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September 9, 2005

***Via Electronic and U.S. Mail***

Public Utility Commission  
Attn: Filing Center  
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Re: In the Matter of PORTLAND GENERAL ELECTRIC Application for a Hydro  
Generation Power Cost Adjustment Mechanism  
**Docket No. UE 165**

In the Matter of PORTLAND GENERAL ELECTRIC Application for Deferral of  
Costs and Benefits Due to Hydro Generation Variance  
**Docket No. UM 1187**

Dear Filing Center:

Enclosed please find an original and six (6) copies of the Opening Brief on behalf  
of the Industrial Customers of Northwest Utilities for filing in the above-referenced docket.

Please return one file-stamped copy of this document in the enclosed stamped  
envelope. Thank you for your assistance in this matter.

Sincerely,

/s/ Christian Griffen  
Christian W. Griffen

Enclosures

cc: Service List

## CERTIFICATE OF SERVICE

I HEREBY CERTIFY that I have this day served the foregoing Opening Brief on behalf of the Industrial Customers of Northwest Utilities upon the parties listed below by causing the same to be mailed, postage-prepaid, through the U.S. Mail.

Dated at Portland, Oregon, this 9th day of September, 2005.

*/s/ Christian Griffen*  
Christian W. Griffen

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**BEFORE THE PUBLIC UTILITY COMMISSION  
OF OREGON**

**UE 165/UM 1187**

In the Matter of	)	
	)	
PORTLAND GENERAL ELECTRIC COMPANY	)	OPENING BRIEF OF THE INDUSTRIAL CUSTOMERS OF NORTHWEST UTILITIES
	)	
Application for Approval of a Hydro Generation Adjustment Tariff.	)	
_____	)	
	)	
In the Matter of	)	
	)	
PORTLAND GENERAL ELECTRIC COMPANY	)	
	)	
Application for Deferral of Costs and Benefits Due to Hydro Generation Variance.	)	
_____	)	

The Industrial Customers of Northwest Utilities (“ICNU”) requests that the Public Utility Commission of Oregon (“OPUC” or the “Commission”) disapprove the stipulations between Portland General Electric Company (“PGE” or the “Company”) and OPUC Staff (collectively, the “Stipulation”),<sup>1/</sup> and reject the System Dispatch Power Cost Adjustment Mechanism (“SD-PCAM”) in Docket No. UE 165. Likewise, the Commission should deny PGE’s request for a deferred account in Docket No. UM 1187. PGE and Staff propose to

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<sup>1/</sup> PGE and Staff filed two separate stipulations in UE 165 and UM 1187, referred to collectively as the “Stipulation” in this Brief. Attached as Exhibit A to the Stipulation filed in UM 1187 is the UE 165 Stipulation. As such, citations to the “Stipulation” in this Brief refer to the UM 1187 stipulation, with specific reference to the UE 165 Stipulation attached as Exhibit A when appropriate. All other citations in this Brief refer to documents filed in UE 165 unless the citation indicates otherwise.

implement the SD-PCAM, which is a temporary cost recovery mechanism that would apply only in 2005 and 2006. The Commission should reject the SD-PCAM for the following reasons:

1. The SD-PCAM does not meet Staff's criteria for an acceptable power cost adjustment mechanism ("PCA"), because:
  - The SD-PCAM is a temporary, one-time mechanism. Both Staff and the Commission have previously determined that it is inappropriate to use a temporary mechanism to address stochastic risk, absent extraordinary circumstances;
  - The SD-PCAM is not limited to extreme events. The SD-PCAM's deadband is significantly smaller than the deadbands approved by the Commission for other PCAs and deferred accounts in recent years;
  - Staff has not determined that the SD-PCAM is revenue neutral. The evidence indicates that the SD-PCAM will result in a charge to customers for 2005 and that the mechanism likely overstates the costs of hydro variation; and
  - PGE and Staff appear to disagree on whether the SD-PCAM applies to direct access customers. The Stipulation does not address rate spread issues and does not specify how or when PGE will recover the deferred amounts.
2. The SD-PCAM more closely resembles a deferred account than a PCA, because it is a temporary measure that will not equitably allocate the burden of power cost variations over time. The Commission determined in UM 1071 that deferred accounting was inappropriate for hydro conditions similar to those in 2005, and there is no evidence that 2006 hydro conditions will justify rate relief. PGE's failure to satisfy the requirements set forth by the Commission in UM 1071 justifies rejecting the SD-PCAM.
3. The SD-PCAM is unlike any mechanism approved by the Commission in the past, and it requires substantial modifications to PGE's Monet power cost model that are incomplete and untested. The Stipulation provides no express opportunity to review those changes prior to implementing the mechanism.

If the Commission decides to adopt the SD-PCAM, the mechanism should not be applied retroactively to January 1, 2005. PGE's Application for deferred accounting in UM 1187 cannot lawfully serve as the basis for retroactive application of the SD-PCAM. The SD-PCAM

explicitly tracks changes in gas and electric prices, but PGE's deferred accounting application in UM 1187 requested deferral of costs that resulted from variations in hydro generation only. In addition, PGE has failed to prove that hydro conditions in 2005 warrant deferred accounting under the standard set out in UM 1071. The Commission cannot lawfully authorize deferral of costs for which PGE has not submitted a deferred accounting application and that do not otherwise meet the substantive standards for deferred accounting.

PGE described the Hydro Generation Adjustment ("HGA") tariff that it initially proposed in UE 165 as a "simple, ongoing, transparent, automatic adjustment clause that tracks the costs and value associated only with hydro generation assets and contracts." Advice No. 04-11 at 3 (May 18, 2004). The SD-PCAM departs dramatically from that proposal. The SD-PCAM is a temporary mechanism that requires complex and burdensome changes to PGE's power cost model, and it will track a broad array of power cost variations in a manner unlike any mechanism previously approved by this Commission. The fact that Staff and PGE request to implement the SD-PCAM in a year in which hydro conditions do not warrant rate relief only highlights the lack of a rationale supporting the Stipulation and the reasons why approving the mechanism would be unwise. ICNU urges the Commission to reject the SD-PCAM and the Stipulation. If, however, the Commission approves the SD-PCAM, it should apply the mechanism to only those costs incurred after the effective date of the Commission's order.

### **BACKGROUND**

On May 18, 2004, PGE filed a request for Commission approval of Schedule 128, which would implement a Hydro Generation Adjustment ("HGA") mechanism. Advice No. 04-

11 at 3.<sup>2/</sup> PGE stated that the HGA would track the “difference between actual hydro generation in MWh and the hydro generation assumption used to set rates in the [Resource Valuation Mechanism (“RVM”)] for the year.” Id. PGE proposed that this difference be “priced at the monthly average on- and off-peak Mid-C index price, adjusted for incremental wheeling costs and losses.” Id. In addition, PGE proposed a deadband of plus and minus \$2.5 million, and the tariff included no sharing mechanism outside of the deadband. Id.

On December 30, 2004, PGE filed a deferred accounting application in UM 1187, requesting approval of a deferred account through which the HGA could be implemented, effective January 1, 2005. Re PGE, OPUC Docket No. UM 1187, Application at 1 (Dec. 30, 2004). PGE stated that it would “calculate deferral amounts pursuant to the Application consistent with our proposed Schedule 128 [the HGA],” which was intended to track “the costs and value associated only with hydro generation assets and contracts.” OPUC Docket No. UM 1187, Application at 2; Advice No. 04-11 at 3. On January 21, 2005, PGE amended its Application, stating that the “principal purpose” of the Application was to implement the HGA effective January 1, 2005, but that the Company requested approval of a deferred account “irrespective of the ultimate outcome in UE 165.” Re PGE, OPUC Docket No. UM 1187, Amended Application at 1 (Jan. 21, 2004).<sup>3/</sup>

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<sup>2/</sup> At the same time PGE filed the HGA, the Company submitted a deferred accounting application (in UM 1157) to provide the opportunity to implement the HGA tariff as of May 18, 2004. On July 2, 2004, PGE withdrew its application in UM 1157.

<sup>3/</sup> PGE attached the proposed Schedule 128 to its Amended Application in UM 1187, and the tariff provided that the HGA cost variances would be calculated by multiplying the actual differences in hydro generation by Mid-C prices. Advice No. 04-11, Proposed Schedule 128 at Original Sheet No. 128-1. Under the HGA, if the 2005 hydro generation variance was zero, the balance of the deferred account would be zero as well.

On February 14, 2005, ICNU, the Citizens' Utility Board ("CUB"), and Staff submitted testimony in UE 165. ICNU and CUB opposed the HGA. ICNU/100, Falkenberg/4; CUB/100, Jenks-Brown/1. Staff also opposed the HGA, but proposed that the Commission adopt an "interim" PCA for calendar years 2005 and 2006 that: 1) included a deadband equal to the revenue requirement effect of plus and minus 250 basis points of ROE, which amounts to approximately \$40 million; and 2) did not provide inappropriate incentives for customers eligible for direct access. Staff/100, Galbraith/2-3, 26.

On April 11, 2005, PGE and Staff executed the Stipulation, which purports to resolve all issues in UE 165 and UM 1187. Stipulation at 1-2; Stipulation, Exhibit A, pp. 1-2. In the Stipulation, PGE and Staff request approval of the SD-PCAM, which the Stipulation describes as "a temporary cost variance mechanism to be applied to calendar years 2005 and 2006." Stipulation at 1. The SD-PCAM tracks the differences between "Base Power Costs" and "Updated Power Costs." "Base Power Costs" are the power costs in PGE's final RVM Monet run from the previous year, updated for cost of service loads and corresponding costs to reflect customer elections made in November. Id. at Exhibit A, p. 2. "Updated Power Costs" are determined by updating the Base Power Cost Monet run for:

- a) Actual hourly hydro generation;
- b) Actual market electricity prices using daily on-peak and off-peak prices from the Dow Jones Mid-Columbia Daily Electricity Firm Price Index and the hourly price shape from the Dow Jones Mid-Columbia Hourly Electricity Firm Price Index; and
- c) Actual market natural gas prices using the Platts GasDat daily index prices for Sumas, AECO, and Malin.

Id. at Exhibit A, pp. 2-3. In other words, “Updated Power Costs” will account for variation in hydro generation, electric prices, and gas prices. In addition, “Updated Power Costs” will not reflect PGE’s *actual* power costs during 2005 or 2006, but rather will reflect a projection of power costs produced by Monet.

The difference between “Base Power Costs” and “Updated Power Costs” is called the System Dispatch Cost Variance (“SDCV”). This amount will be deferred into an account subject to a \$15 million deadband when the SDCV is positive and a \$7.5 million deadband when the SDCV is negative. Id. at Exhibit A, p. 3. Customers will bear 80% of all variances outside of the deadband. Id. Recovery or refund of the SDCV is subject to an earnings test described in the Stipulation. Id. at Exhibit A, pp. 3-4. Refunds will occur only if PGE is exceeding its authorized rate of return.

The Stipulation also provides that the SD-PCAM is an automatic adjustment clause under ORS § 757.210 and requests that a tariff implementing the SD-PCAM take effect on the first day of the month following Commission approval. Id. at Exhibit A, p. 4. The Stipulation states that the terms of an “ongoing” power cost adjustment mechanism will be addressed in PGE’s next general rate case and that PGE will hire a consultant to evaluate and prepare a report to be completed by December 31, 2005, regarding the statistical distribution of net power costs. Id. at Exhibit A, p. 5. Finally, the Stipulation requests that the Commission approve PGE’s deferred accounting application in UM 1187 to allow the SD-PCAM to be implemented retroactively to January 1, 2005. Id. at Exhibit A, pp. 4-5.



## ARGUMENT

The Commission should reject the SD-PCAM because it is unnecessary and unjustified. Staff argued convincingly in UM 1071 that one-time deferred accounts are inappropriate to address the stochastic risk associated with ongoing power cost variability because authorizing temporary mechanisms in below-normal hydro years only results in utilities over-recovering net power costs over time. The SD-PCAM is such a temporary mechanism, and authorizing PGE to address power cost variations in 2005 and 2006 through the SD-PCAM will likely result in the over-recovery that Staff warned about in UM 1071. In addition, the SD-PCAM conflicts with Staff's previously-stated criteria for an acceptable PCA. Finally, the SD-PCAM does not satisfy the criteria for one-time power cost recovery that the Commission adopted in UM 1071.

Even if the Commission approves the SD-PCAM, the Commission should deny the request to authorize deferred accounting to implement the mechanism retroactively. 2005 hydro conditions fall well within the normal range of hydro variation that the Commission considered when it established PGE's power costs for 2005, and the Commission determined in UM 1071 that deferred accounting was inappropriate in such circumstances. Furthermore, the SD-PCAM will defer costs attributable to gas and electric price variations regardless of whether any hydro generation variation occurs, which goes far beyond the scope of PGE's application for deferred accounting in UM 1187. The Commission cannot lawfully authorize deferral of costs for which a valid application has not been submitted. As a result, using deferred accounting to implement the SD-PCAM, effective as of January 1, 2005, will result in unlawful retroactive ratemaking.

**A. The Commission Should Reject the SD-PCAM Because the Mechanism Does Not Satisfy Staff’s Criteria for PCAs**

Staff’s support for the SD-PCAM is puzzling given that the mechanism does not satisfy the criteria that Staff has used to evaluate power cost recovery mechanisms in this proceeding and in the past. In UM 1071, Staff explained that the Commission should not judge a hydro-related cost recovery mechanism according to whether it appropriately matched the costs and benefits of hydro generation based on a “snapshot” of conditions at one point in time.<sup>4/</sup> ICNU/401 at 2. The proper focus, according to Staff, was matching hydro-related costs and benefits over time. Id. Staff supported a permanent mechanism to achieve this goal:

[Staff] seeks an ongoing permanent allocation of the risks and rewards of hydro production. Our arguments in UM 1071 have consistently emphasized the need for a long-run inter-temporal matching of the benefits and costs of hydro production. We have consistently argued that a one-time deferral of above-average hydro costs is a temporary measure that creates the need for additional rate adjustments in the future to avoid a permanent mismatch between ratepayer benefits and costs and actual benefits and costs. One-time deferral is not an acceptable solution.

ICNU/402 at 7. Based on these concerns and others, Staff recommended denying PGE’s request for a deferred account to track deviations in hydro costs in 2003.

In UE 165, Staff assessed PGE’s proposed HGA according to whether it:

1) protected against extreme fluctuations in NVPC; 2) was revenue neutral; and 3) did not provide inappropriate incentives for customers eligible for direct access. Staff/100,

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<sup>4/</sup> Staff applied this criteria in the context of whether PGE’s application for deferred accounting in UM 1071 would “match appropriately the costs borne by and benefits received by ratepayers” under ORS § 757.259(2)(e). ICNU/401 at 2. Staff’s focus on the matching of costs and benefits over time, however, applies to all hydro-related cost recovery mechanisms, not just a deferred account.

Galbraith/10-12. As described below, the SD-PCAM does not meet the criteria applied by Staff in UM 1071 or in this Docket.

**1. The SD-PCAM Is a Temporary Mechanism That Will Result In Over-Recovery of Costs**

There is no dispute that the SD-PCAM is a temporary mechanism. The Stipulation itself describes the SD-PCAM as “a *temporary* cost variance mechanism to be applied to calendar years 2005 and 2006.” Stipulation at 1 (emphasis added). Staff described the SD-PCAM as a “temporary mechanism” in testimony and at the hearing as well. Staff/300, Galbraith/1; Hearing Transcript (“Tr.”) at 18:24-25 (Galbraith) (Aug. 9, 2005). Because the SD-PCAM is a temporary mechanism, rather than an ongoing mechanism that permanently allocates risks and benefits, it should be judged according to the standard adopted in UM 1071 for one-time deferred accounts.

In UM 1071, Staff stated that “stochastic risk, risk that is quantifiable and known in advance, is best addressed in general rate proceedings or through a permanent PCA mechanism.” ICNU/402 at 4. In Order No. 04-108, the Commission stated that it “agree[d] with Staff that risks normally included in modeling power costs (stochastic risks) are not appropriate for deferred accounting” and denied PGE’s application. Re PGE, OPUC Docket No. UM 1071, Order No. 04-108 at 9 (Mar. 2, 2004) (“Order No. 04-108”). In this proceeding, Staff has pointed to the fact that the SD-PCAM lasts for two years rather than just one as an “important consideration” in Staff’s support for a temporary mechanism because 2006 hydro conditions are unknown. Tr. 35:8-12 (Galbraith). This distinction is meaningless in terms of achieving the “long-run inter-temporal matching of benefits and costs” that Staff used to judge PGE’s request in UM 1071. ICNU/402 at 7. Regardless of whether the SD-PCAM lasts for one year or two, it

is a “temporary measure” that runs the risk of permanently mismatching the costs and benefits of hydro generation variation over time. ICNU/402 at 7. In this way, the SD-PCAM is more akin to a temporary deferred account with a pre-defined deadband and sharing mechanism than an ongoing PCA, because the SD-PCAM will only be in effect for 2005 and 2006.

In addition, although 2006 power costs remain somewhat uncertain, it is incorrect to conclude that PGE has no idea whether hydro conditions will deviate from normalized values. In July 2001, the parties to PGE’s last rate case entered into a stipulation concerning power costs. The stipulation provided for a Schedule 125C adjustment to reflect “reduced hydro generation from that available in the water year used to develop normalized power costs . . . over the period October 2001 through December 2002.” Re PGE, OPUC Docket No. UE 115, Order No. 01-777 at 18 n.24, Appendix D at 2 (Aug. 31, 2001). This shows that PGE has some knowledge regarding potential hydro conditions in 2006. In addition, it demonstrates how one-time deferrals can be used to game cost recovery. Presumably, PGE still has the ability to withdraw its request for a deferred account in this case. The flexibility to withdraw a filing allows a utility to withdraw a cost recovery mechanism if conditions improve, while allowing a request to go forward if adverse conditions prevail.

In a similar case, UE 137, PGE proposed a PCA mechanism, but later withdrew the filing, stating that it would “rely on traditional regulatory methods to address changes in net variable power costs [(“NVPC”)].” Re PGE, OPUC Docket No. UE 137, Order No. 02-675 at 1 (Oct. 1, 2002). PGE also filed, and then withdrew, applications for deferred accounting related to 2004 hydro conditions in UM 1128 and UM 1157. It is unclear whether PGE was gaming the system in these instances, but it clearly shows that the potential for such abuse exists.

The fact that PGE currently projects that a 2005 deferred account will result in a charge to customers only highlights Staff's admonition that authorizing a "one-time deferral and amortization of replacement power costs . . . results in above average costs and below average benefits being reflected in rates over time" unless additional rate adjustments that offset the charge to customers are authorized in the future. ICNU/401 at 4. Mr. Falkenberg provides an example that quantifies the potential for over-recovery. ICNU/300, Falkenberg/16-18. Approving the temporary SD-PCAM deferred account likely will result in a "permanent mismatch" of costs and benefits because: 1) PGE estimates that implementing the SD-PCAM in 2005 will result in additional costs for customers; and 2) there is no certainty that customers will receive a credit in 2006 due to above average hydro conditions or that the Commission will approve an ongoing PCA that is substantially similar to the SD-PCAM in 2007.

## **2. The SD-PCAM Is Not an Extreme Event Mechanism**

In the past, Staff has argued that PCAs should apply only to extreme events. Re PGE, OPUC Docket No. UE 137, Staff/100, Galbraith/1 (Aug. 16, 2002); ICNU/402 at 7. This requirement accomplishes two things. First, it recognizes that utilities should bear some risk of power cost variations between rate cases. Second, it incents the utility to control its costs.

The SD-PCAM is not limited to "extreme events." Staff has discussed a "large deadband" as way to design an extreme event PCA. Staff/100, Galbraith/11. The \$15 million/\$7.5 million deadband in the SD-PCAM is much less than the approximately \$40 million deadband that Staff proposed in UE 137 and in the interim PCA that Staff previously proposed in this Docket. Furthermore, it is smaller than the \$28 million deadband in PGE's UE 115 PCA and the \$35 million deadband in the PGE's 2001 power cost deferral. OPUC Docket No. UE

115, Order No. 01-777 at 19; Re PGE, OPUC Docket No. UM 1008/1009, Order No. 01-231 at Appendix A, p. 4 (Mar. 14, 2001). Finally, the \$15 million deadband is smaller than the deadband of 250 basis points of ROE discussed in UM 995, which the Commission used as a reference point to determine that the financial impact at issue in UM 1071 did not warrant deferred accounting.

Staff has argued that the smaller scope of costs included in the SD-PCAM justifies the small deadband, but the cost variations encompassed by the SD-PCAM belie Staff's claim. Staff/300, Galbraith/10. The "Updated" Monet run will include updated hydro generation, electric prices, and gas prices, all of which are significant components of overall NVPC. Indeed, hydro generation, electric prices, and gas prices were all included among the top five factors that PGE identified as contributing to the \$38 million (after deadband and sharing) balance of the Company's UE 115 PCA.<sup>5/</sup> Re PGE, OPUC Docket No. UM 1039, PGE/200, Niman-Hager-Tooman/2 (Jan. 30, 2004). Although actual loads and new contracts will be excluded from the update, it is unclear what the actual effect of excluding these factors will be. CUB argues that excluding load from the update may actually do more harm than good, because excluding actual load from the mechanism shifts the risk of variations in load to customers. CUB/200, Jenks-Brown/8-10, 18-19.

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<sup>5/</sup> Lost energy revenues due to reduced load was also in the top five factors contributing to the UE 115 PCA balance; however, that amount was so significant because load projections had failed to account for the load loss that occurred due to PGE's high rates that took effect in UE 115. OPUC Docket No. UM 1039, PGE/200, Niman-Hager-Tooman/2. After reviewing the results of the UE 115 PCA, Staff concluded that including the costs of load adjustments in a PCA was inappropriate. OPUC Docket No. UE 137, Staff/100, Galbraith/1.

**3. PGE and Staff Have Not Demonstrated That the SD-PCAM Is Revenue Neutral**

There is no evidence that the SD-PCAM meets Staff's revenue neutrality criteria.

The revenue neutrality requirement protects customers from over-recovery of power costs over time. Staff has indicated that it will be unable to analyze whether the SD-PCAM is revenue neutral until PGE develops its expected value power cost modeling. Tr. 42:6-23 (Galbraith).

Regardless of whether the SD-PCAM ends up being revenue neutral during 2005 and 2006, the mechanism will likely overestimate the actual power cost variance during that period. ICNU/300, Falkenberg/30. This will occur because the mechanism is based on simulated rather than actual power costs. Even though PGE's actual power cost variance for January to March 2005 was \$7 million, PGE has calculated that the SD-PCAM would defer \$11.1 million during that period. Id. The combined effect of using updated gas costs and Monet simulations to determine the dispatch of gas plants could lead to anomalous results. As Mr. Falkenberg pointed out, in the past, Monet has been a poor predictor of gas-fired generation. Id. at Falkenberg/32.

In addition, as CUB pointed out, even if hydro generation is below normal and PGE acts prudently to replace the lost generation, the SD-PCAM will not take into account the cost savings that result from the utility's actions. CUB/200, Jenks-Brown/14-15. Approving the SD-PCAM for 2005 when the results are largely known will likely result in customers bearing above average hydro costs over time. The SD-PCAM will only increase that disparity by overestimating the power cost variances.

**4. PGE and Staff Have Not Agreed Whether the SD-PCAM Applies to Direct Access Customers**

Staff's third PCA criterion is that a PCA should not create adverse incentives for customers eligible for direct access. Staff/100, Galbraith/12-13. According to Staff: "[t]he ability of the customer to disconnect their annual energy expense from regulated cost-of-service ratemaking is the primary benefit of these options. Applying a PCA adjustment rate to the programs eliminates this benefit." Id. at Galbraith/20. The Stipulation does not address the applicability of the SD-PCAM to direct access customers, and it is unclear whether Staff and PGE agree on this point.<sup>6/</sup> Tr. 43:5-16 (Galbraith). Staff previously has proposed that PCAs not apply to direct access customers, and Staff's proposed "interim" PCA would have applied to cost-of-service customers only. Staff/100, Galbraith/26. PGE, on the other hand, has supported applying PCAs to direct access customers and proposed that the HGA apply to customers receiving direct access service or paying a market-based rate. PGE/700, Kuns/2-3.

It is unclear whether Staff and PGE agree on the applicability of the SD-PCAM. Staff's position remains unchanged for the time being, although Staff's witness indicated that Staff would determine its position if the issue comes before the Commission. Tr. 43:5-16 (Galbraith). PGE has given no indication that its position has changed, and Staff's witness testified that he did not know the Company's position. Id. at 44:4-8 (Galbraith). As such, even if the Commission approves the Stipulation, this critical issue will remain unresolved for PGE's largest customers.

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<sup>6/</sup> The Stipulation does not address the rate spread pursuant to which PGE would charge or credit customers under the SD-PCAM. In fact, the Stipulation does not specify when or how deferred costs will be recovered.



**B. The SD-PCAM Rests on Substantial Modeling Changes That the Stipulation Provides No Express Opportunity to Review**

The SD-PCAM differs significantly from other PCAs in that it determines the power cost variances to be charged or credited to customers according to the difference between a computer model run that produced PGE's baseline power costs and a computer-modeled simulation of the Company's updated power costs. The SD-PCAM does not compare PGE's base power costs to the Company's actual power costs. There is no evidence that the SD-PCAM approach is viable or that the modeling changes will work as expected. Further, the Stipulation provides no express opportunity to review the model changes or the results of its calculations prior to the SD-PCAM balance being included in rates.

Staff has indicated that temporary implementation of the SD-PCAM and the study of the distribution of NVPC provided for in the Stipulation will set the stage for adopting a permanent PCA in PGE's upcoming rate case, which provides a basis to overlook the SD-PCAM's flaws. However, the SD-PCAM represents a fundamental change in the manner in which PGE determines the power costs it collects from customers, and the uncertainty of the events anticipated by Staff justify rejecting the SD-PCAM.

**1. The Timing of the Agreement on the SD-PCAM Has Provided Little Opportunity for Meaningful Review in This Proceeding**

The agreement on the SD-PCAM came late in the UE 165 schedule, giving other parties only a limited opportunity to review the proposed mechanism prior to the request for Commission approval. ICNU/300, Falkenberg/24. No party had proposed or discussed a mechanism like the SD-PCAM in UE 165 prior to the agreement in the Stipulation. *Id.* at Falkenberg/23. PGE's HGA was a relatively simple mechanism that focused on the value of

hydro generation variations only. Staff's proposed PCA was broader, but it still resembled the PCAs addressed in previous proceedings, and it did not make use of a new methodology or require substantial changes to Monet. The SD-PCAM's model-based methodology is unlike either of these approaches. As a result, the Stipulation actually raised as many questions as it resolved, because the agreement on the SD-PCAM marked the beginning of PGE's efforts to modify the Monet model. Getting answers to those questions was impossible, however, because, as PGE's responses to many of ICNU's discovery requests about the SD-PCAM demonstrate, the Company has "not completed the modifications necessary to implement the stipulation." ICNU/302, Falkenberg/2.

**2. The Stipulation Provides No Express Opportunity to Review the Model Changes Prior to Amortization of the SD-PCAM Balance**

The problem with the lack of review of the SD-PCAM in this proceeding is only compounded by the fact that the Stipulation does not provide an express opportunity to review the changes to the model or the calculation of the amounts to be charged or credited to customers prior to those amounts being included in rates. In fact, the Stipulation designates the SD-PCAM as an automatic adjustment clause, which means that rate changes can take effect under the mechanism without the full process that accompanies most tariff filings. Stipulation at Exhibit A, p. 4. ORS § 757.210 defines an "automatic adjustment clause" as:

[A] provision of a rate schedule which provides for rate increases or decreases or both, without prior hearing, reflecting increases or decreases or both in costs incurred or revenues earned by a utility and which is subject to review by the commission at least once every two years.

In addition, the deferred accounting statute provides:

Unless subject to an automatic adjustment clause under ORS 757.210(1), amounts described in this section shall be allowed in rates only to the extent authorized by the Commission in a proceeding under ORS 757.210 to change rates and upon review of the utility's earnings at the time of application to amortize the deferral.

ORS § 757.259(5). In other words, when PGE seeks to amortize any SD-PCAM balance, there is no requirement to hold a hearing or provide any other opportunity to review the calculation of the power cost variances or the substantial model changes necessary to implement the Stipulation. The lack of ability to conduct discovery and provide testimony regarding a completed SD-PCAM in this proceeding means that approval, implementation, and amortization of the power cost variances under the mechanism could occur with an unprecedented lack of review.

PGE has argued that concerns about the lack of review associated with the mechanism are unfounded because “[a]t a minimum, amortization of any collection or refund under the SD-PCAM will require a tariff filing and, thus, trigger all of the statutory and Commission processes pertaining to tariff filings.” PGE/1100, Lesh-Tinker/19-20. First, PGE’s claim is inconsistent with designation of the SD-PCAM as an automatic adjustment clause. As described above, one of the primary purposes of an automatic adjustment clause is to allow changes to rates under the clause *without* all of the processes pertaining to traditional tariff filings. See ORS § 757.210. Although PGE may file a tariff to recover the SD-PCAM deferrals, the statutes provide for authorization of such a tariff “without prior hearing” or a “proceeding under ORS 757.210 to change rates.” ORS §§ 757.210, 757.259.

Second, PGE's claim conflicts with the approvals requested in the Stipulation. The UE 165 Stipulation requests that a tariff implementing the SD-PCAM take effect on the first day of the month following Commission approval, and the UM 1187 Stipulation requests "a Commission order allowing such calculation and *amortization* [of cost variances] from and after January 1, 2005, to the effective date of the implementation of the requested temporary cost variance tariff in UE 165." Stipulation at Exhibit A, p. 4; Stipulation at 2 (emphasis added). The dual approvals requested in the Stipulation contradict PGE's claim that a tariff filing will be made to amortize amounts incurred in 2005.

**3. The Risks of the Untested Results Under the SD-PCAM Outweigh the Benefit of a Study of the Distribution of PGE's NVPC**

Staff has indicated that one of the reasons it has agreed to a mechanism that does not meet its previously announced PCA criteria is because the Stipulation requires PGE to study expected value power cost modeling and develop a distribution of PGE's NVPC. Staff/300, Galbraith/11. The Stipulation provides that PGE will hire a consultant for the purpose of evaluating the statistical distribution of net power, at a cost of up to \$100,000. Stipulation at Exhibit A, p. 5. Staff hopes to use this study to develop a permanent PCA in PGE's upcoming rate case.

Staff testified that studying improvements in power cost modeling is one reason for authorizing a "temporary mechanism;" however, subjecting customers to the risk of millions of dollars of power cost deferrals seems to far outweigh the benefit of a \$100,000 study. Staff/300, Galbraith/11. Staff anticipates that a permanent PCA will be implemented as part of PGE's next rate case based on the knowledge gained from the SD-PCAM, but there is no assurance that this will occur. The Stipulation itself provides that "Staff and PGE reserve the

ability to accept or reject the opinion or work product of the consultant for use in ratemaking, including in PGE’s next general rate case.” Stipulation at Exhibit A, p. 5. More importantly, the testimony supporting the Stipulation states that Staff and PGE “disagree on the appropriateness and feasibility of developing expected value power costs.” Staff-PGE/100, Galbraith-Tinker/7. As a result, even if the consultant’s study yields results, PGE likely will oppose the use of expected value power cost modeling to develop a PCA in the next rate case.

If the Commission does wish to implement a mechanism such as the SD-PCAM, the best proceeding in which to do so is the general rate case that PGE is expected to file before the end of the year. Staff indicated in UM 1071 that a PCA should not be implemented outside of a general rate case.<sup>2/</sup> ICNU/401 at 4. A general rate case will provide the opportunity to fully examine the significant changes that the SD-PCAM requires before implementing a mechanism. Furthermore, a general rate case is a more appropriate proceeding in which to determine whether a PCA is justified, because the Commission has the opportunity to review all of the utility’s operations and make appropriate adjustments to ROE, rather than conducting an isolated view of power costs. Finally, since normalized power costs include hydro variability, the Commission should consider whether to change the manner in which hydro costs are reflected in rates prior to adopting a hydro-based PCA.

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<sup>2/</sup> At the hearing, Staff’s witness stated that the recommendation that a PCA only be implemented with a base rate change was specific to the mechanism that Staff was proposing at that time. Tr. 23:8-15 (Galbraith). However, Staff’s comments in UM 1071 discussed the recommendation in general terms of implementing an “automatic adjustment clause,” not just the specific mechanism supported by Staff. ICNU/401 at 4.

**4. The RVM Already Provides Significant Protection Against Gas and Electric Price Variations**

Authorizing the SD-PCAM also is inappropriate because it would provide PGE an additional mechanism to insulate the Company from the risk of fluctuations in gas and electric prices. Although utilities normally manage and receive the risks and benefits of such cost variations between rate cases, PGE already has a mechanism in place that provides unique protections against annual variations in gas and electric costs. Each year, PGE resets its NVPC under the annual adjustment to the RVM in Schedule 125. The annual adjustment to the RVM allows PGE to update costs related to: 1) applicable resources; 2) Company market power purchases; 3) costs of fuel and transportation; 4) hydro operating constraints imposed by governmental agencies; 5) market power prices (including transmission); 6) transmission and ancillary services; and 7) changes in its retail load forecast. Although PGE does not update its forecast hydro generation under the RVM, PGE's NVPC include normalized hydro conditions based on 69 years of hydro data, which account for a wide range of hydro variation. The ability to reset NVPC annually creates an extraordinary cost recovery advantage for PGE and insulates the Company from a significant amount of risk. To authorize the SD-PCAM in addition to the annual update to PGE's power costs each year under the RVM would shift an unacceptable amount of risk to customers.

**C. Authorizing Deferred Accounting to Implement the SD-PCAM for 2005 Conflicts with the Commission's Decision in UM 1071**

As discussed above, because the SD-PCAM is a temporary mechanism, it is more similar in nature from a risk allocation standpoint to a one-time deferred account than an ongoing PCA. In addition, PGE and Staff specifically request that the Commission authorize deferred

accounting in UM 1187 to implement the SD-PCAM retroactively in 2005. The Commission's decision in UM 1071 demonstrates that 2005 hydro conditions do not justify deferred accounting. Therefore, the Commission should reject the SD-PCAM or, at a minimum, not apply the mechanism retroactively. If PGE's UM 1187 Application does not satisfy the requirements for deferred accounting, then it cannot serve as the basis for retroactive application of the SD-PCAM.

**1. Order No. 04-108 Establishes the Framework to Examine PGE's Deferred Accounting Application**

In Order No. 04-108, the Commission adopted a framework to evaluate whether it would approve PGE's request to defer costs related to variations in 2003 hydro generation. Order No. 04-108 at 8-9. The Commission stated that it evaluates a deferred accounting application according to whether it: 1) warrants an exercise of the Commission's discretion; and 2) fits 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.

With respect to the type of event that caused the request for deferral, the Commission distinguished "stochastic" risks from "scenario" risks. Id. Stochastic risks are those that are subject to prediction or quantification and are capable of being modeled in rates. Id. at 8. Scenario risks, on the other hand, are not subject to quantification or prediction. Id. at 8-9.

The Commission considered the magnitude of the event's effect in terms of the financial impact on the utility. For stochastic risks, the event must have a "substantial" financial impact on the utility. Id. at 9. For scenario risks, the financial impact must be "material." Id.

The Commission denied PGE's application in UM 1071 using this framework. The Commission found that hydro variability had been included in the normalization process used to establish PGE's base rates and that the 2003 hydro conditions represented a 1 in 4.5 year hydro event. Id. The Commission deemed this type of hydro variability a "stochastic" risk and found that the PGE's request was "not extraordinary enough to justify deferred accounting." Id.

The Commission also found that the financial impact of the "excess hydro costs [was] not significant enough in [UM 1071] to warrant a deferral." Id. PGE claimed that the impact of 2003 hydro conditions was \$31.6 million, or 172 basis points of ROE, which the Commission noted was "well short of the 250 basis points of [ROE] within which we allowed no recovery in UM 995."<sup>8/</sup> Id. Staff had estimated that the excess cost of 2003 hydro variation was about \$17.5 million. The Commission determined that all of these impacts were "not significant to warrant a deferral." Id. at 11.

**2. 2005 Hydro Conditions Represent a Stochastic Risk That Was Taken Into Account When the Commission Set PGE's Power Costs in UE 161**

The hydro conditions that PGE and Staff claim justify deferred accounting in 2005 are almost identical to those that the Commission determined were insufficient to justify deferred accounting in UM 1071. Staff's witness admitted at the hearing that 2005 hydro conditions were contemplated in establishing base energy rates for 2005, and that 2005 hydro

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<sup>8/</sup> The Commission also pointed out that it had approved an equivalent deadband for PGE and Idaho Power in power cost deferrals in the past. Order No. 04-108 at 9 n.7.



conditions represent a stochastic risk. Tr. 36:5-14, 37:4-6 (Galbraith). In addition, PGE's evidence demonstrates that, as of April 8, 2005, hydro conditions in 2005 represented only a one in five-year event, and the Company has acknowledged that hydro conditions have improved substantially since that time. OPUC Docket No. UM 1187, PGE/100, Dahlgren-Tinker/3; ICNU/300, Falkenberg/19-20; PGE/1100, Lesh-Tinker/21. The Commission determined in UM 1071 that costs resulting from stochastic risks and hydro variations of this magnitude do not justify deferred accounting. Order No. 04-108 at 8-9.

**3. 2005 Hydro Conditions Have Not Had a Substantial Financial Impact on PGE**

The financial impact of 2005 hydro conditions on PGE also does not justify deferred accounting. As of June 23, 2005, PGE estimated that the total impact of 2005 hydro conditions would be \$17.5 million prior to application of SD-PCAM deadband and sharing mechanism. PGE/1100, Lesh-Tinker/21-22. This would result in a charge to customers of \$1.97 million once the deadband and sharing are applied. Id. The \$17.5 million financial impact of 2005 hydro conditions is exactly the same as the Staff estimate that the Commission declared was "not significant enough to warrant a deferral" in UM 1071. Order No. 04-108 at 11.

PGE has argued that the multi-year impact of hydro variability justifies authorizing deferred accounting for 2005, even if hydro conditions similar to those in 2005 were considered when setting base energy rates in UE 161. OPUC Docket No. UM 1187, Amended Application at 2-3. PGE's 2004 Results of Operations report, however, reflected that the Company earned a 10.28% ROE in 2004 and a normalized ROE of 11.66%. CUB/200, Jenks-Brown/30 n.5. In UM 1071, PGE had projected that its 2003 ROE would drop to 8% without a deferred account. Order No. 04-108 at 9. In denying PGE's application, the Commission noted

that an 8% ROE was “far from a dire figure.” Id. PGE’s financial results from 2004 do not reflect a multi-year financial impact that justifies deferred accounting.

**4. Approval of a Deferred Accounting for 2005 Will Not Appropriately Match Costs and Benefits Under ORS § 757.259**

The other aspect of the deferred accounting framework described by the Commission in Order No. 04-108 is whether the application is consistent with ORS § 757.259. Order No. 04-108 at 7. PGE’s Amended Application in UM 1187 requested a deferred account pursuant to ORS § 757.259(2)(e), in order to “match appropriately the costs borne by and benefits received by ratepayers.” OPUC Docket No. UM 1187, Amended Application at 3. On its face, the SD-PCAM does not match costs and benefits, because the cost of reduced hydro will be recovered after it is incurred. In addition, the record in this proceeding demonstrates that approving PGE’s deferred accounting application will result in a “mismatch” of costs and benefits instead of the “long-run inter-temporal matching of the benefits and costs of hydro production” that Staff has stated a hydro-related cost recovery mechanism should seek to achieve. ICNU/402 at 7. The Commission previously has stated that it will “not grant deferral unless it is clearly within the reach of the statute.” Re PacifiCorp, OPUC Docket No. UE 76, Order No. 92-1128 at 8 (Aug. 4, 1992). The Commission should deny the request for a deferred account to implement the SD-PCAM, because the temporary mechanism will result in a mismatch of the costs and benefits of PGE’s hydro production to ratepayers over time.

**D. Implementing the SD-PCAM Effective January 1, 2005, Would Violate the Rule Against Retroactive Ratemaking**

PGE’s deferred accounting application in UM 1187 should be denied because approving a deferral of 2005 costs according to the SD-PCAM methodology would violate the

rule against retroactive ratemaking. PGE's deferred accounting application was originally intended to implement the HGA proposed by the Company for 2005, which PGE described as "focused and narrow, *only* encompassing variations from PGE's hydro generating resources and hydro supply contracts." Advice No. 04-11 at 4 (emphasis added). The SD-PCAM, on the other hand, will defer not only those costs that PGE theoretically might incur as a result of hydro generation variation but also costs related to gas and electric price variation regardless of whether any hydro generation variation occurs. As a result, PGE and Staff now seek authorization to defer costs related to variations in: 1) hydro generation; 2) electric prices; and 3) gas prices, based on a deferred accounting application that requested authorization to defer the costs of hydro generation variation only.

PGE uses Monet to establish its NVPC each year in the RVM proceeding; thus, the model already includes substantial amounts of gas and wholesale power purchases. When PGE updates gas and electric prices for purposes of the SD-PCAM, however, Monet will automatically reprice all of these gas and wholesale power purchases from the RVM levels. ICNU/300, Falkenberg/9. The amount by which the purchases in the Updated Power Cost run differ from those in the Base Power Cost run will be included in the SD-PCAM deferred account balance. As a result, even if hydro conditions are normal, the Updated Power Cost Monet run will differ from the Base Power Cost Monet run and the SD-PCAM will record a deferral balance. PGE and Staff do not dispute that the SD-PCAM could produce this result.<sup>2/</sup> The fact that the HGA applied only to hydro costs, while the SD-PCAM also includes gas and electric

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<sup>2/</sup> Staff testified that "[e]ven if normal hydro conditions were to actually occur, the MONET update methodology could still produce a positive, or negative, SDCV due to changes in market energy prices." Staff/300, Galbraith/6.

costs, could have a significant impact on customers. PGE acknowledges that hydro conditions have improved since the UM 1187 application; however, it is common knowledge that wholesale gas and electric prices have increased dramatically in the wake of Hurricane Katrina.

As described below, deferred accounting is a limited statutory exception to the rule against retroactive ratemaking. It is unlawful to defer any costs without explicit Commission authorization, and the Commission lacks authority to approve deferred accounting applications that do not meet the substantive and procedural requirements of ORS § 757.259. PGE never submitted an application that requested deferral of costs related to gas and electric price variations. Under these circumstances, even if the Commission approved the SD-PCAM going forward, it would be unlawful to record in the UM 1187 deferred account all costs that would have been deferred under the SD-PCAM since January 1, 2005.

**1. Retroactive Ratemaking Prohibits Including Past Costs or Revenues in Future Rates**

The Commission generally sets rates on a prospective basis. See Re US West Communications, OPUC Docket No. UT 135, Order No. 97-180 at 3-5 (May 22, 1997). Once new rates go into effect, “[u]tilities typically bear the risk for changes in normal operating expenses between rate cases.” Re PacifiCorp, Docket Nos. UM 995/UE 121/UC 578, Order No. 01-420 at 4 (May 11, 2001). If utility costs increase or decrease between rate cases, the rule against retroactive ratemaking prevents the Commission from adjusting future rates “retroactively” to reflect those past costs. OPUC Docket No. UT 135, Order No. 97-180 at 5.

The Commission has described the principle behind the rule as follows:

From the customer’s viewpoint, the principle underlying the prohibition against retroactive ratemaking is that the customer should know what a utility service costs him at the time he takes it.

The posted tariff on the day of service represents a contract between the customer and the utility. The customer should not expect to pay more and the utility should not expect to get less.

Re PGE, OPUC Docket No. UM 989, Order No. 02-227 at 8 (Mar. 25, 2002) (quoting Testimony of Commissioner Charles Davis on HB 2145, Mar. 21, 1987, at 3). The Washington Utilities and Transportation Commission (“WUTC”) has stated that the “evil in retroactive ratemaking . . . is that the consumer has no opportunity prior to receiving or consuming the service to learn what the rate is or to participate in a proceeding by which the rate is set.” WUTC v. Puget Sound Energy, WUTC Docket No. U-81-41, Sixth Supp. Order at 17-18 (Dec. 19, 1988). The Commission has described the rule against retroactive ratemaking as one of the “cornerstones of Oregon regulatory law.” OPUC Docket No. UM 989, Order No. 02-227 at 8.

**2. Deferred Accounting Provides a Narrow Exception to the Rule Against Retroactive Ratemaking If Certain Requirements Are Met**

In 1987, the Oregon Attorney General issued an opinion stating that, without specific statutory authorization, deferred accounting was unlawful in Oregon because it violated the rule against retroactive ratemaking. Or. Op. Att’y Gen. No. Op-6076 at 10 (Mar. 18, 1987). The legislature subsequently passed the deferred accounting statute, ORS § 757.259, which provides a legislative grant of authority for the Commission to engage in retroactive ratemaking under specific circumstances. OPUC Docket No. UM 989, Order No. 02-227 at 9. Given that the Commission’s authority to approve what would otherwise be an unlawful practice is limited to that provided by the statute, the Commission has construed its authority narrowly:

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, Docket No. UE 115, Order No. 01-988 at 8 (Nov. 20, 2001) (internal citations omitted).<sup>10/</sup> In addition, as described above, the Commission does “not grant deferral unless it is clearly within the reach of the statute.” OPUC Docket No. UE 76, Order No. 92-1128 at 8.

**3. A Deferred Accounting Application Must Identify The Costs That a Utility Seeks To Defer**

Any request for deferred accounting must be made by an application that identifies the specific costs at issue. ORS § 757.259(2) provides that the Commission may authorize deferral of amounts “[u]pon application of a utility or ratepayer or upon the commission’s own motion . . . .” In addition, ORS § 757.259(4) provides that the Commission may only authorize deferrals “beginning with the date of the application.”

PGE filed its application in UM 1187 under ORS § 757.259(2)(e), which provides that a deferred account may only be authorized for “identifiable” utility expenses or revenues, indicating that the costs to be deferred should be identified in the application. Without a requirement that the application for deferred accounting specify the costs being deferred, utilities could file annual generic requests for deferred accounts and then selectively seek recovery of cost variations. As noted above, deferred accounting cannot be used to recover ongoing general expenditures. OPUC Docket No. UE 115, Order No. 01-988 at 8.

The OPUC rule governing deferred accounting implements this requirement by dictating that each application for deferred accounting shall include a “description of the utility

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<sup>10/</sup> In addition, the statute itself authorizes the Commission to permit deferred accounting only for specific types of costs (ORS § 757.259(1)-(2)), for a limited time period (ORS § 757.259(3)), and in limited amounts (ORS § 757.259(5)-(7)).

expense or revenue for which deferred accounting is requested.” OAR § 860-027-0300(3). The rule also requires that a utility that requests deferred accounting provide all parties in that utility’s last general rate case with a written notice of the application that also contains a “description of the utility expense or revenue for which deferred accounting is requested.” OAR § 860-027-0300(6).

The requirements of the ORS § 757.259 and OAR § 860-027-0300 serve an important purpose in the authorization for deferred accounting. Both the application and the notice provide “notice” to customers that the utility may seek to recover in rates certain costs or revenues for which recovery would not otherwise be permitted. As such, both the filing of the application and the description of the costs in that application are important because the application: 1) establishes the date upon which deferrals may commence; 2) establishes the scope of the costs that may be deferred; and 3) provides notice to customers of the filing and the amount and nature of the costs at issue.

#### **4. Retroactive Approval of the SD-PCAM Would Result in Retroactive Ratemaking**

In UT 135, the Commission denied US West Communications’ (“USWC”) application for approval of an Interconnection Cost Adjustment Mechanism (“ICAM”), finding that the “operation of the ICAM would constitute retroactive ratemaking [and did] not fit any of the statutory exceptions that authorize retroactive ratemaking.” OPUC Docket No. UT 135, Order No. 97-180 at 12. The ICAM would have recovered three categories of costs that USWC claimed it would incur to implement the Telecommunications Act of 1996: 1) costs incurred prior to filing the application; 2) costs incurred after the filing; and 3) costs that were unanticipated at the time the ICAM is approved. *Id.* at 4. In denying USWC’s request, the

Commission unequivocally stated that “there is no reasonable claim for costs incurred prior to the date the application was filed or for cost categories discovered after the ICAM is approved.”

Id. at 4.<sup>11/</sup>

The Commission also rejected USWC’s argument that the Commission could implement the ICAM by authorizing deferred accounting under the deferred accounting statute applicable to telecommunication utilities, ORS § 759.200. The Commission found that ORS § 759.200 did not permit deferral of the cost categories included in the ICAM and specifically pointed out that “[e]ven if ORS 759.200 did apply, USWC ha[d] not applied for deferred accounting under ORS 759.200(3).”<sup>12/</sup> Id. at 9 n.7. As such, Order No. 97-180 demonstrates that including past costs that do not meet the substantive and procedural requirements of the deferred accounting statute in a cost recovery mechanism constitutes retroactive ratemaking.

Approval of the SD-PCAM deferred account would violate the rule against retroactive ratemaking for the same reasons identified in UT 135. The SD-PCAM would defer costs related to gas and electric price variation that were not identified in PGE’s Application and for which no subsequent application was filed. In UT 135, the Commission determined there is no “reasonable claim” for such costs.<sup>13/</sup> Id. at 4. In addition, the Commission’s decision in UT

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<sup>11/</sup> The “application” referred to in Order No. 97-180 was the application for the ICAM itself, not an application for deferred accounting; however, the retroactive ratemaking principle that the Commission applied to costs incurred before the filing of USWC’s application in UT 135 applies with equal force to PGE’s deferred accounting Application in UM 1187.

<sup>12/</sup> The Commission noted that the costs eligible for deferral under ORS § 759.200 are more limited than those under ORS § 757.259. OPUC Docket No. UT 135, Order No. 97-180 at 9. However, the requirements that an application be filed and that deferral may be authorized beginning with the date of application are the same in ORS §§ 757.259 and 759.200.

<sup>13/</sup> Authorizing recovery of these costs would also violate ORS § 757.259(4), which provides that the Commission may authorize deferral of the costs in the application “beginning with the date of the application.”



135 that it would constitute retroactive ratemaking to recover through the ICAM costs that were unanticipated when the application was filed indicates that it is improper to expand the category of costs for which recovery is requested under an application without amending the application. In this case, despite the fact that the SD-PCAM plainly encompasses a broader scope of costs than just those that result from hydro generation variation, PGE did not amend its application.

The basic principles regarding retroactive ratemaking confirm that retroactively authorizing the SD-PCAM is unlawful. Because PGE did not submit an application to defer costs related to variations in gas and electric prices in 2005, customers have had no “notice” that these amounts might be included in future rates. The formal “notice” that OAR § 860-027-0300 required PGE to serve on parties in the Company’s last rate case did not provide actual notice that the Company was seeking to defer any costs that were not the result of a hydro generation variance. Furthermore, PGE’s Application in UM 1187 did not provide constructive notice that the Company sought to defer costs related to gas and electric price variations because it only discussed variations in hydro generation. These circumstances invoke precisely the “evil” of retroactive ratemaking identified by the WUTC, that customers have had no opportunity to know what amounts may be included in future rates. WUTC Docket No. U-81-41, Sixth Supp. Order at 17-18.

**5. Staff’s Focus on the Method of Calculating the Deferral Does Not Cure the Retroactive Ratemaking Concerns**

Staff has argued that authorizing deferral of costs related to gas and electric prices regardless of whether any variation in hydro generation occurs would not lead to retroactive ratemaking even though PGE did not identify those costs in its application. Staff/400, Galbraith/5-7. According to Staff, the “Commission has the discretion to condition a utility’s

deferral request by requiring the utility to defer other costs or revenues to create a deferral that appropriately matched costs borne by and benefits received by ratepayers.” Id. at Galbraith/6. Staff’s arguments are unconvincing.

The deferred accounting statute and the Commission’s deferred accounting decisions both reflect that the Commission does not, as Staff suggests, have broad discretion to authorize deferral of costs as it sees fit. The Commission’s authority to authorize deferred accounting is limited only to that provided by ORS § 757.259. Order No. 97-180 demonstrates that allowing recovery through a cost recovery mechanism of costs that do not meet the requirements in the deferred accounting statute would constitute retroactive ratemaking. OPUC Docket No. UT 135, Order No. 97-180 at 9, 12. Moreover, the Commission has explicitly stated that it construes the deferred accounting statute narrowly and that it will “not grant deferral unless it is clearly within the reach of the statute.” OPUC Docket No. UE 76, Order No. 92-1128 at 8; OPUC Docket No. UE 115, Order No. 01-988 at 8. The Commission cannot authorize deferred accounting of a cost for which an application has not been submitted, and it cannot order deferral of costs incurred prior to the date of such an application. ORS § 757.259(2), (4).

The gist of Staff’s argument is that once PGE has submitted its application for deferred accounting related to hydro generation, the Commission has the discretion to determine the most appropriate method to value and defer the costs of any hydro generation variance. The problem with this argument is that the SD-PCAM does more than merely value the hydro generation variances that do occur according to a different methodology, the SD-PCAM actually defers costs related to gas and electric price variation even if no variation in hydro generation occurs at all. The SD-PCAM would establish a different deferred account altogether, and that

account goes far beyond what PGE requested to be approved in UM 1187. It is unlawful retroactive ratemaking to authorize a deferred account that would include costs that PGE will incur regardless of any variation in hydro generation.

### **CONCLUSION**

The Commission should reject the Stipulation and the SD-PCAM. The SD-PCAM is untested, unproven, and inconsistent with the criteria by which Staff has evaluated previous PCA proposals. The mechanism should be rejected because hydro variability is a stochastic risk that has been included in normalized rates, and PGE has failed to show a substantial financial impact from failure to adopt the mechanism. Implementing the mechanism for 2005 would result in unlawful retroactive ratemaking, and would require the Commission to ignore the precedent established by its decision in UM 1071. Staff and PGE have not provided a convincing justification to adopt the mechanism or the Stipulation, and the uncertainty of implementing the mechanism without further study far outweighs the purported benefit. ICNU requests that the Commission reject the Stipulation and the SD-PCAM or, at the very least, deny PGE and Staff's request to implement the mechanism retroactively.

Dated this 9th day of September, 2005.

Respectfully submitted,

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