

1 PUBLIC UTILITY COMMISSION
2 OF OREGON
3 UM 1623

4 In the Matter of

5 PORTLAND GENERAL ELECTRIC
6 COMPANY

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

STAFF PREHEARING MEMORANDUM

9 **I. Introduction.**

10 The question presented in this docket is whether the FAS 87 pension expense that
11 Portland General Electric Company (PGE) seeks to defer for later amortization into rates
12 satisfies the statutory criteria for deferral in ORS 757.259(2)(e) and the discretionary criteria set
13 forth in in Order No. 05-1070. Staff recommends that the Commission find the expense does not
14 meet the criteria.

15 **II. PGE's deferral application.**

16 In its original application filed on August 22, 2012, PGE asked to defer for later
17 amortization into rates (1) the Company's Financial Accounting Standard (FAS) 87 expense in
18 2012 and 2013 that exceeded the \$5.1 million of FAS 87 expense assumed in PGE's revenue
19 requirement in Docket No. UE 215, and (2) carrying costs on PGE's cash contributions to the
20 Company's pension plan. PGE asked the Commission to re-authorize the deferral on August 22,
21 2013, and on August 22, 2014. PGE originally proposed that net FAS 87 expense deferred
22 under the Commission's orders be placed into a balancing account.¹

23 In its opening testimony filed in this docket on December 2, 2015, the Company modified
24 its original deferral request by (1) removing amounts in the original request related to the prepaid
25 pension asset (i.e. carrying costs associated with cash contributions), (2) shortening the deferral

26 ¹ PGE Application for Deferred Accounting 4 (August 22, 2012).

1 period from August 22, 2012 through August 21, 2015 to August 22, 2012 through December
2 31, 2013, and (3) withdrawing the request to place the deferred amounts in a balancing account.²
3 PGE explains in its opening testimony that it removed carrying costs associated with cash
4 contributions in response to the Commission's treatment of pension expense in Docket No. UM
5 1633.³ PGE explains that it shortened the deferral period to exclude net FAS 87 expense in 2014
6 and 2015 to reduce the complexity of this case and "because the variances (between the actual
7 and forecasted levels of FAS 87 expense) for 2014 and 2015 are largely offsetting."⁴ PGE states
8 that its actual 2014 net pension expense was approximately \$3.5 million below the amount
9 approved in UE 262, and that PGE expects its actual 2015 net pension expense to be
10 approximately \$3.6 million above the amount approved in UE 283.⁵

11 PGE's actual net FAS 87 pension expense after capitalization was \$13.2 million in 2012
12 and \$18.6 million in 2013.⁶ PGE seeks to defer approximately \$2.9 million for 2012 and \$13.5
13 million for 2013.⁷

14 **III. Commission criteria for deferral.**

15 The Commission determines whether a deferral application filed under ORS
16 757.259(2)(e) should be granted with a two-stage review.⁸ During the first stage, the
17 Commission examines whether the application meets requirements of ORS 757.259(2)(e).
18 Under ORS 757.259(2)(e), the Commission is authorized to allow deferral of "identifiable
19 utility expenses or revenues, the recovery or refund of which the commission finds should

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21 ² PGE/100, Batzler-Hager/5-6.

22 ³ PGE/100, Batzler/Hager/5-6.

23 ⁴ PGE/100, Batzler/Hager/5.

24 ⁵ PGE/100, Batzler-Hager/5-6.

25 ⁶ PGE100, Batzler-Hager/3.

26 ⁷ PGE/100, Batzler-Hager/3.

⁸ See e.g., *In the Matter of Portland General Electric Application for Deferred Accounting of Excess Power Costs Due to Plant Outage*, Order No. 07-049 (Docket No. UM 1234) (2007).

1 be deferred in order to minimize the frequency of rate changes or the fluctuation of rate
2 levels or to match appropriately the costs borne by and benefits received by ratepayers.”

3 In the second stage of examination, the Commission determines whether the
4 deferral application meets its discretionary criteria by examining the nature of the event
5 leading to the request for deferral and magnitude of harm.⁹ When applying its
6 discretionary criteria to a request to defer, the Commission first will examine the triggering
7 event that led to the deferral application.¹⁰ “The Commission will look to whether the event
8 was modeled in rates, and if so, whether extenuating circumstances were involved that
9 were not foreseeable during the rate case, or whether the event fell within a foreseen range
10 of risk when rates were last set.”¹¹ If the event was not modeled, the Commission will
11 “consider whether it was foreseeable as happening in the normal course of events, or not
12 likely to have been capable of forecast. The Commission will examine whether or not the
13 ‘risks are reasonably predictable and quantifiable.’”¹²

14 Next, the Commission examines the magnitude of the underlying event in terms of the
15 potential harm. “The type of event—modeled in rates or not, foreseeable or not—will affect the
16 amount of harm that must be shown by the utility. If the event was modeled or foreseen, without
17 extenuating circumstances, the magnitude of harm must be substantial to warrant the
18 Commission’s exercise of discretion in opening a deferred account.”¹³ However, if the event
19 was neither modeled nor foreseen, or if extenuating circumstances were not foreseen, the
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22 ⁹ *In the Matter of the Public Utility Commission of Oregon Staff Request to Open an*
23 *Investigation Related to Deferred Accounting*, Order No. 05-1070 (Docket No. UM 1147)
(2005).

24 ¹⁰ *Id.*

25 ¹¹ *Id.*

26 ¹² *Id.*, quoting Order No. 04-108 at 9.

¹³ *Id.*

1 Commission has explained that the “magnitude of harm that would justify deferral likely would
2 be lower.”¹⁴

3 **IV. Analysis.**

4 **A. PGE’s application does not satisfy the statutory criteria for deferral.**

5 PGE asserts that its deferral request matches costs and benefits because “PGE’s pension
6 plan is a prudent offering of its total compensation package and FAS 87 expense represents the
7 actual cost of providing this plan over the benefit of time in which the expense is determined and
8 reflected on PGE’s income statement.”¹⁵ PGE fails to recognize that pension expense
9 calculations under FAS 87 represent a long-term method of accounting and the costs and benefits
10 should be considered over the long-term.¹⁶ As the Commission noted in its final order in its
11 recent investigation into pension cost recovery, “[b]ecause FAS 87 expense is based on an
12 accrual, not cash basis, the amount of pension costs recorded is generally different than the
13 actual amount of annual contributions made. Over the life of the plan, however, total
14 contributions are expected to equal total FAS 86 expense[.]”¹⁷

15 Provided that the forecast of pension expense established in a rate case represents the
16 median expectation of future pension expense, it should be expected that actual pension expense
17 will exceed the forecast fifty percent of the time and be less than the forecast the remaining fifty
18 percent of the time.¹⁸ Authorizing special rate recovery for two years in which the forecasted
19 expense in rates is less than PGE’s actual pension expense without counterbalancing with
20 refunds in years in which PGE over-recovers pension expense in rates, does not match customer
21 benefits and costs.¹⁹

22 ¹⁴ *Id.*

23 ¹⁵ PGE/200, Batzler-Hager/18.

24 ¹⁶ See e.g., ICNU/100, Mullins/7.

25 ¹⁷ *In the Matter of Public Utility Commission of Oregon Investigation into Treatment of Pension
26 Costs in Utility Rates*, Order No. 15-226 at 2 (Docket No. UM 1633).

26 ¹⁸ See e.g., ICNU/100, Mullins/6.

¹⁹ See Staff/100, Bahr/6.

1 PGE has also not established that this deferral minimizes the need for rate changes.²⁰

2 **B. PGE's application does not satisfy the Commission's discretionary criteria**
3 **for deferral.**

4 **1. The possibility that the forecasted discount rate modeled in rates is**
5 **higher than the actual discount rate is a foreseeable risk.**

6 As discussed above, the event leading to PGE's request for deferral was PGE earning less
7 of a return on its pension expense in 2012 and 2013 because the actual discount rate in those
8 years was lower than that forecasted and modeled into PGE's rates. Because the discount rate is
9 modeled in rates, the appropriate inquiry is "whether the event was within a foreseen range of
10 risk, or whether extenuating circumstances were involved that rendered the event
11 unforeseeable."²¹

12 PGE concedes that forecasted discount rates "by their nature contain uncertainty."²² PGE
13 asserts that the lower than expected discount rates were "unpredictable and unquantifiable"
14 because "every forecast (by leading experts) of macro-economic and financial conditions, which
15 include the forecasts of long-term high-quality bond rates, projected healthy year-over-year
16 growth for 2010-2011 and beyond."²³ Staff does not agree that the fact that leading experts were
17 wrong about the forecasts is "an extenuating circumstance" that makes the decline in discount
18 rate unforeseeable.

19 Staff also disagrees that the discount rate was so low in 2012 and 2013 that it was beyond
20 the foreseen range of risk when PGE's rates were set. While it is true the discount rate has
21 dropped lower in recent years than at any time since 1987 (when FAS 87 was implemented), the
22 percentage decrease in discount rates is not unprecedented.²⁴ Discount rates sank a full 200 basis

23 ²⁰ See CUB/100, McGovern/12 ("With three general rate cases in three years, this is not a
24 deferral aimed at minimizing rate changes.").

25 ²¹ *In the Matter of Portland General Electric Application for Deferred Accounting of Excess*
26 *Power Costs Due to Plant Outage, supra*, Order No. 07-049.

²² PGE/200, Batzler-Hager/11.

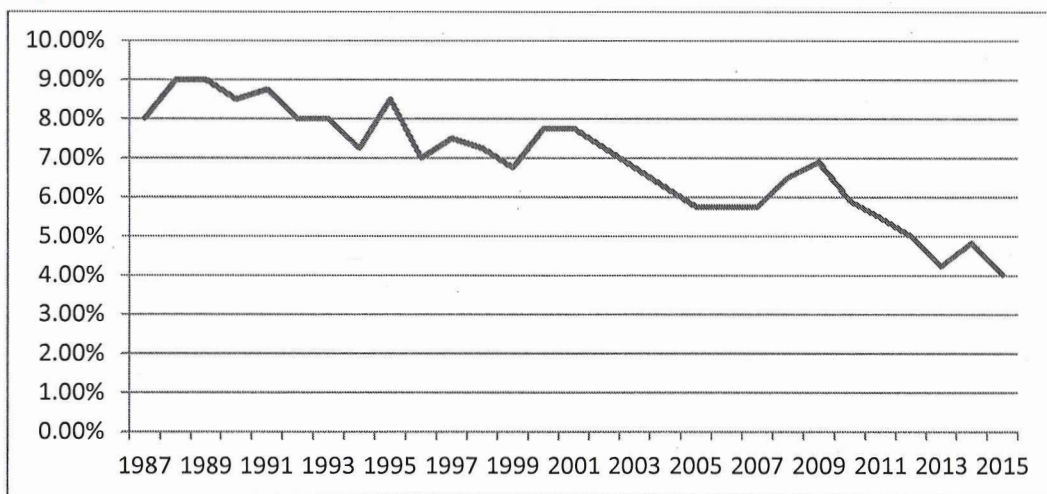
²³ PGE/200, Batzler-Hager/11.

²⁴ Staff/100, Bahr/7.

1 points between 2001 and 2005.²⁵ From 1991 to 1994, discount rates decreased 150 basis points,
2 and in decreased 150 basis points in a single year between 1995 and 1996.²⁶

3 The graph below depicts PGE's discount rate from 1987 through 2015.

4 **Table 1.**



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14 Given the long-term trend of declining discount rates and short-term variability from year
15 to year, the decrease in discount rates in 2012 and 2013 of 47 basis points and 76 basis points,
16 respectively, are not beyond a foreseen range of risk.

17 **2. The unrecovered pension expense at issue in the deferral application is not**
18 **“substantial.”**

19

20 The Company's 2012 revenues were approximately \$1.805 billion, and its net income
21 was approximately \$141 million.²⁷ The Company's revenues and net income in 2013 were
22 \$1.810 billion and \$105 million, respectively.²⁸ The deferral amounts at issue in this proceeding
23 (\$2.9 million and \$13.5 million) are less than one percent of the Company's annual revenues for
24 the years in which the expenses were incurred.

24 ²⁵ Staff/100, Bahr/7.

25 ²⁶ Staff/100, Bahr/7-8.

26 ²⁷ Staff/100, Bahr/12.

²⁸ Staff/100, Bahr/12-13.

1 The Commission has not specified a dollar figure that signifies a “substantial harm.”
2 However, previous Commission orders show what amounts the Commission finds substantial:

3 Although we decline to set a numerical criterion, we can give negative and
4 positive examples. In UM 995, for instance, we established a deadband around
5 PacifiCorp’s baseline of 250 basis points of return on equity. We allowed no
6 recovery of costs or refunds to customers within that deadband, reasoning that
7 the band represented risks assumed, or reward gained, in the course of utility
8 business. In the Idaho Power cases, discussed below, we allowed partial
9 recovery for a financial impact that represented approximately 700 basis points
10 of Idaho Power’s return on equity.²⁹

11 In Docket No. UM 1071, the Commission denied PGE’s request to defer costs associated
12 with hydro replacement power in part because the financial impact was not substantial:

13 In the present application, PGE claims that it has incurred \$31.6 million in
14 excess NVPC, only some of which is attributable to hydro replacement costs.
15 PGE asserts that this excess NVPC amounts to 172 basis points of return on
16 equity. This is well short of the 250 basis points of return on equity within we
17 allowed no recovery in UM 995.

18 * * * * *

19 We find that the cause of PGE’s request is not extraordinary enough to justify
20 deferred accounting. We further find that the financial impact to PGE of excess
21 hydro costs is not significant enough to warrant a deferral. Accordingly, we
22 conclude that PGE’s application for deferred accounting should be denied.³⁰

23 Fluctuations in the discount rate are like hydro variability. The Commission concluded
24 that hydro variability is a “stochastic risk.” The Commission has concluded that it is appropriate
25 to require “substantial” harm before deferral is warranted for stochastic risks because stochastic
26 risk causes costs to swing above and below the average included in rates, so the effect should
27 average out.

28 Culling out two years for special rate recovery of FAS 87 expense is not warranted. As
29 noted in the testimony of the Citizens’ Utility Board of Oregon (CUB), since PGE began

30 ²⁹ *In the Matter of Portland General Electric Company Application for Deferral of Hydro
Replacement Power Costs*, Order No. 04-108 at 9 (Docket No. UM 1071).

³⁰ *Id.*, at 9-11.

1 collecting FAS 87 expense in rates, there have been years in which PGE has significantly over-
2 recovered pension expense. CUB testified that from 1997-2004, the Company collected, in rates,
3 \$84 million in excess of actual pension expense.³¹ PGE's under recovery of \$2.9 million in 2012
4 and \$13.5 in 2013 is not extraordinary.

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6 **V. Conclusion.**

7 Staff recommends that the Commission deny PGE's application to defer.

8 DATED this 28th day of March 2016.

9 Respectfully submitted,

10 ELLEN F. ROSENBLUM
11 Attorney General

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13 _____
14 Stephanie S. Andrus, #92512
15 Sr. Assistant Attorney General
16 Of Attorneys for Staff of the Public Utility
17 Commission of Oregon

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³¹ CUB/100, McGovern/7.