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October 7, 2004

Via Facsimile, Electronically, and US Mail

Ms. Carol Hulse
Oregon Public Utility Commission
P.O. Box 2148
Salem OR 97308-2148

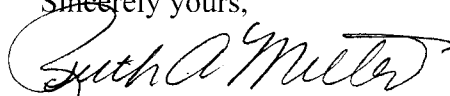
Re: In the Matter of PUBLIC UTILITY COMMISSION OF OREGON Staff
Request to Open an Investigation Related to Deferred Accounting
Docket No. UM 1147

Dear Ms. Hulse:

Enclosed please find an original and six (6) copies of the Opening Comments of the Industrial Customers of Northwest Utilities in the above-captioned Docket.

Please return one file-stamped copy of the document in the self-addressed, stamped envelope provided. Thank you for your assistance.

Sincerely yours,



Ruth A. Miller

Enclosures
cc: Service List

**BEFORE THE PUBLIC UTILITY COMMISSION
OF OREGON**

UM 1147

In the Matter of)	
)	
PUBLIC UTILITY COMMISSION OF)	OPENING COMMENTS OF THE
OREGON)	INDUSTRIAL CUSTOMERS
)	OF NORTHWEST UTILITIES
Staff Request to Open an Investigation)	
Related to Deferred Accounting.)	
_____)	

INTRODUCTION

Pursuant to the prehearing conference memorandum (“Memorandum”) issued in Public Utility Commission of Oregon (“OPUC” or “Commission”) Docket No. UM 1147 on July 26, 2004, and the Clarification of Prehearing Conference Memorandum (“Clarification Memorandum”) issued on July 28, 2004, the Industrial Customers of Northwest Utilities (“ICNU”) submits the following comments regarding the OPUC’s investigation into its deferred accounting policies and practices. ICNU supports adoption of a deferred accounting policy that limits deferred accounting of costs to instances in which discrete costs are incurred under extraordinary and unanticipated circumstances. In addition, ICNU supports adoption of a full procedural schedule in this Docket that includes opening and reply comments regarding the substantive issues.

The goal in this proceeding should be for the Commission to examine its policies, practices, and procedures under the deferred accounting statutes and rules, and establish generic standards that apply to deferred accounting requests. As part of its investigation, the

Commission should determine whether rules should be adopted to implement policies related to deferred accounting and whether statutory changes related to deferred accounting are necessary.

This proceeding should not involve attempts to make fact-specific determinations for individual utilities. As a result, ICNU recommends that the Commission adopt a procedural process in this Docket that includes an opportunity for the parties to submit written comments on the issues and recommend policies for Commission approval. Such a process will allow for adequate development of a record to resolve the issues. A schedule that includes testimony sponsored by a witness and an opportunity for cross-examination, such as the one proposed by Portland General Electric Company (“PGE” or the “Company”) at the prehearing conference, is unnecessary.

DISCUSSION

The Clarification Memorandum states that the Parties should address the following issues in opening comments:

1. Begin addressing the merits of the ten issues identified in Appendix A of the Memorandum. Comments should identify policy matters raised by the issues and set forth initial positions on those policy matters.
2. Discuss whether each issue requires factual development or raises a factual sub-issue.
3. Identify when resolution of a policy matter is dependent upon development of facts.
4. Discuss the interrelationship of the issues. Do certain issues need to be resolved before others? Do the issues that require early resolution require factual development?
5. Recommend a procedural process to adequately develop a record on both facts and policy.

Appendix A to the Memorandum provided a list of issues identified by the parties for discussion in this proceeding, but was not necessarily developed as an exclusive issues list for this Docket.

The issues listed in Appendix A are:

1. Should the requirements for a deferral request differ depending on the circumstances underlying the request, e.g. materiality requirements that differ depending on whether the costs at issue are associated with stochastic risk or scenario risk?
2. Under what circumstances is a particular deferral not within the normal risk range that utilities absorb between rate cases?
3. Should deferrals be limited to the costs associated with the cost-causing factors identified in the original application for deferred accounting?
4. What interest rate should be applied to a deferral balance?
5. What should be the filing requirements and process for deferred accounting investigations?
6. What are the alternatives to deferred accounting for recovery of excess utility costs or revenues between rate cases?
7. Do the Commission's deferred accounting practices and procedures ensure symmetrical treatment of deferrals for excess utility costs and deferrals for excess utility revenues?
8. Should there be an overall cap on the amount of costs that a utility can defer in one year?
9. What must applicant show to demonstrate that a deferral under ORS 757.259(2)(e) will either (a) minimize the frequency of rate changes or fluctuation of rate levels, or (b) match ratepayer benefits and costs?
10. What types of costs are eligible for deferred accounting, e.g. do the costs have to be extraordinary, unanticipated, nonrecurring, and/or discrete?

A summary of ICNU's initial position on each of these issues is provided below, along with a description of the procedural implications of addressing each issue in this Docket. Since additional comments on these and other issues are contemplated later in this Docket, ICNU is reserving detailed comment for a later time.

1. Should the requirements for a deferral request differ depending on the circumstances underlying the request, e.g. materiality requirements that differ depending on whether the costs at issue are associated with stochastic risk or scenario risk?

ICNU supports adoption of a policy that considers all facts and circumstances in resolving a request for deferred accounting. ICNU is concerned, however, about establishing a policy that would result in evaluating deferred accounting requests solely on the basis of requirements that would differ according to the facts underlying the petition. Such an approach may leave the Commission and the parties without any definitive standards to evaluate deferred accounting petitions.

The example stated in the issue refers to the rationale described by the Commission in a recent order denying PGE's request for deferred accounting treatment of excess hydro replacement costs during 2003 in UM 1071. Re PGE, OPUC Docket No. UM 1071, Order No. 04-108 (Mar. 2, 2004) ("Order No. 04-108"). In Order No. 04-108, the Commission described an analysis to evaluate whether a particular deferred accounting request: 1) warranted an exercise of the Commission's discretion to consider a deferral; and 2) fit within the criteria in the deferred accounting statute. Id. at 8. The Commission determined that an exercise of its discretion depended on consideration of two interrelated factors: 1) the type of event that caused the request for deferral; and 2) the magnitude of the event's effect. Id.

The Commission considered the type of event that caused the request for deferral in terms of “stochastic” and “scenario” risks. Stochastic risks are those that are subject to prediction or quantification and may be capable of being modeled in rates. Id. at 8-9. Scenario risks, on the other hand, are not subject to quantification or prediction. Id. at 8.

The Commission considered the magnitude of the event’s effect in terms of the financial impact on the utility. For stochastic risks, the Commission found that the financial impact on the utility must be “substantial.” Id. at 9. For scenario risks, the Commission found that the financial impact on the utility must be “material.” Id.

Implementing differing requirements to evaluate a deferred accounting request as part of a larger overall analytical framework may be workable. This is the approach taken by the Commission in Order No. 04-108. The differing requirements established in Order No. 04-108, however, were only one component of the framework described by the Commission, and the order did not indicate that those differing requirements for differing types of requests should be dispositive. Nevertheless, ICNU supports a deferred accounting framework that treats costs differently depending on whether they are capable of being modeled in rates.

Resolving whether requirements for a deferral request should differ based on the circumstances surrounding the request does not require factual development. This is a decision about whether it would be advisable for the Commission to pursue a particular policy. Such a decision can be made based upon written comments submitted by the parties. This issue can be addressed concurrently with all other issues in this Docket; however, if the ALJ decides to bifurcate this Docket, issues regarding the types of costs that are appropriate for deferred accounting should be addressed in the first phase of the proceeding.

2. Under what circumstances is a particular deferral not within the normal risk range that utilities absorb between rate cases?

Whether a particular deferral is not within the risk range that utilities absorb between rate cases is a fact-specific decision that will depend on the circumstances of each case. The Commission should evaluate the evidence in the record for each deferred accounting request to determine whether the cost or revenue at issue falls within the range of risk accepted by the utility.

Providing evidence to determine the circumstances in which a deferral falls outside the normal risk range for a utility is unnecessary in this proceeding. The goal of this proceeding is not to establish a particular risk range for all Oregon utilities. Indeed, each utility likely has a different risk range and it would be difficult, if not impossible, to establish that range for each utility in a generic investigation. Determining whether a particular deferral falls outside of the risk normally accepted by a utility will be case-specific. As a result, the parties should address in written comments the general framework for evaluating the risk accepted by a utility and determining whether a particular cost falls within the zone of risk, rather than attempting to quantify a range of risk for each utility through submission of testimony and evidence.

3. Should deferrals be limited to the costs associated with the cost-causing factors identified in the original application for deferred accounting?

Deferrals should be limited to the cost causing factors identified in the original application. The deferred accounting statute provides that costs or revenues to be deferred under ORS § 757.259(2)(e) must be “identifiable.” Furthermore, the Commission previously has stated that “[f]or the most part, deferrals under [ORS § 757.259(2)(e) are] to be of discrete items which might substantially affect a utility’s earnings on a short term basis.” Re PacifiCorp, OPUC

Docket No. UE 76, Order No. 92-1128 at 8 (Aug. 4, 1992). Deferral of “discrete” and “identifiable” items does not indicate that deferred accounts should be authorized for the purpose of deferring costs that are unknown or unidentified at the time of the application.

In Docket No. UM 995, PacifiCorp filed a request to defer approximately \$63 million in excess power costs related to high wholesale power prices during the western power crisis. PacifiCorp’s deferred account in UM 995 eventually included \$259 million associated with high wholesale power prices, below-normal hydro conditions, and the outage of the Hunter 1 generating plant. ICNU contended that authorization of such a large deferred account that included costs associated with a multitude of causes was inconsistent with the purpose of deferred accounting. Furthermore, the prudence review of such a large and amorphous deferred account proved extremely difficult. Limiting deferred accounts to the cost causing factors is an important way to prevent the “morphing” of deferred accounting requests such as occurred in UM 995. The Commission should adopt a policy that discourages utilities from filing generic deferred accounting requests in the hope of recovering unknown future cost variations.

Resolving whether deferrals should be limited to the costs associated with the cost-causing factors identified in the application is a policy matter that does not require factual development. In addition, this issue can be addressed concurrently with all other issues in this proceeding. As such, testimony and evidence on this issue are unnecessary and the parties should address this limit on deferred accounting in written comments.

4. What interest rate should be applied to a deferral balance?

The Commission should adopt a policy of using the utility's cost of short-term debt as the interest rate to apply to deferral balances. The current practice is to allow utilities to earn interest on a deferral balance at the authorized rate of return, which allows the utility to benefit from the deferral of costs when short-term interest rates are lower than that level. In addition, many deferred accounts are recovered over a relatively short period of time for which a short-term interest rate is more appropriate.

Determining the interest rate to apply to deferral balances is a policy matter that requires no evidence or factual development. The parties can argue their positions regarding the appropriate interest rate to apply to deferral balances in written comments that address all issues concurrently. If specific circumstances justify departure from the standard rule in a particular deferral request, those facts can be determined in that case.

5. What should be the filing requirements and process for deferred accounting investigations?

ICNU supports revision of the Commission's filing requirements and process for deferred accounting applications. In particular, specific procedures are needed to address the first phase of a deferred accounting request, authorization of the deferred account. The rules currently provide for submission of comments regarding a deferred accounting request within a time period set forth in the notice that must accompany the application, and that time period may be no less than twenty-five days. OAR § 860-027-0300(6)(d). The applicant then has ten days to submit reply comments. OAR § 860-027-0300(8). The rules provide that the Commission will consider the matter at a public meeting. OAR § 860-027-0300(7). Nevertheless, the deferred accounting statute provides that a party may request a hearing on the request.

ORS § 757.259(2). As a result, there is no definite process for deferred accounting applications and particular requests may follow different procedural paths.

Although flexibility in the process is helpful to address different types of deferred accounting requests, at times these procedures have proved too amorphous, and the standard for approval of a deferred account has been unclear. For example, applications such as PGE's request in UM 1071 have been left pending before the Commission for months prior to any action being taken. A prehearing conference was not scheduled in UM 1071 until eight months after the application was filed. Furthermore, PGE argued after Order No. 04-108 was issued in UM 1071 that it was improper for the Commission to consider disputed issues of fact in the deferral authorization phase of a proceeding. Re PGE, OPUC Docket No. UM 1071, PGE's Application for Reconsideration and Rehearing of Order No. 04-108 at 9 (May 3, 2004). Under these circumstances, the Commission should clarify the issues that need to be resolved in both the initial request for deferral and any request to recover deferred amounts in rates, and should adopt guidelines for how deferral applications will be processed.

ICNU is not proposing a detailed process for deferred accounting requests to follow at this time. Nevertheless, this is a very important issue that likely merits its own rulemaking. Developing an appropriate process for addressing deferred accounting applications does not require factual evidence or testimony, and this issue can be addressed concurrently with all other issues.

6. What are the alternatives to deferred accounting for recovery of excess utility costs or revenues between rate cases?

Determining the alternatives to deferred accounting is outside the scope of this proceeding, which is a general investigation of the Commission's deferred accounting policies

and practices. Whether an alternative to deferred accounting is appropriate for treatment of a particular cost will depend on the facts surrounding that cost. If, however, the Commission intends to consider the alternatives to deferred accounting in this proceeding, development of factual evidence or testimony is unnecessary to do so.

7. Do the Commission's deferred accounting practices and procedures ensure symmetrical treatment of deferrals for excess utility costs and deferrals for excess utility revenues?

The Commission's deferred accounting policies generally provide symmetrical treatment for deferrals of excess utility costs and revenues. However, the allocation of risks is asymmetrical, because the majority of deferred accounting requests relate to utility costs. Staff and Intervenors do not have the resources or access to information necessary to determine whether utility costs are declining, thereby increasing revenues. As a result, the policies applicable to deferred accounting should recognize the one-sided nature of the process. This issue can be addressed through written comments.

8. Should there be an overall cap on the amount of costs that a utility can defer in one year?

ICNU supports an overall cap on the amount of costs that a utility can defer in one year. This cap would be based on a percentage of the utility's gross revenues for the previous calendar year. Such a cap would provide an important limit on the use of deferred accounting. A cap also would prevent the "ballooning" of a deferral balance such as when PacifiCorp recorded approximately \$259 million in its deferred account in UM 995. Although utilities typically accept the risk and reap the reward of cost fluctuations between rate cases, deferred accounting provides an exception to that rule. Nevertheless, deferred accounting was not intended to provide the opportunity to recover large-scale costs incurred between rate cases. A

cap on the amount of costs that can be deferred in one year will ensure that only a limited amount of costs are eligible for deferral each year. In addition, it will require utilities to file rate cases when large cost increases occur rather than seeking to recover those costs through deferred accounting.

9. What must applicant show to demonstrate that a deferral under ORS § 757.259(2)(e) will either (a) minimize the frequency of rate changes or fluctuation of rate levels, or (b) match ratepayer benefits and costs?

The meaning of “minimize the frequency of rate changes or fluctuation of rate levels” and “match appropriately the costs borne by and benefits received by ratepayers” has been the subject of controversy in previous deferred accounting proceedings. Certain deferred accounting applications have attempted to justify the request on the basis that, without deferred accounting, the utility would be required to file a general rate case to collect the costs at issue. Such unsupported assertions are insufficient to demonstrate that the deferred account would minimize the frequency of rate changes under the statute. Utilities should not be permitted to justify authorization of a deferred account merely by asserting that the Commission must authorize the request in order to avoid the threatened rate case.

With respect to the matching of costs and benefits, the Commission authorized deferred accounting on this basis in Docket UM 246, in which PGE requested deferred accounting treatment for legal costs associated with litigation over a coal supply contract. Re PGE, OPUC Docket No. UM 246, Order No. 90-311 at 1 (Mar. 5, 1990). PGE agreed in that docket to limit its right to recover deferred legal expenses from customers to the extent that the company could demonstrate that customers benefited from those costs. Id. The Commission authorized PGE’s request, finding that “[s]ince any benefits from the deferred expenses will

accrue to future ratepayers, and since the legal expenses associated with such litigation are likely to be substantial, the commission finds that deferral of such expenses is appropriate.” Id. The Commission has subsequently described this use of deferred accounting “to allow future matching of costs with benefits expected to be created by a revised contract” as a “good example of appropriate use of the matching provision to authorize deferral of added costs” OPUC Docket No. UE 76, Order No. 92-1128 at 9. In other words, matching of costs and benefits means that deferred accounting is appropriate when present costs are going to result in some demonstrable benefit to customers in the future.

Determination of the meaning of the terms in ORS § 757.259(2)(e) is a matter of statutory interpretation. No factual development is necessary to address and resolve this issue.

10. What types of costs are eligible for deferred accounting (e.g. do the costs have to be extraordinary, unanticipated, nonrecurring, and/or discrete)?

Deferred accounting provides an exception to the rule that utilities accept the risk and reap the reward of cost fluctuations between rate cases. The Oregon Attorney General’s office found that without specific legislative authorization to engage in deferred accounting, the practice would be unlawful in Oregon because it would violate the rule against retroactive ratemaking. Or. Op. Att’y Gen. No. OP-6076 at 18 (Mar. 18, 1987). As such, the costs that should be eligible for deferred accounting are those that are authorized by statute.

ORS § 757.259(2) establishes two general categories of costs or revenues appropriate for deferral: 1) the specific costs or revenues listed in subsections (a)-(d) of ORS § 757.259(2); and 2) under ORS § 757.259(2)(e), “[i]dentifiable 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 has previously characterized the deferred accounting statute as follows:

ORS 757.259 allows this Commission to authorize the deferral of certain expenses for later incorporation in rates. We have previously construed that statute narrowly, and limited its application to the recovery of discrete expenses that might affect a utility’s earnings on a short-term basis. The statute cannot be used to authorize the deferral of general expenditures that a utility incurs in an ongoing and continuous manner.

Re PGE, OPUC Docket No. UE 115, Order No. 01-988 at 8 (Nov. 20, 2001) (internal citations omitted). As such, the use of deferred accounting should be limited in general.

The types of costs eligible for deferred accounting should be particularly limited with respect to the category of costs described in ORS § 757.259(2)(e). The costs deferred under this provision should be limited to extraordinary, unanticipated, and discrete costs. Indeed, the Commission has denied requests for deferred accounting under this section when the cause was “not extraordinary enough to justify deferred accounting.” Order No. 04-108 at 11. In short, ORS § 757.259(2)(e) was intended to allow recovery of costs that were the result of extraordinary circumstances that occur between rate cases, not to provide a mechanism for general cost recovery between rate cases. Under these circumstances, the Commission should adopt a policy that delineates that deferred accounting is appropriate for extraordinary and unanticipated costs.

Defining the types of costs that are eligible and appropriate for deferral can be addressed through written comments. As described above, if the proceeding is to be bifurcated, issues regarding the nature of deferred accounting should be addressed in the first phase of the

Docket. Nevertheless, written testimony sponsored by a witness and evidence on this topic is unnecessary.

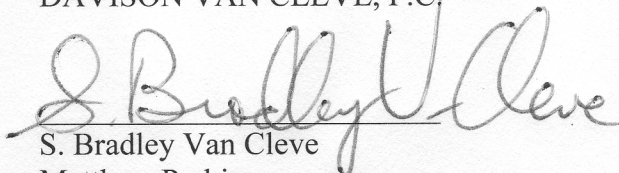
CONCLUSION

The Commission should adopt a full procedural schedule in this case that provides the opportunity for parties to address all substantive issues in two rounds of simultaneous comments. The investigation in this Docket involves examination of the Commission's deferred accounting policies and practices—it is not the forum to make fact-specific decisions regarding particular utilities. Under these circumstances, testimony sponsored by a witness with the opportunity for cross-examination is unnecessary. Fact-specific inquiries related to the circumstances of a particular deferred accounting request can be conducted in the proceeding related to that deferral. ICNU appreciates the opportunity to submit these initial comments and looks forward to addressing all of these issues in detail once the full procedural schedule is established.

Dated this 7th day of October, 2004.

Respectfully submitted,

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Of Attorneys for Industrial Customers of Northwest
Utilities

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that I have this day served the foregoing Opening Comments of the Industrial Customers of Northwest Utilities upon the parties listed below, listed on the official service list for Docket No. UM 1147, by causing the same to be mailed, postage-prepaid, through the U.S. Mail, as well as an electronic copy via email.

Dated at Portland, Oregon, this 7th day of October, 2004.


Ruth A. Miller

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