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March 12, 2014

VIA ELECTRONIC AND U.S. MAIL

PUC Filing Center
Public Utility Commission of Oregon
PO Box 1088
Salem, OR 97308-1088

Re: UM 1633 – In the Matter of OREGON PUBLIC UTILITY COMMISSION, Investigation into Treatment of Pension Costs in Utility Rates

Attention Filing Center:

Enclosed for filing in docket UM 1633 are an original and five copies of Idaho Power Company's Rebuttal Testimony of Bruce E. MacMahon. A copy of this filing has been served on all parties to this proceeding as indicated on the attached certificate of service.

Very truly yours,

Wendy McIndoo

Wendy McIndoo
Office Manager

Enclosures

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BEFORE THE PUBLIC UTILITY COMMISSION
OF OREGON

DOCKET NO. UM 1633

In the Matter of	)
	)
PUBLIC UTILITY COMMISSION OF OREGON,	)
	)
	)
Investigation into Treatment of Pension Costs in Utility Rates.	)
	)

IDAHO POWER COMPANY

REBUTTAL TESTIMONY

OF

BRUCE E. MACMAHON

March 12, 2014

Q. Please state your name, business address, and present occupation.

A. My name is Bruce E. MacMahon, my business address is 1221 West Idaho Street, Boise, Idaho 83702 and I am the Director of Accounting and Financial Reporting for Idaho Power Company .

Q. What is your educational background?

A. I graduated from Saint Mary's College in Moraga, California in 1983, receiving a Bachelor of Business Administration Degree in Accounting. Since that time, I have participated in numerous training courses related to industry, taxation, accounting, management and leadership, as well as developed course material and provided instruction on technical business topics. I became a licensed Certified Public Accountant in the state of Idaho in 1987. At various times in my career I have been a member of the Associated Taxpayers of Idaho, the Tax Committee of the Edison Electric Institute, and a member of the Tax Executives Institute. Currently, I am a member of the Idaho Society of CPAs, and a board member of the Treasure Valley CFO Forum.

Q. Please outline your business experience.

A. I have worked in government and industry since graduating from college in 1983. I initially worked for the Federal Energy Regulatory Commission as a Financial Auditor, taking part in a number of audits of regulated utility companies, including Idaho Power. From 1984 to 1996 I provided corporate tax services for Boise Cascade Corporation, and from 1996 to 1998 I worked for Idaho Power as a Tax Research Coordinator and then as Idaho Power's Corporate Tax Director from 1998 to 2003. From 2003 to 2007 I served as the Chief Financial Officer for IDACOMM, Inc., an affiliated company to Idaho Power Company, and from 2007 to 2010, I was the President of Idacorp Financial Services, Inc., also an affiliated company to Idaho Power. In 2010, I became the Director of Accounting and Financial Reporting for

Idaho Power Company, my current position. Each of my various positions has consisted of tax-related or accounting-related preparation, analysis, research, and leadership for these technical areas.

Q. What is the purpose of your rebuttal testimony?

A. The purpose of my testimony is to inform the Public Utility Commission of Oregon ("Commission") that the current regulatory treatment of pension costs in Oregon sufficiently provides Idaho Power with an opportunity to recover prudently incurred pension costs; therefore, no change to that treatment is needed for Idaho Power at this time. My testimony will support this view by providing the Commission with information demonstrating that Idaho Power is differently situated as compared to the Joint Utilities.[1]

Q. Please explain how the remainder of your testimony is organized.

A. My rebuttal testimony is presented as follows:

- Section I provides an introduction and overview of this docket and my understanding of the parties' positions.
- Section II details a number of factors contributing to differences that exist between Idaho Power's pension costs as compared to those of the Joint Utilities.
- Section III presents Idaho Power's proposal in this docket.
- Section IV provides a summary of Idaho Power's proposal and conclusions

<u>Section I - Introduction</u>

Q. What is the main issue that produced this docket?

A. "In several recent proceedings, Investor Owned Utilities ("IOU's") have requested that the Commission expand its approach to pension cost recovery to include costs

[1] The Joint Utilities are Northwest Natural Gas Company, Portland General Electric Company, PacifiCorp, Avista Utilities, and Cascade Natural Gas.

that current policy does not address. In response to these proposals, the Commission issued Order No. 12-408 which opened an investigation to "review treatment of pension expense on a general, non-utility specific basis."[2] The purpose of this docket is to complete that investigation, and to establish an appropriate policy for rate recovery of pension-related costs on a prospective basis. On September 30, 2013, the Joint Utilities filed joint testimony[3] requesting that they be allowed to prospectively recover financing costs associated with their prepaid pension assets. On Thursday, December 19, 2013, Staff, the Citizens' Utility Board of Oregon ("CUB"), and the Northwest Industrial Gas Users ("NWIGU") and the Industrial Customers of Northwest Utilities ("ICNU") (collectively "NWIGU/ICNU") filed reply testimony responding to a proposal by the Joint Utilities.

Q. Please summarize the Joint Utilities' proposal.

A. The Joint Utilities request that the Commission continue to allow them to recover FAS 87 expense as well as allow for the recovery in rates the financing costs related to prepaid pension assets that result from timing differences between cash contributions to their pension plans and the recognitions of expense. "Specifically, utilities have pointed out that the current recovery policy, based only on FAS 87[4] expense, does not recognize significant financing costs incurred by the utilities in carry out their legal obligations to fund their pension plans."[5]

Q. Please summarize the proposals by Staff, CUB and NWIGU/ICNU.

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[2] *Re Northwest Natural Gas Co.*, Docket UG 221, Order No. 12-408 at 4 (Oct. 26, 2012).

[3] On September 30, 2013, Idaho Power filed a letter stating it did not intend to file opening testimony in this docket.

[4] The "expense" associated with a pension plan is determined in accordance with FASB Statement of Financial Accounting Standards No. 87 which has been subsequently codified into the FASB Accounting Standards Codification Topic 715, Compensation – Retirement Benefits (ASC Topic 715). This expense is therefore often referred to as FAS 87 expense, which is how it will be referred to in this testimony.

[5] Joint Testimony/100, Joint Parties/1-2.

A. Staff's primary recommendation is to disallow the inclusion in rate base any of the current prepaid pension asset/accrued pension liability. The associated deferred tax asset or liability on the current balance, according to Staff, should also be excluded from rates. Staff further suggests that FAS 87 should continue to be used as a proxy for pension costs in setting rates and utilities should have the opportunity to recover the financing cost of any prepaid or accrued pension balance accumulating prospectively that is not associated with excess pension investment returns. Alternatively, Staff recommends that the Commission allow the utilities the opportunity to recover a return on a portion of both the current and prospective prepaid or accrued pension account balances and to continue the use of FAS 87 to set rates. Various provisions for netting and exclusions of amounts were proposed. The resulting Commission-authorized prepaid or accrued pension balance allowed into rate base should carry a lower rate of return ("ROR") than the Company's authorized ROR.[6]

CUB recommends continuing ratemaking based on FAS 87, whether FAS 87 is positive or negative, and CUB would be willing to consider a balancing account for FAS 87 expense.[7]

NWIGU/ICNU's primary recommendation is to not modify how pension costs are treated in rates.[8]

Section II – Idaho Power's Pension Plan

Q. Please provide an overview of Idaho Power's pension plan.

A. Idaho Power's pension plan was established in 1943 and continues as part of the

[6] Staff/100, Bahr/2.

[7] CUB/100, Jenks-McGovern/42-34.

[8] NWIGU-ICNU /100, Smith/44-45.

Company's total compensation package for employees. The plan is a defined benefit pension plan covering all eligible employees of Idaho Power. The plan is subject to the provisions of the Employee Retirement Income Security Act of 1974 ("ERISA"), as amended.

As part of the Company's total compensation package, employees receive pension benefits, payable at normal retirement age, after accumulating five years of vested service, as defined by the plan. There is no partial vesting of benefits. The plan provides for normal retirement upon reaching age 65, early retirement with reduced monthly benefits as early as age 55 with 10 years of service, or retirement at any age with 30 years of service (with reduced monthly benefits if before age 62).

Q. Does Idaho Power use the same methodology to account for pension expense in both of its jurisdictions?

A. No. In the Company's Oregon jurisdiction, the current ratemaking policy allows for recovery of FAS 87 expense. In the Company's Idaho jurisdiction, the Idaho Commission authorized[9] the Company to account for its defined benefit pension expense on a cash basis following removal[10] of the accrued FAS 87 amounts from Idaho Power's 2003 test year revenue requirement. As part of its Order, the Idaho Commission acknowledged that it is appropriate for the Company to seek recovery in the Company's revenue requirement of reasonable and prudently incurred defined benefit pension expense based on actual cash contributions.[11]

Q. Has the Company attempted to align pension recovery in both of its jurisdictions?

[9] Case No. IPC-E-07-07, Order No. 30333 at 4 (June 1, 2007).

[10] Case No. IPC-E-03-13, Order No. 29505 at 15 and 21 (May 25,2004).

[11] Case No. IPC-E-07-07, Order No. 30333 at 4.

A. Yes. In Docket UM 1455, Idaho Power filed a request to move from an accrual (FAS 87) to a cash basis of pension recovery to align the regulatory treatment for pension expense in both Oregon and Idaho. Ultimately, the Company withdrew its request based on the settlement of a concurrent general rate case, Docket UE 213, in which the Company entered into a settlement stipulation that stated "the parties further agree that the stipulated revenue requirement in this rate case includes a FAS 87 expense"[12] although no specific dollar amount of pension recovery was specified in the stipulation.

Q. Does Idaho Power currently have a pre-paid pension asset?

A. No. Idaho Power has an accrued pension liability on its books. This means that for Idaho Power, cumulative FAS 87 pension expense exceeds the cumulative cash contributions made to the pension plan to date. In other words, Idaho Power has not paid out more in cash on a cumulative basis toward its pension than it has recorded as expense.

Q. Please explain why Idaho Power is differently situated as compared to the Joint Utilities?

A. The factors that combine to measure pension costs, both on a FAS 87 basis or on a cash contribution basis, are complex. Measuring what may happen over a long future period, both from an employee behavior basis and from the market's ability to return on assets, is inherently difficult and uncertain. For Idaho Power, its plan experience during the ten-year period from 2000 through 2010 shifted from producing a pre-paid pension asset to producing an accrued pension liability. During this time its FAS 87 expense rose significantly, and Idaho Power's funding requirements were not triggered until the end of the decade. Starting in 2010 and

[12] *Re Idaho Power Co.*, Docket UE 213, Order No. 10-064 at 4 (Feb. 24, 2010).

continuing since, Idaho Power has made annual contributions to its plan.

A large reason for this shift toward a net liability was the relatively long period of time that Idaho Power was not required to make contributions to its pension plan while at the same time recording FAS 87 expense. At the onset of a major downturn in the capital markets in 2008, losses were triggered for Idaho Power's pension trust assets, which combined with discount rates decreasing to historically low levels, increased the level of required cash contributions while at the same time increasing FAS 87 expense initially to an even greater extent. Various legal reforms were enacted to shore up funding requirements that developed. Funding relief rules emerged in 2008 as a response to the severity of funding requirements in the Pension Protection Act ("PPA") that went into effect about the time of the economic downturn. The Worker, Retiree, and Employer Recovery Act of 2008, the Pension Relief Act of 2010, as well as the Moving Ahead for Progress in the 21st Century Act of 2012, each brought funding options to plan sponsors. Idaho Power was in a position to make certain elections under these rules, deferring its need to resume funding until 2010. This funding deferral, allowed under the relief provisions of recently enacted law, was a contributing factor to Idaho Power's movement from a prepaid pension asset in the early part of the decade, to an accrued pension liability by the end of the decade.

Idaho Power and the Joint Utilities have each made their own funding elections under allowable rules, and these may be a contributing factor to the funded status differences between each utility.

Additionally, Idaho Power's pension plan has remained a key element of its total retiree benefits package for employee long-term income security, while other companies may have shifted to other methods, such as a greater reliance on defined contribution plans. To the extent the Joint Utilities have made such strategic choices, their future pension obligations may not be growing at the rate of a plan that continues to add new participants. Idaho Power's plan remains open to new participants.

In measuring the plan's benefit obligation each year, assumptions are made for expected salary growth, personnel turnover, discount rates, as well as smoothing amounts deferred from other years and brought into the measurement at an amortized amount – all of these contribute to the actual final obligation. There are some elections within these calculations that could significantly differ from company to company. For example, Idaho Power uses a custom bond portfolio to compute its allowable discount rate, using bonds that mirror the length of time the benefits are expected to be paid out. A closed or frozen plan would likely have a shorter time horizon, and would properly use a discount rate derived from the shorter term bonds.

Idaho Power's pension plan remains open (though with reduced benefit for those hired on or after January 1, 2011). The Joint Utilities have plans that are in varying degrees of closed or frozen status. After a plan is closed the effects on FAS 87 expense related to expected future salary increases diminish as the remaining participating employees approach retirement. Future salary increases are factored into the FAS 87 expense, but are not factored into funding requirements. As a result, closing a plan may more quickly reduce pension expense as compared to pension funding, causing upward pressure on the prepaid asset versus the impact to an open plan.

Idaho Power's timing and position within its funded status as the market collapsed in 2008 and its timing and elections with respect to commencing new funding in 2010 have each had an impact on its net position as a liability. The cumulative impact of each company's options and elections logically drive differing financial results for each company.

Q. Does Idaho Power expect to remain in an accrued pension liability position in the long-term?

A. No. Idaho Power's pension plan expense and funding schedules have produced both a prepaid pension asset, as well as a pension liability, over the last 20 years. With the exception of one year, Idaho Power's prepaid asset or accrued liability has never been significant or sustained. Based on the recovery of the market and the increase in discount rates, Idaho Power believes its current pension liability will begin to trend toward a prepaid asset, but does not anticipate balances to be significant, whether a net liability or a prepaid asset during the next five years. Inherent uncertainties of projecting beyond that timeframe make it difficult to predict if the Company will have significant or sustained balances in a net prepaid or a net liability position.

Q. Please explain why you believe continued recovery of FAS 87 expense is appropriate specifically for Idaho Power.

A. FAS 87 is intended to smooth a company's pension expense over the life of its pension plan and help to show a more consistent cost from year to year. As described above, the Company's accrued liability position has swung from a pre-paid pension asset position in the early part of the last decade to a liability position by the end of that decade and potentially back to a prepaid within another five years. This kind of volatility, caused by factors that may not be as prevalent for the Joint Utilities that operate frozen or closed plans, is why the Company does not believe embedding a prepaid pension asset or an accrued liability into its rate base is appropriate in Idaho Power's circumstances. The Company believes such treatment is more appropriate in circumstances in which the amounts funded by the company cumulatively in excess of FAS 87 expense are significant, and expected to remain so for a number of years.

Section III – Idaho Power's Response and Proposal

Q. What is Idaho Power's response to the proposals of the Staff, CUB and NWIGU/ICNU?

A. As described above, Idaho Power does not expect its current prepaid pension liability or any anticipated prepaid pension asset to be significant in the next five year timeframe. For purposes of expense recovery, Idaho Power agrees with Staff, CUB, and NWIGU/ICNU that the existing regulatory treatment—the recovery of FAS 87 pension expense—is adequate, at least in Idaho Power's circumstances. Idaho Power believes the FAS 87 amount submitted in a general rate case to be an appropriate measure of pension expense for such period and subsequent periods while such general rates are in effect.

Additionally, Idaho Power does not support the notion of breaking down the net pension amount on the balance sheet into components, such as the portion that arises from so-called "excess earnings". The multiplicity of interrelated factors that contribute to the balance of the net pension asset or liability cannot be cleanly separated without undue complexity. This would result in additional actuarial computations based on assumptions of "what might have been". If the Commission is disposed to make a new regulatory policy for the balance sheet amounts, Idaho Power supports the inclusion or exclusion of the entire balance.

In its testimony, CUB stated that it might be willing to consider the implementation of a balancing account for pension recovery. Because FAS 87 expense is naturally less volatile than cash contributions, Idaho Power does not believe that a balancing account is necessary. Under existing circumstances, FAS 87 expense as included in general rate cases currently provides an appropriate measure for incurred pension expense.

Q. What is Idaho Power's proposal for itself in this docket?

A. The Company believes that the existing regulatory treatment for the recovery of pension expense in its Oregon jurisdiction sufficiently provides Idaho Power with a reasonable opportunity to recover its prudently incurred pension costs and should remain unchanged for Idaho Power. This is due in part because Idaho Power's Oregon jurisdiction is a relatively small portion of its company operations, and its Idaho jurisdiction provides for regulatory recovery on a cash basis for over 95 percent of its incurred costs. Using a FAS 87 approach without rate base adjustments for Idaho Power's Oregon jurisdiction pension costs results in a clear, predictable and consistent method of cost recovery. If the Commission chooses to adopt any modification to the current regulatory treatment for pension costs in light of the issues raised in this case, Idaho Power requests that the Commission recognize that Idaho Power is situated differently than the other utilities and therefore an across–the-board application of such modification would be inappropriate. Idaho Power requests that if the Commission wishes to consider a different regulatory treatment for pension cost recovery going forward, that it assess the merits of applying such treatment individually for each utility.

Section IV - Conclusion

Q. Please summarize your testimony.

A. The Company believes that the current method of pension expense recovery in its Oregon jurisdiction remains adequate for Idaho Power. My testimony provides the Commission with insight as to why Idaho Power is situated differently than the Joint Utilities and why those differences are significant enough to warrant individual treatment in this general policy docket.

Q. Does this conclude your direct testimony in this case?

A. Yes, it does.

CERTIFICATE OF SERVICE

I hereby certify that I served a true and correct copy of the foregoing document in Docket UM 1633 on the following named person(s) on the date indicated below by email addressed to said person(s) at his or her last-known address(es) indicated below.

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