Portland General Electric Company
121 SW Salmon Street • Portland, Oregon 97204
PortlandGeneral.com

March 12, 2014

Email / US Mail

Public Utility Commission of Oregon
Filing Center
3930 Fairview Industrial Dr., SE
P.O. Box 1088
Salem, OR 97308-1088

RE: **UM 1633 - PGE Rebuttal Testimony**

Attention: Filing Center

Enclosed for filing in the captioned docket are an original and five copies of:

Rebuttal Testimony of Portland General Electric Company:

- PGE/100

Also enclosed are an original and three copies of:

- Exhibit 101

These documents are being serviced upon the UM 1633 service list.

If you have any questions or require further information, please call me at 503-464-7580. Please direct all formal correspondence and requests to the following email addresses: pge.opuc.filings@pgn.com.

Sincerely,

Patrick G. Hager
Manager, Regulatory Affairs

Enclosures

cc: UM 1633 Service List

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I. Introduction

Q. Please state your names and positions with Portland General Electric ("PGE").

A. My name is Patrick G. Hager. I am a Manager of Regulatory Affairs at PGE. I am responsible for analyzing PGE's cost of capital. My qualifications are described in Joint Testimony Exhibit 103.

My name is Jardon Jaramillo. My position is Director of Compensation and Benefits in the Human Resources Department. My qualifications are described at the end of this testimony.

Q. What is the purpose of your testimony?

A. The purpose of this docket is to recommend and set policy regarding the treatment of pension costs. As such, the opening round of testimony spoke broadly on the elements of pensions, the costs involved in administering a pension plan, and policy recommendations for the prospective regulatory treatment of pension costs. Recognizing that all companies have different histories surrounding their pension plans, past pension costs, and build-up of their current prepaid pension asset, opening testimony did not present the specifics of any company's pension plan. With the filing of reply testimony, parties have now introduced specific examples in testimony that pertain to the history of PGE's pension plan. While PGE still believes that a general rate case proceeding is the appropriate setting for discussing the specifics of our pension plan and related costs, we feel obligated to respond to the issues raised by CUB and Staff directed at PGE's pension plan.

Q. How is the remainder of your testimony organized?

A. In Section II, we respond to specific issues raised by Staff regarding the development of PGE's prepaid pension asset. Section III addresses specific issues raised by CUB including the build-up and development of PGE's prepaid pension asset, the market performance of PGE's pension plan assets, the concept of "incentive regulation", and negative expense. Finally, as other parties appear to have only analyzed specific components of PGE's pension plan, PGE presents an illustrative cost-benefit analysis incorporating all the pieces related to PGE's pension costs.

II. PGE's Response to Staff

Q. Is Staff's assertion that over 50% of PGE's prepaid balance was created prior to enactment of the Pension Protection Act (2008) correct[1]?

A. No. Looking at PGE's cash contributions post-PPA, $56 million has been contributed, which represents approximately 73% of PGE's current prepaid pension asset balance ($76.6 million, as of December 31, 2013).

Q. If PGE did have a large prepaid pension asset prior to 2008, why has it suddenly become a regulatory risk?

A. The issue of the timing differences between the build-up of the prepaid pension asset and its amortization through expense has been around since the inception of FAS 87. The point at which PGE sought regulatory treatment of this mismatch is irrelevant. As discussed in Joint Utilities Exhibits 300 and 400, beginning in 2008, the build-up of the prepaid pension asset was exacerbated by:

1) The PPA accelerating the period over which pension liabilities are funded;
2) The 2008 stock market crash and subsequent decline in interest rates; and
3) Financial regulations in general becoming increasingly stricter.

[1] Staff Exhibit 100, page 19

III. PGE's Response to CUB

Q. CUB claims that PGE's prepaid pension asset has been built by negative expense and not by cash contributions[2]. Is this an accurate portrayal?

A. No. As discussed above, PGE has contributed $56 million into the prepaid pension asset since 2010 and $66 million since 2005. During this time period, PGE recognized one year of negative expense (-$2.4 million in 2008). So, while negative expense has played a role in the past, it represents a small portion of the current prepaid pension asset.

Q. Has CUB properly framed the discussion around PGE's market performance[3]?

A. No. CUB discusses the market performance of assets in the context of actual vs. projected rate of return. What is important when looking at the <u>performance</u> of a company's pension assets is how their returns measure up to <u>market</u> benchmark returns, not projections.

Q. What is the difference between market benchmark return and projected return?

A. A projected return or expected return on assets (EROA) is a long-term estimate that is actuarially determined and generally does not vary significantly from year to year. Its purpose is not to accurately forecast the real market returns for the year, but rather to provide an estimate of the expected average. This average helps smooth FAS 87 expense year to year with the understanding that while actual market returns can vary widely up and down each year, over time they will average near the forecasted projections.

Market benchmark returns are the actual returns that similar pension plans experienced during any given year. These have nothing to do with estimates or projections, only actual performance in the market at large.

Q. Why benchmark against market returns?

[2] CUB Exhibit 100, page 13
[3] CUB Exhibit 100, page 17-18

A. By looking at the market benchmarks you can have an accurate indication of plan performance and management.

Q. How do PGE's pension returns compare to the market benchmarks?

A. PGE's pension asset has consistently outperformed similarly sized pension plans for the last five years, performing in the top decile of funds over the five years ending September 30, 2013. Additionally, from 2000 through 2011, PGE's pension plan performance outpaced the average pension returns of the nation's largest companies (companies listed in the 2012 *Fortune* 1000) by an average of 1.2% annually. Since 1994, PGE has outperformed the market benchmark by 86 basis points on average. This is not the result of a "single year's showing of above average market performance[4]", it is the result of consistently beating the market benchmarks.

Q. CUB notes that PGE's plan lost value during 2008[5]. Was this unexpected?

A. No. Almost all pension plans lost value during the Great Recession. While PGE's pension assets lost value that year, it still outperformed the market benchmark by approximately 80 basis points[6].

Table 1

Year	Plan Assets	Actual Return	Market Benchmark	Difference	Improvement over Benchmark
	A	B	C	D = B – C	E = D * A
2008	$347,000,000	-26.66%	-27.48%	0.82%	$2,845,400

Q. Should one expect a pension plan to consistently perform better than the benchmark?

A. No. To perform better than the market benchmark during any year is difficult. The fact that PGE consistently beat the market benchmark is an indication of better than average plan management.

[4] CUB Exhibit 100, page 18, line 11
[5] CUB Exhibit 100, page 18
[6] This can be translated into approximately $2.8 million improvement on market benchmark returns.

Q. What does this mean for PGE customers?

A. Market benchmark asset returns are what one might expect from a prudently run pension plan. As asset returns are one of the primary factors in determining both the level of FAS 87 expense and the amount of cash contributions needed to fund the pension plan, customers benefit from above benchmark returns through reduced FAS 87 expense and reduced cash contributions.

Q. Is PGE proposing "incentive regulation[7]"?

A. No. But as noted above, better than average market performance benefits customers. The current regulatory framework acts as a disincentive to manage the plan to achieve returns above market benchmarks.

Q. Explain how PGE is currently dis-incented.

A. The better PGE's pension asset performance is the lower its FAS 87 expense becomes for the year and the slower its prepaid pension asset winds down. As FAS 87 expense is the only thing used to set rates and the more FAS 87 expense that is incurred in the year, the more you can reduce the prepaid pension asset, realizing better than average returns can actually harm PGE's bottom line.

Q. Is PGE still asking for the opportunity to recover the costs associated with financing the prepaid pension asset?

A. Yes. PGE has incurred a cost as a direct result of funding the prepaid pension asset, while at the same time customers have received a benefit.

Q. Have PGE's pension investment fund managers "underperformed[8]"?

[7] CUB Exhibit 100, page 17
[8] CUB Exhibit 100, page 33, line 16

A. No. On the contrary, PGE's investment fund managers are incented to beat the market benchmarks and more often than not, they have, to the benefit of PGE's customers. As discussed above, when actual returns are higher than the market benchmarks, pension plan assets and the funded status of a plan is higher than one would expect from average plan performance. This results in reduced cash contributions and reduced FAS 87 expense. Both of these corresponding outcomes benefit customers.

Q. Is it difficult to determine the prudency of PGE's pension plan management?

A. No. One simply needs to look at PGE's plan performance and justifications for contributions to determine if PGE has acted prudently in regards to managing its pension plan over the years.

Q. Are there issues with CUB's analysis related to PGE?

A. Yes. In their analysis, CUB focuses on select time frames and aspects related to PGE's pension plan that yield the greatest results in support of CUB's arguments. On one hand CUB argues that one must go back to the beginning of FAS 87 in order to have an accurate look at the components affecting the prepaid pension asset, while at the same time they perform analyses that focus on very specific time periods.

Q. Has PGE performed any cost/benefit analysis around the cost of its pension plan?

A. Yes. PGE has analyzed the costs and benefits related to our pension plan from the inception of FAS 87 to the present, provided here as PGE Exhibit 101. While prior analyses from other parties have focused on one or two components of pension costs, PGE's model provides a more comprehensive look at the components related to the cost of administering and maintaining its pension plan.

Q. What are the components involved?

A. PGE Exhibit 101 has split the costs and benefits into two categories; those which have been included in revenue requirement as part of a general rate proceeding and those which have not. The components within those two categories include: FAS 87 expense in revenue requirement, actual FAS 87 expense, cash contributions, the prepaid pension asset balance, the deferred tax liability/asset (DTL/DTA) included in revenue requirement, and the actual DTL/DTA for each year from 1987-2013. For demonstration purposes only, the amounts identified as being "in Revenue Requirement" are those used for setting rates in a general rate proceeding and are assumed to remain in effect until the next general rate proceeding.

Q. What does this analysis show and what conclusions can be drawn from it?

A. The analysis in PGE Exhibit 101 shows all the costs that customers have paid compared to all the benefits they have received since the inception of FAS 87. When taking a more comprehensive look at pension costs and benefits, customers have avoided a total of over $96 million in potential pension costs.

Q. Is PGE asking for recovery of these costs?

A. No. This analysis is meant to be illustrative only; PGE is not asking to go back in time to recover past costs.

Q. Please summarize your testimony.

A. While this is a generic docket, meant to set policy regarding the treatment of pension costs, PGE felt it necessary to respond to the specific pieces of Staff and CUB testimony where PGE's pension history is discussed. The facts support that PGE continues to incur costs related to the financing of its pension plan that are not addressed by the current regulatory framework. Furthermore, PGE has and can demonstrate the prudent management of its pension costs provided a benefit to customers. As such, PGE is simply asking for the opportunity to recover its prudently incurred pension plan costs.

Q. Mr. Jaramillo, please summarize your qualifications.

A. I received a Bachelor of Arts degree in economics from Northwest Nazarene University and am completing coursework toward a Masters of Business Administration at the University of California, Los Angeles. Prior to joining PGE, I worked at Deloitte & Touche, where I served various public utilities as an external auditor and worked in mergers and acquisitions consulting. I joined PGE in 2011, becoming the Director of Compensation and Benefits in 2013.

Q. Does this conclude your testimony?

A. Yes.

List of Exhibits

PGE Exhibit	Description
101	PGE Pension Plan Cost-Benefit Analysis

CERTIFICATE OF SERVICE

I hereby certify that I have this day caused **PORTLAND GENERAL ELECTRIC COMPANY REBUTTAL TESTIMONY** to be served by electronic mail to those parties whose email addresses appear on the attached service list for OPUC Docket No. UM 1633.

DATED at Portland, Oregon, this 12th day of March 2014.

Patrick G. Hager
Manager, Regulatory Affairs
Portland General Electric Company
121 SW Salmon St., 1WTC0702
Portland, OR 97204
(503) 464-7580 Telephone
(503) 464-7651 Fax
patrick.hager@pgn.com

SERVICE LIST – 03/12/14
OPUC DOCKET # UM 1633

OPUC Dockets CITIZENS UTILITY BOARD OF OREGON dockets@oregoncub.org	Robert Jenks (C) CITIZENS UTILITY BOARD OF OREGON bob@oregoncub.org
G. Catriona McCracken (C) CITIZENS UTILITY BOARD OF OREGON catriona@oregoncub.org	Irion A Sanger (C) DAVISON VAN CLEVE las@dvclaw.com
S Bradley Van Cleve (C) DAVISON VAN CLEVE bvc@dvclaw.com	Jay Tingey PORTLAND GENERAL ELECTRIC pge.opuc.filings@pgn.com
David J. Meyer (W) (C) AVISTA CORPORATION david.meyer@avistacorp.com	Douglas C Tingey PORTLAND GENERAL ELECTRIC doug.tingey@pgn.com
Elizabeth Andrews (C) AVISTA CORPORATION liz.andrews@avistacorp.com	Brian Bahr (C) PUBLIC UTILITY COMMISSION Brian.bahr@state.or.us
Patrick Ehrbar (C) AVISTA CORPORATION pat.ehrbar@avistacorp.com	Jason W Jones (C) PUBLIC UTILITY COMMISSION jason.w.jones@state.or.us
Tommy Brooks (C) CABLE HUSTON BENEDICT HAAGENSEN & LLOYD tbrooks@cablehuston.com	Pamela Archer CASCADE NATURAL GAS pamela.archer@cngc.com
Chad M. Stokes (C) CABLE HUSTON BENEDICT HAAGENSEN & LLOYD cstokes@cablehuston.com	Michael Parvinen CASCADE NATURAL GAS michael.parvinen@cngc.com
MaryAlice Rosales CASCADE NATURAL GAS maryalice.rosales@cngc.com	Regulatory Dockets IDAHO POWER COMPANY dockets@idahopower.com
Lisa D. Nordstrom (C) IDAHO POWER COMPANY lnordstrom@idahopower.com	Lisa Rackner (C) MCDOWELL RACKNER & GIBSON dockets@mcd-law.com
Edward Finklea (W) (C) NORTHWEST INDUSTRIAL GAS USERS efinklea@nwigu.com	E-Filing NORTHWEST NATURAL efiling@nwnatural.com
Mark R. Thompson (C) NORTHWEST NATURAL mark.thompson@nwnatural.com	R. Bryce Dalley (C) PACIFIC POWER bryce.dalley@pacificorp.com
Sarah Wallace (C) PACIFIC POWER sarah.wallace@pacificorp.com	Oregon Dockets PACIFIC POWER oregon.dockets@pacificorp.com
Ralph Smith LARKIN & ASSOICATES PLLC rsmithla@aol.com	

	Test Year				Test Year				Test Year		Test Year					Test Year					Test Year		Test Year		Test Year		
$s in millions	**1987**	**1988**	**1989**	**1990**	**1991**	**1992**	**1993**	**1994**	**1995**	**1996**	**1997**	**1998**	**1999**	**2000**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**
FAS 87 Actual	(1.30)	2.90	3.20	1.60	3.60	3.10	2.00	0.90	(2.30)	(1.10)	(5.00)	(8.20)	(13.90)	(13.20)	(15.50)	(13.10)	(6.70)	(4.40)	-	3.90	2.30	(2.40)	0.40	3.70	5.42	12.43	19.09
FAS 87 in Revenue Requirement[1]	-	-	-	-	0.05	0.05	0.05	0.05	0.61	0.61	0.80	0.80	0.80	0.80	0.80	-	-	-	-	-	1.10	1.10	-	-	5.10	5.10	5.10
Prepaid Actual	(2.70)	1.20	3.70	2.90	0.20	(2.90)	(4.30)	(5.40)	(2.90)	(0.90)	4.00	-	14.00	39.00	55.00	68.00	73.00	78.00	88.00	84.00	82.00	84.00	85.00	111.00	129.00	108.00	76.57
Prepaid Return On	(0.20)	(0.11)	0.36	0.48	0.23	(0.20)	(0.52)	(0.71)	(0.55)	(0.25)	0.21	0.27	0.94	3.57	6.33	7.87	9.02	9.66	10.62	11.01	9.66	9.66	9.87	11.45	13.62	13.45	10.47
DTL/DTA Actual[2]	0.81	(0.36)	(1.11)	(0.87)	(0.06)	0.87	1.29	1.62	0.87	0.27	(1.20)	-	(4.20)	(11.70)	(16.50)	(20.08)	(22.53)	(24.28)	(26.85)	(25.34)	(24.25)	(25.31)	(25.20)	(37.52)	(46.43)	(38.63)	(29.06)
DTL/DTA Return On Actual	(0.07)	(0.04)	0.12	0.16	0.07	(0.06)	(0.16)	(0.21)	(0.17)	(0.08)	0.06	0.08	0.28	1.07	1.90	2.34	2.73	3.00	3.27	3.34	2.89	2.88	2.95	3.66	4.76	4.83	3.84
DTL/DTA Return On in Revenue Requirement	(0.07)	(0.07)	(0.07)	(0.07)	0.07	0.07	0.07	0.07	(0.17)	(0.17)	0.06	0.06	0.06	0.06	0.06	2.34	2.34	2.34	2.34	2.34	2.89	2.89	2.95	2.95	4.76	4.76	4.76
Pension Expense - Customer Cost / (Benefit) in Revenue Requirement	-	-	-	-	0.05	0.05	0.05	0.05	0.61	0.61	0.80	0.80	0.80	0.80	0.80	-	-	-	-	-	1.10	1.10	-	-	5.10	5.10	5.10
Pension Expense - Customer Cost / (Benefit)	1.30	(2.90)	(3.20)	(1.60)	(3.60)	(3.10)	(2.00)	(0.90)	2.30	1.10	5.00	8.20	13.90	13.20	15.50	13.10	6.70	4.40	-	(3.90)	(2.30)	2.40	(0.40)	(3.70)	(5.42)	(12.43)	(19.09)
Prepaid - Customer Cost / (Benefit)	0.20	0.11	(0.36)	(0.48)	(0.23)	0.20	0.52	0.71	0.55	0.25	(0.21)	(0.27)	(0.94)	(3.57)	(6.33)	(7.87)	(9.02)	(9.66)	(10.62)	(11.01)	(9.66)	(9.66)	(9.87)	(11.45)	(13.62)	(13.45)	(10.47)
Deferred Tax - Customer Cost / (Benefit) in Revenue Requirement	(0.07)	(0.07)	(0.07)	(0.07)	0.07	0.07	0.07	0.07	(0.17)	(0.17)	0.06	0.06	0.06	0.06	0.06	2.34	2.34	2.34	2.34	2.34	2.89	2.89	2.95	2.95	4.76	4.76	4.76
Deferred Tax - Customer Cost / (Benefit)	0.07	0.04	(0.12)	(0.16)	(0.07)	0.06	0.16	0.21	0.17	0.08	(0.06)	(0.08)	(0.28)	(1.07)	(1.90)	(2.34)	(2.73)	(3.00)	(3.27)	(3.34)	(2.89)	(2.88)	(2.95)	(3.66)	(4.76)	(4.83)	(3.84)
Customers - In Revenue Requirement	(0.07)	(0.07)	(0.07)	(0.07)	0.12	0.12	0.12	0.12	0.45	0.45	0.86	0.86	0.86	0.86	0.86	2.34	2.34	2.34	2.34	2.34	3.99	3.99	2.95	2.95	9.86	9.86	9.86
Customers - Not in Revenue Requirement	1.56	(2.75)	(3.67)	(2.24)	(3.89)	(2.84)	(1.32)	0.02	3.02	1.43	4.73	7.85	12.68	8.56	7.28	2.89	(5.05)	(8.26)	(13.89)	(18.25)	(14.84)	(10.14)	(13.22)	(18.81)	(23.79)	(30.70)	(33.40)
Cumulative - Customer Cost / (Benefit)	1.50	(1.32)	(5.06)	(7.37)	(11.14)	(13.87)	(15.06)	(14.93)	(11.46)	(9.59)	(4.00)	4.71	18.25	27.68	35.82	41.04	38.34	32.42	20.86	4.96	(5.90)	(12.06)	(22.33)	(38.19)	(52.12)	(72.96)	**(96.50)**

Orders	Grossed up COC
order 87-1017	16.07%
Order 91-186	14.56%
Order 95-322	13.30%
1996	13.46%
01-777	12.80%
07-015	11.64%
09-020	11.68%
10-478	11.35%

1. For 1987 - 1990 data on pension costs in rates is unavailable. As a result amount has conservatively been set to zero
2. For 1987 - 2001, the DTL/DTA is based on actual percentage split from 2002-2009