff’s testimony, and CUB’s brief, both parties argue that “because

this deferral would result in a rate change that otherwise would not occur without the deferral ... it does not minimize the frequency of rate changes.” Staff/100/p. 6; CUB Opening Brief, p. 4. If that were the criteria, no deferral could ever meet it, since all granted deferrals result in a rate change. PGE is not aware of this unfounded argument being made previously, and it should be dismissed here. ICNU argues that PGE should somehow show it met the requirements for interim rates to meet the criteria. No interim rate filings were made, in part because this deferral had been filed. It should be remembered, however, that PGE’s earnings in 2013 PGE’s were 357 basis points below the level authorized the previous rate case.¹

Matching costs to benefits. In claiming that PGE has not met the matching cost to benefits alternative, CUB makes an argument that is difficult to follow. CUB claims that providing adequate compensation to employees to provide electric service to customers only provides “attenuated and tangential” benefits to customers because “the only ratepayer benefit discussed is supplying service—an act that it [PGE] is required to furnish.” CUB Opening Brief, p. 5. PGE’s fundamental obligation is to provide electric service to customers, and we hope CUB is not arguing that the costs of providing that service should not be recovered, because PGE is required to provide service.

Staff and ICNU make different versions of the argument that the Commission should look past the deferral period, both historically and in the future, to decide if a deferral is appropriate. Their argument itself raises issues of retroactive ratemaking. It also distorts the reality of FAS 87 expense in ratemaking. Both parties claim that over a very long time, FAS 87 expense may balance out. Staff goes so far as to say “it should be expected that actual pension expense will exceed the forecast fifty percent of the time and be less than the forecast the remaining fifty percent of the time.” Staff Opening Brief, p. 4 (citing ICNU testimony). First,

¹ 2013 actual regulated ROE was 6.43% vs. PGE’s authorized ROE of 10%.

that cannot be said with any level of confidence – we don't know what will happen in future ratemaking proceedings, with market performance, or legal changes. Second, even if future forecasts turn out that way, that does not address the dollar impact of the diversions from the projections. And third, this argument attempts to ignore the reality that during 2012 and 2013 PGE incurred \$16.4 million dollars in actual FAS 87 expense above and beyond the level set in rates. That is five standard deviations away from the projected amount and several times higher than the highest FAS 87 expense PGE had ever previously incurred. This is not simply “fluctuation around the mean” as CUB suggests in testimony. CUB/100/p. 14. PGE's FAS 87 expense has remained at a level between four to five times amounts recorded in 2010. PGE/200/p. 25. This was and continues to be an unusual, extraordinary time for pension expenses due to unprecedented market changes and legal requirements. This was not a normal fluctuation.

Unforeseen. In Order 05-1070 the Commission said: “we will consider whether it was foreseeable as happening in the normal course of events, or not likely to have been capable of forecast.” As stated above and explained in PGE's testimony, FAS 87 pension expense during the deferral period was vastly different than any historical expense, and from the level used to set rates. Some parties attempt to minimize that, but without success. Staff goes so far as to say: “Staff does not agree that the fact that leading experts were wrong about the forecasts is ‘an extenuating circumstance’ that makes the decline in discount rate unforeseeable.” Staff Opening Brief, p. 4. Again, Staff is attempting to set up an impossible standard. To meet this standard PGE, and all others involved in ratemaking, would need to be able to foresee fundamental market changes that are not seen by leading experts in the field. This large increase in FAS 87 expense was, by definition, unforeseeable.

Magnitude: Order 05-1070 also gave direction on the magnitude of harm to be considered for deferrals. That Order stated:

If the event was modeled or foreseen, without extenuating circumstances, the magnitude of harm must be substantial to warrant the Commission's exercise of discretion in opening a deferred account. If the event was neither modeled nor foreseen, or if extenuating circumstances were not foreseen, then the magnitude of harm that would justify deferral likely would be lower.

As explained in PGE's testimony, there were extenuating circumstances, and this magnitude of diversion from the forecast was not foreseen or foreseeable. The magnitude of harm, then is lower than "substantial". At the risk of being repetitive, the list below from PGE's opening brief demonstrates the magnitude of impact of the excess FAS 87 pension expense:

1. PGE's 2012 (full-year) net pension expense was \$13.2 million, 160% above the \$5.1 million included in retail prices in UE 215. Prior to this year the highest annual net pension expense PGE had ever incurred was \$5.4 million. PGE/200 at 13.
2. PGE's 2013 net pension expense was \$18.6 million, 265% above the amount included in retail prices. *Id.*
3. The excess pension expense that PGE is seeking recovery of for 2012 represents 2% of PGE's net income, and 13% of PGE's net income for 2013. *Id.* at 14.
4. Actual pension expense in 2012 was four standard deviations above the average expense between 1987 and 2010. For 2013, pension expense was five standard deviations above that mean. *Id.* at 20.
5. In part because of this increased pension expense, PGE's earnings were below its authorized level of 10%. In 2012, PGE's regulated adjusted ROE was 9.46%, and in 2013 it was 6.43%. PGE/100/p. 6.

ICNU makes a rather unconvincing attempt to argue that PGE largely ignores the financial impact of its increased pension expense. To support their claim, ICNU argues that PGE's use of percentages to illustrate the magnitude of harm can be subjective and uses an example of a \$32,000 expense authorized in PGE's 2016 prices. ICNU Opening Brief, p. 16. The fact is, as described above, that PGE has used a number of different ways to demonstrate the substantial magnitude of harm incurred and for ICNU to compare a \$13.5 million increase in pension expense (over the amount set in 2013 prices) to a theoretical increase of \$64,000 over amounts in rates is a faulty premise.

Additionally, ICNU attempts to diminish the importance of PGE highlighting its increased pension expense as an impact to net income for 2012 and 2013 by pointing out that PGE's 2014 SEC Form 10-K says "exactly the same thing." ICNU Opening Brief, p. 16. This argument is misleading. The statement that ICNU is referring to in PGE's 2014 10-K does in fact say the "exactly the same thing" because what ICNU is citing is a passage that is a recap of the drivers for 2013, not 2014. ICNU/200/p. 6.

ICNU also claims in its opening brief and in testimony that PGE's net income was unusually low for 2013 because of the Cascade Crossing write-off and increased power cost expenses and that these should not be factored into PGE's net income or regulated adjusted return on equity (ROE) for the year. ICNU Opening Brief, p. 17; ICNU/100/p. 5. As PGE has pointed out, Cascade Crossing was a utility project and therefore should be (and was) treated as a utility expense, and PGE's increased power cost expenses were a direct result of providing electric service to PGE's customers. PGE/200/p. 23. PGE agrees that its net income was exceptionally low for 2013. This is a principle reason why the Commission should allow PGE to defer amounts requested for 2013. The fact remains that the amounts requested for 2013

represent 13 percent of PGE's net income for the year and 86 basis points of ROE. ICNU's attempt to dismiss PGE's under-earning is unavailing.

The FAS 87 expenses subject to this deferral meet the level of harm required. They also meet the "substantial" harm standard.

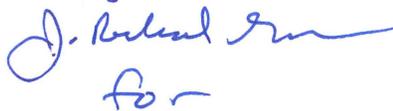
IV. CONCLUSION

Other parties have made numerous arguments about deferral criteria. But, they are not arguments for deferral or ratemaking policy, they are outcome based arguments. It is doubtful that they would be making the same arguments and setting up the same road-blocks to a deferral that involved a refund to customers. The matter should be decided on a fair policy basis.

PGE has met the statutory requirements for deferral, and the Commission's directions for exercise of its discretion. The 2012-2013 period was an unusual time in the financial markets, and with pension legal requirements. The Commission has determined that FAS 87 is the appropriate cost to be recognized in ratemaking, and here FAS 87 expense far exceeded the amount used to set rates. PGE's earnings during the bulk of the deferral in 2013 were 357 basis points below authorized level. Deferral is appropriate.

DATED this 15th day of April, 2016.

Respectfully submitted,



for

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