

1 **BEFORE THE PUBLIC UTILITY COMMISSION**

2 **OF OREGON**

3 UM 1633

4 In the Matter of

5 PUBLIC UTILITY COMMISSION OF
6 OREGON

7 INVESTIGATION INTO TREATMENT OF
8 PENSION COSTS IN UTILITY RATES

STAFF'S RESPONSE BRIEF

9 **I. Introduction**

10 For almost 30 years, the Public Utility Commission of Oregon (Commission) "has allowed
11 regulated utilities to recover in rates its pension expenses based upon an actuarial calculation of the
12 utility's 'Net Periodic Pension Costs,' using the standards established by the Federal Accounting
13 Standards Board in its Financial Account Statement (FAS 87)."¹ The Joint Utilities² argue that the
14 Commission should continue this policy of using the FAS 87 expense for ratemaking purposes, but
15 that the Commission should also include the "difference between cumulative contributions and
16 cumulative accounting costs incurred" (*i.e.* the "prepaid pension asset balance") in rate base.³

17 The Public Utility Commission of Oregon Staff (Staff) recommends that the Commission
18 affirm its long-standing policy of only using FAS 87 'net periodic pension costs' as an estimate of
19 the pension expense to be included in rates.⁴ Staff opposes inclusion of the current prepaid
20 pension asset accounting balance in rate base in order to allow the Joint Utilities to earn a rate of
21 return on the prepaid pension asset balance.⁵ If the Commission is inclined to consider inclusion of
22 the current prepaid pension asset accounting balance in future rate base, Staff recommends
23 reasonable parameters to determine the appropriate balance to be included.⁶

24 ¹ See *In the Matter of Northwest Natural Gas Co.*, Docket No. UG 221, Order No. 12-437 at 18.

25 ² The Joint Utilities are Avista Corporation, Cascade Natural Gas Corporation, Northwest Natural Gas Company, PacificCorp d/b/a PacificCorp, and Portland General Electric. Currently, they all have prepaid pension asset balances.

26 ³ See Joint Utilities' Opening Brief at 1, lines 9-12.

⁴ See Staff's Opening Brief at 6, lines 15-17.

⁵ See *Id.* at 7-9.

⁶ See *Id.* at 10-11.

1 On March 24, 2015, the Joint Utilities filed an opening brief. Pursuant to the schedule
2 adopted for this proceeding, Staff files this brief in response to the Joint Utilities opening brief and
3 will file its cross-answering brief on May 15, 2015. In this brief, Staff responds to the Joint
4 Utilities' opening brief as it relates to arguments it makes against Staff's position, but also requests
5 that its prehearing brief be incorporated by reference.

6 **II. DISCUSSION**

7 1. The Commission's long-standing policy of pension costs recovery is lawful.

8 No party has claimed that the Commission's current policy on pension cost recovery is
9 unlawful. In fact, every party – even the Joint Utilities – agrees that it is also the appropriate policy
10 for pension cost recovery.

11 As a matter of policy, the Joint Utilities request that the Commission continue the current
12 pension policy, but add an element to it – namely, allow them to put the prepaid pension asset
13 balance in rate base so they can earn a rate of return on the balance.⁷ While the parties dispute
14 whether inclusion of the prepaid pension asset in rate base is appropriate policy or lawful, no party
15 disputes that the current treatment of pension costs is lawful.

16 2. If past cash contributions are expenses, retroactive ratemaking prohibits the inclusion of the
17 prepaid pension asset in rate base.

18 Staff has argued that recovery through rates of the prepaid pension asset balance is
19 prohibited retroactive ratemaking because cash contributions are considered expenses under the
20 Commission's existing policy.⁸ Staff then argued it would be illogical to conclude that utility
21 expenses that were not and cannot be recovered in future rates because of the rule against
22 retroactive ratemaking are entitled to earn a rate of return by placing them in future rate base.⁹

23 As an illustration, assume that a utility is allowed \$1 million in employee salaries and
24 wages each year. For a period of five years, the utility's actual employee salary and wages
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26 ⁷ See Joint Utilities' Opening Brief at 3, lines 12-15.

⁸ See Staff's Prehearing Brief at 7, lines 3-12.

⁹ See Id., lines 13-16.

1 expense is \$1.3 million per year, resulting in the utility expending \$1.5 million more over a five-
2 year period than was allowed in rates. The rule against retroactive ratemaking would prohibit the
3 \$1.5 million from being recovered in future rates. In addition, it seems improbable that the
4 Commission would allow the \$1.5 million accrued difference between what was collected in rates
5 and what was actually paid by the utility to be put into rate base in a future general rate proceeding
6 and left in rate base until such a time as the utility collected the historic expenditure of salaries and
7 wages in future rates, but if you strip the FAS-87 accounting terminology out of the present
8 situation that is the type of treatment the Joint Utilities are requesting for past cash contributions in
9 excess of the 'net period pensions costs.'

10 The Joint Utilities' assert that Staff's argument fails because it relies on the faulty premise
11 that retroactive ratemaking prohibits recovery of historical cash contributions.¹⁰ The Joint Utilities
12 argue that Staff recognizes that each utility's historical cash contributions will eventually be
13 recovered through future FAS-87 expense, which they argue undermines Staff's claim that it is
14 illegal to recover these historical cash contributions.¹¹

15 The Joint Utilities argument appears reasonable unless you consider the difference between
16 FAS-87 pension expense accounting and actual pension expense recovery in rates. The
17 "accounting cost" and the cash cost will be equal over the life of the plan ("a fundamental
18 characteristic of the accounting cost is that the accumulated contributions will equal the
19 accumulated pension costs over the life of the plan.")¹² However, the pension expense in rates
20 does not equal the accounting or cash costs. The FAS-87 "net period pension costs" changes year-
21 by-year, but the amount in rates only changes in general rate proceedings, so a utility can and will
22 over-or-under collect for pension expense in any given year and the amount collected in rates will
23 not equal the FAS-87 accounting cost. The Commission's current pension policy is not to
24 guarantee that a utility will receive all of its historical cash contributions over time, but rather to
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26 ¹⁰ See Joint Utilities' Opening Brief at 4, lines 8-10.

¹¹ See Id.

¹² See Staff's Prehearing Brief at 4, lines 17-19 citing Joint Testimony/200; Vogl/11, line 17 through Vogl/12, line 2.

1 estimate the utility's test year pension expense, just like it estimates all other expenses it estimates
2 in rates.

3 3. The Joint Utilities' proposal to recover a rate of return on their prepaid pension assets violates
4 the holistic nature of ratemaking.

5 Staff argues that the cash contribution expenses that created the current prepaid pension
6 asset were incurred in the past and the Commission should ask whether or not these pension costs
7 could have been absorbed at the time they were incurred and still resulted in just and reasonable
8 rates.¹³ The Joint Utilities argue that it would be improper retroactive ratemaking to determine
9 whether or not they were able to absorb their historical cash contributions and have rates that were
10 just and reasonable.¹⁴ Staff notes that deferred accounting was available to the Joint Utilities
11 during the times they were required to make cash contributions in excess of the amount of pension
12 expense that had been estimated and paid through rates. If the Joint Utilities had sought deferred
13 accounting, those deferred cash contributions would have been subject to a prudence review and
14 subject to an earnings test to preserve the holistic nature of ratemaking. Although the Commission
15 uses FAS-87 'net period pension costs' to estimate pension costs in a test year, FAS-87 accounting
16 should not drive ratemaking or change the traditional regulatory treatment of out-of-period costs.

17 According to the Joint Utilities, the Commission must accept the entire current prepaid
18 pension asset balance or it will run afoul of retroactive ratemaking. However, the rule against
19 retroactive ratemaking prohibits past losses or profits from being considered when establishing
20 future rates, but it does not prohibit the consideration of historic information to estimate future
21 costs.¹⁵ For example, the Commission regularly relies on historic information to make decisions
22 about future expected expense levels, such as looking at a four-year historical average of an
23 expense account, but it still sets the rates prospectively. Any true-up of expense levels of the past
24 requires specific legislative authorization, as in ORS 757.259.

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26 ¹³ See Staff's Prehearing Brief at 9, lines 1-4.

¹⁴ See Joint Utilities' Opening Brief at 8, lines 3-10.

¹⁵ See Order No. 08-487 at 30.

1 In order to avoid the prohibition against retroactive ratemaking, the Joint Utilities argue
2 that historic cash contributions are “investments” to be included on a prospective basis. The Joint
3 Utilities would be able to avoid both the application of holistic ratemaking and Commission
4 oversight over the appropriate amount to be included in rate base. That should be reason enough to
5 decline the Joint Utilities’ invitation to change long-standing Commission policy.

6 **III. Conclusion**

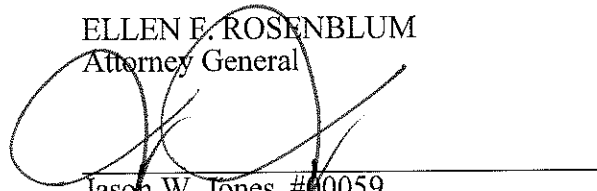
7 Staff requests that the Commission maintain its long-standing policy of pension cost
8 recovery. No party has challenged the legality of the current Commission policy, but the Joint
9 Utilities request an addition to the current policy that raises a host of challenging policy and legal
10 issues. On both policy and legal grounds, Staff recommends against the Joint Utilities’ proposal to
11 include historic cash contributions in future rate base. In the event the Commission deems the
12 current prepaid pension asset balance an investment appropriate for rate base treatment, Staff
13 recommends reasonable parameters for which costs should be included.¹⁶

14 For the foregoing reasons, Staff respectfully requests that the Commission affirm its current
15 pension cost recovery policy. In the alternative, Staff proposes reasonable parameters for
16 determining the appropriate amount of prepaid pension asset balances allowed into rate base.

17 DATED this 24th day of April 2015.

18 Respectfully submitted,

19 ELLEN E. ROSENBLUM
20 Attorney General



21 Jason W. Jones, #00059
22 Assistant Attorney General
23 Of Attorneys for Staff of the Public Utility
24 Commission of Oregon

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26 ¹⁶ See Staff’s Prehearing Brief at 10-11.