BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

UM 1147

In the Matter of	)
	)
PUBLIC UTILITY COMMISSION OF OREGON STAFF	)
	)
Request to open an investigation related to deferred accounting	)

REPLY COMMENTS

OF THE

CITIZENS' UTILITY BOARD OF OREGON

February 18, 2005

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I. Introduction

CUB's position in this docket is laid out in our opening comments, so our reply comments are primarily limited to reactions to other parties' opening comments. By way of introduction, we would like to reiterate that deferred accounting certainly has its use as a regulatory tool, but, as an exception to the prohibition on retroactive ratemaking, it should be used sparingly and only when circumstances warrant.

II. Comments

The primary issues appear to be Staff's proposed materiality guidelines and their recommendation that a utility's rate of return is not an appropriate interest rate for deferred accounts. The utilities put forward a number of arguments against Staff's and our recommendations, but none that were convincing to us, so we continue to support our earlier position.

A. Commission Is Exercising Its Authority In This Docket

Parties opposed to reining-in the recent use of deferrals attempt to portray guidelines and materiality tests as "self-imposing limitations" on the Commission's ability and/or authority to use deferred accounting. PacifiCorp/1. To the contrary, the Commission is exercising its discretion in this docket in reaction to the recent controversy over deferrals.

The Commission has, and will continue to have, broad authority in its discretion to use deferred accounting. There is nothing about creating a general framework for deferral applications that limits the Commission's ability to use deferred accounting to the full extent of ORS 757.259. From our perspective, clarification of the appropriate use of deferrals and the place of deferred accounting in regulation will only serve to reduce confusion, reduce inappropriate deferral applications, and allow the Commission and the parties to focus on those applications that genuinely warrant deferred accounting.

B. Open-Season & Symmetric Vs. Controlled & Asymmetric

We cannot help but notice that those parties who argue against any type of guidelines or materiality test for deferral applications also argue that deferrals are a symmetric tool, while those parties advocating for a curbed use of deferrals feel that deferred accounting gives utilities the upper hand. It is not without a touch of cynicism that we point out, if deferrals were as useful to customer groups as they are to utilities, we wouldn't be recommending guidelines and materiality tests.

C. Staff's Matrix Is Appropriate

Utilities seem desperate to discredit Staff's "deferred accounting materiality matrix," which makes their protestations seem self-serving. PacifiCorp/2. Staff's matrix is neither too rigid nor too nebulous; it was designed to provide a general framework within which the applicant, as well as the Commission, can asses the appropriateness of an application for deferral.

The event category "Commission-Approved" seemed to be confusing for the utilities, while being generally clear to customer groups.

> This "Commission-approved" exception swallows the rule. It tells you absolutely nothing about when the materiality test applies because in every case the Commission must approve a deferred accounting application.

PGE/Opening Comments 2005/15

Staff's category did not confuse us. Staff's intent for Commission-Approved was to encompass those events that stem from government and/or Commission actions. The government or Commission action would come first, then the deferral application. This category of events was not for Commission or government actions in response to a deferral application.

In other words, a government or the Commission would initiate an action which invited or anticipated a deferral, such as a tax change, and the deferral application would be filed in response to this circumstance. This allows for addressing public policy issues, tax changes, or government regulations without impacting a utility's return. For the most part, we see these uses of deferred accounting as relatively uncontroversial.

i. The Stochastic-Scenario Grey Area

PacifiCorp points out that there is a grey area between stochastic events and scenario events. The example the Company uses is that of hydro variation, which, under a normal range of circumstances is not sufficient for deferral, but under a wider range of circumstances might warrant a stochastic event deferral, while under extreme circumstances with other inter-relating factors might be eligible for a scenario deferral.

Though the Company's point may be theoretically valid, practically speaking, it is most likely moot, because any event involving stochastic or normalized variables that are so out-of-whack as to constitute a scenario event is likely to have cleared the higher materiality threshold anyway. This is not to suggest that there will never be disagreements between utilities and customer groups over the classification of a given deferral as stochastic or scenario, but Staff's matrix provides a framework within which to present arguments.

ii. Stochastic & Normalized

PacifiCorp pointed out that the word "stochastic" may have too narrow a definition for the category Staff envisioned. We certainly agree that the concept of stochastic, as PacifiCorp defines it, should be broadened to include those factors and variables which fluctuate over time and are normalized, one way or another, for ratemaking purposes. This includes the normalization of weather and loads, as well as the forward price curves used as the best estimate of future market prices. Perhaps PacifiCorp would be more comfortable if the category were renamed "Stochastic & Normalized".

D. Interest Rate

A utility has different costs for its long-term and short-term capital, and we agree with Staff that this can no longer be ignored. Staff's proposed solution is well-reasoned and thoughtful, and the process by which they arrived at their suggested interest rates seems reasonable and appropriate.

i. Interest Rate & Risk of Recovery

> There is no evidence in this docket or elsewhere regarding the relative risk of recovery of deferred accounts and how it compares with the risk of other utility investments. Second, the risk of recovery is irrelevant to determining the appropriate interest rate.

PGE/Opening Comments 2005/18

We did discuss the relative risk of deferred accounts compared to other utility investments in our opening comments at 3, though it seems to us that it goes without saying. Take a given utility expense with a known cost. If you put that cost into rates along with everything else, the utility may under-recover or over-recover the cost, because the load, upon which rates were based, may vary due to weather, economic circumstances, etceteras. However, if that cost is put into a deferred account, the utility will recover the entire cost, dollar for dollar, until the account has been completely amortized. Period. Suggesting that recovery of a deferred account is the same as recovery of any other utility investment is absurd.

Second, if the risk of recovery is irrelevant in determining an appropriate interest rate, why are a utility's return on equity and its cost of capital such contentious issues? Would PGE suggest to the rating agencies that the creditors' risk of recovery is irrelevant in the interest rate those creditors should charge PGE?

ii. Interest Rate & Amortization Period

In our opening comments we pointed out that the time-period over which a utility recovers a deferral should be considered in establishing an appropriate interest rate. Allowing a utility to earn its full rate of return on a deferred account allows the utility to profit from the spread between short-term interest rates and its rate of return. Customers pay the utility its rate of return, based on long-term cost of capital, while the company only has to pay short-term rates on its revolvers or other sources or short-term capital.

iii. Interest Rate & Short-Term Rates

> Utilities do not identify specific types of financial sources with particular financial needs. Rather, the utility's financial sources are collectively treated as a general source of funds, whose weighted average cost is used to determine its authorized cost of capital.

PGE/Opening Comments 2005/19

> The Commission has never sorted through PacifiCorp's investments in this manner and imputed lower returns than the Company's weighted cost of capital based upon the perceived low risk of recovery. … PacifiCorp's investments are not financed discreetly and instead rely on PacifiCorp's overall mix of debt and equity.

PacifiCorp/Opening Comments 2005/10

PGE and PacifiCorp seem to be arguing that one cannot separate out which financing goes to which expense, and that it is impossible to assign one particular source of capital to one particular expense. Therefore, it would be irrational and unfair to assign a short-term interest rate to a deferred account.

While there may be some theoretical truth to this, that is exactly the process we use to set a utility's rate of return in the first place. Short-term debt is removed from rate of return because it is presumed that long-term debt is what finances long-term, rate-based capital investment. This is done with the full knowledge that short-term capital is used for capital construction. If the Commission plans to use the utility's rate of return for everything, then it ought to include all sources of capital, including short-term, when calculating a utility's rate of return.

We would also like to point out that PGE's assertion that, "the utility's financial sources are collectively treated as a general source of funds, whose weighted average cost is used to determine its authorized cost of capital," is incorrect. A utility's short-term debt is NOT included in the weighted averaged when determining a utility's authorized rate of return.

E. PGE's 100 Meter Deferral Sprint

PGE's rapid-fire process for deferral applications is not appropriate. The Company proposes a 20-day deadline from the filing date for comments, and a 30-day deadline for the prehearing conference, by which time the parties must know whether a hearing will be necessary and whether they need discovery about the deferral item, mechanism, or amount. Especially recently, dockets have been filed one after another, and scheduling between them takes coordination. Such tight deadlines ignores the reality of multiple dockets, as well as holidays, vacations, and other responsibilities.

> For deferral applications in which no hearing is requested within the deadlines listed above, all factual claims in the application and any supplement are deemed true for the purpose of considering whether the deferral application should be approved.

PGE/Opening Comments 2005/21

Could PGE be suggesting that, once a utility has slipped past those deadlines, even the Commission can't question the information in the application? PGE's eagerness to rush deferrals through, plays into the Company's argument that deferred accounting should be left open and unfettered for its use.

F. Utility Misuse Of Deferrals Not A Failure To Compensate Utilities

Idaho Power and PacifiCorp both not-so-subtly suggest that a PCA would clear up this pesky deferral problem. Unfortunately, the utilities have failed to convince us that they need a general PCA or that the balance of risk traditionally shared with customers is entirely off-kilter. While there has been a fair amount of discussion about PGE's desire for a PCA in recent years, PGE is unique in Oregon in its short position. Neither Idaho Power nor PacifiCorp has filed a request for a PCA or presented evidence to support their perceived need for a PCA.

From our perspective, this pesky deferral problem stems from an overuse of deferrals by utilities to shift risk, as well as costs, onto customers without compensating customers for bearing that risk. We have become more vocal about deferrals, not because we feel that deferred accounting is a fundamentally bad idea, but because a number of recent deferrals have been either regulatorily inappropriate, misused as a catch-all utility recovery tool, or even frivolous.

III. Conclusion

Deferred accounting has its place in regulatory finance, but recent overuse of deferrals has highlighted a need to clarify the appropriate uses of deferred accounting.

Staff's proposals, both in regard to their materiality matrix and their interest rate recommendations, are well thought-out and provide a coherent framework within which the Commission and the parties can approach deferral applications.

Respectfully submitted,
February 18, 2005,

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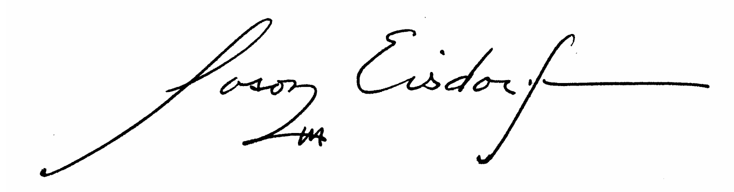
Utility Analyst
Citizens' Utility Board of Oregon

CERTIFICATE OF SERVICE

I hereby certify that on this 18th day of February, 2005, I served the foregoing Comments of the Citizens' Utility Board of Oregon in docket UM 1147 upon each party listed below, by email and U.S. mail, postage prepaid, and upon the Commission by email and by sending 6 copies by U.S. mail, postage prepaid, to the Commission's Salem offices.

Respectfully submitted,



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