BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

UE 173

In the Matter of	)
PACIFICORP,	)
Application for Approval of A Power Cost Adjustment Mechanism.	)

CLOSING BRIEF

OF THE

CITIZENS' UTILITY BOARD OF OREGON

January 27, 2006

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I. Introduction

Between tortured analogies and obvious misunderstandings of the Commission's UE 165 Order, PacifiCorp's Reply Brief fails to move us from our position. CUB stands by the comprehensive power cost adjustment mechanism we propose in our testimony as one that is clear, simple, does not require annual tinkering, is easily understood by customers and rating agencies alike, and stands the best chance of long-term operation without unintended consequences.

II. The Great Symmetry Debate

In its Reply Brief, PacifiCorp outlines an extensive, melodramatic Russian roulette analogy as a general commentary on symmetry. PacifiCorp Reply Brief at 3-4. PacifiCorp's analogy leaves us scratching our heads at its convolutions. It starts out as if the Company's premise is that the odds are equal, and that we propose to change them, but then switches gears as if the Company's premise is that the odds are unequal, and that we want to keep it that way. In either case, our recommendation is to fully load our six-shooter and put that analogy out of its misery.

PacifiCorp's tortured example appears, we think, to claim that the current balance of risk related to variable power cost fluctuations is asymmetrically distributed between customers and the Company. The Company uses this premise to claim it needs its proposed mechanism to level the playing field.

PacifiCorp is paid a rate of return in part to manage power cost fluctuations. This is not asymmetric, this is regulatory practice. The greater the risk the Company bears, the higher its return on equity; the lower the Company's risk, the lower its return on equity. There is no such thing as perfect symmetry between a utility and its customers in regard to power costs, there is only a balance between risk and return.

We consider the risk balance that currently exists to be consistent with the Company's return on equity that was established in its last rate case. In UE 170, where PacifiCorp's current return on equity was established, the Commission adopted an annual transition adjustment mechanism for PacifiCorp, but not a power cost adjustment mechanism. The Company's return on equity was established in that context, and it now appears that PacifiCorp aims to alter that context. The Company's return on equity as it relates to its allocated risk is not an issue in this docket. Therefore, CUB proposes an asymmetrical deadband with the goal of achieving revenue neutrality in order to preserve the balance of risk and return that was established in UE 170.

III. PacifiCorp's Reply Brief

There are several places in PacifiCorp's Reply Brief where the Company's interpretation of the Commission's Order in UE 165 differs from ours, and, we feel, does not reflect the Order as it was written.

A. Tenure

When explaining why the Company does not believe the UE 165 Order applies to this docket, PacifiCorp describes "important differences" between the scope of the UE 165 Order and this docket. PacifiCorp Reply Brief at 1.

> The PGE Order considered a short-term (two-year) arrangement … PacifiCorp is proposing a long-term mechanism.

UE 173 PacifiCorp Reply Brief at 2.

Yes, the proposed mechanism in UE 165 was interim, but the lengthy discussion on pages 8 through 11 of the Commission's Order in UE 165 describes criteria for a long-term hydropower mechanism. In fact, one of the principal design criteria the Commission recommends is permanence; therefore, the Commission's discussion of design criteria certainly applies to long-term mechanisms, not simply interim ones.

B. Application Of Both Power Cost & Earnings Deadbands

The Company seems quite confused about the Commission's proposal, in the UE 165 Order, for two deadbands: a power cost deadband and an earnings deadband.

i. Power Cost Deadband

The power cost deadband described by the Commission is one based on event frequency and measured by variable power costs, not one measured in a "range of reasonable total returns," as described by the Company. PacifiCorp Reply Brief at 3.

The Commission proposes a power cost deadband to define an unusual event, such as a 1 in 4.5-year hydropower shortfall. We do not know, however, what the financial impact of a 1 in 4.5-year hydro event would be when measured in basis points of return on equity. We most certainly don't know how a 1 in 4.5-year comprehensive variable power cost fluctuation would translate into basis points of return on equity.

When discussing the proposed interim mechanism (not the criteria for a long-term mechanism) in UE 165, the Commission writes:

> PGE and Staff provided no evidence on the frequency with which the mechanism would be triggered under the range of hydro conditions (based on the historical record)…We believe that an upper deadband of $15 million is reasonable for limiting recovery to unusual events, at least in the short-run until further information about likely results under the mechanism can be developed.

UE 165 OPUC Order No. 05-1261 at 11.

It appears that PacifiCorp somehow took the Commission's earnings deadband of ±100 basis points, and applied it instead as a power cost deadband: "a deadband of 100 basis points would apply to PCAM charges and credits." PacifiCorp Reply Brief, page 3. This ignores both the Commission's parameter of an unusual event, as well as the Commission's use of that parameter when speaking of a hydropower mechanism.

ii. Earnings Deadband

The design criteria cited by the Commission in UE 165 include an earnings deadband of ±100 basis points of return on equity. We read the Commission's proposal as saying that when earnings are within 100 basis points of a utility's allowed rate of return, the utility should absorb the benefit or burden of that variance.

As PacifiCorp uses the ±100 basis points benchmark for a power cost deadband, it has to look elsewhere for an earnings deadband. It appears that the Company takes the

Commission's comment, on page 10 of the UE 165 Order, about a range of ±25-50 basis points in a rate case return on equity decision, and applies that range to what it thinks the Commission intended as an earnings deadband. PacifiCorp Reply Brief at 3. Well, PacifiCorp didn't actually apply the range, it applied the lowest extent of that range, ±25 basis points. This is a far cry from the Commission's suggestion of an earnings deadband of ±100 basis points of return on equity.

iii. Application Of Both Deadbands

Following this confusion, PacifiCorp's Reply Brief reverses the order of deadband application, as laid out by the Commission in its UE 165 Order. In PacifiCorp's interpretation, the earnings deadband is applied first, and if the Company's earnings are outside the deadband, then the Company can amortize those variable power costs that fall outside of the power cost deadband.

> If the overall return test is satisfied, a deadband of 100 basis points would apply to PCAM charges and credits.

PacifiCorp Reply Brief at 3.

The Commission's Order in UE 165, however, first applies the power cost deadband and sharing bands. Following this, the costs or credits that qualify for amortization are then subject to the Commission's proposed earnings deadband.

> If earnings are outside this deadband, recovery or refund would be allowed to the perimeter of the range. For example, if the utility's earnings are below the bottom of the range, recovery for poor hydro conditions (as determined through application of the power cost deadband and further sharing between the company and customers) would be allowed up to the bottom of the range.

UE 165 OPUC Order No. 05-1261 at 9.

CUB's interpretation of the Commission's UE 165 Order, is that charges and credits can be applied only if they exceed the power cost deadband, and then only to the extent that the Company's earnings are outside the earnings deadband. Put another way, if the earnings test is satisfied, the charges and credits can be applied, but only to the extent they do not cause the utility's earnings to fall within the earnings deadband.

C. An Objective Basis?!

PacifiCorp claims that the only evidence the Commission can use to evaluate the proposals of the Company, Staff, and CUB is evidence that first appears in its Opening Brief:

> Ideology aside, the only objective basis for determining the reasonableness of the parties' various proposals is to consider the numeric results they produce. PacifiCorp's Opening Brief does just that (at 12-17). There, it is demonstrated that PacifiCorp's proposal exposes its shareholders to the potential for substantial unrecovered costs, while the results of the CUB and Staff proposals are punitive and quixotic and at times counter-productive.

PacifiCorp Reply Brief at 7.

The evidence that PacifiCorp cites was not put on the record during testimony. CUB, Staff, and other intervenors did not have an opportunity to review work papers, ask data requests, or cross-examine a witness sponsoring this evidence. The numbers in the Company's tables are at odds with PacifiCorp's historic conditions and, as far as we know, with anyone's anticipated conditions. Instead, the numbers reflect a hypothetical extreme far worse than even the 2000-2001 Energy Crisis. CUB Reply Brief at 8-10, and Staff Reply Brief at 7-9. Yet PacifiCorp now cites these examples as the ***only objective basis*** for the Commission to evaluate the parties' proposals. Our impression of PacifiCorp's examples is that they are wholly inappropriate, unreliable, unrealistic, and represent extreme subjectivity.

D. Annual Variable Power Cost Adjustments Make A Difference

While we disagree with PacifiCorp's assertion that deadbands prevent the Company from recovering its power costs on an expected basis, even the Company admits (in a footnote) that its transition adjustment mechanism, established in UE 170, has changed this calculation:

> Absent a mechanism such as PacifiCorp's TAM, in an environment of constantly increasing fuel and purchased power costs, a deadband virtually assures that the Company will not have a fair opportunity to earn its allowed rate of return on an expected basis.

PacifiCorp Reply Brief at 2.

CUB did not support a transition adjustment mechanism for PacifiCorp, and is not sure of the basis for the Company's suggestion that we are in an environment of constantly increasing fuel and purchased power costs. We would note, however, that Pacificorp's transition adjustment mechanism has reduced the Company's exposure to changing costs, which is the primary driver the Company cites in proposing a power cost adjustment mechanism.

PacifiCorp has a problem with evidence. The evidence that supports their initial application is a Standard & Poor's report that examines the role of fuel and purchased-power adjustment mechanisms for utilities. However, that same report acknowledges PGE's resource valuation mechanism, in combination with PGE's ability to apply for deferrals, as a "quasi" adjustment mechanism with which Standard & Poor's appears satisfied. PPL/101/Omohundro/5. Today, after the Commission's Order in UE 170, PacifiCorp also has an annual power cost update, coupled with the ability to file for a deferral, and, therefore, has the same sort of "quasi" adjustment mechanism. Since the Company can no longer rely on the evidence in its testimony, PacifiCorp made up tables of examples, which are not in evidence, that it now cites as the only objective basis for the Commission to evaluate the parties' proposals.

E. PacifiCorp's Position On Hydropower Vs Comprehensive

We do agree with PacifiCorp that, in its Order in UE 165, the Commission was proposing design criteria for a hydropower-only mechanism, and that it is not clear whether the Commission believes these criteria should also apply to a comprehensive mechanism. However, the Company does seem to believe that the Commission's discussion of deadbands in its UE 165 Order may, indeed, apply to comprehensive mechanisms.

> Nonetheless, there is one area where the PGE Order would appear to signal Commission preferences that might have bearing on this case. In the PGE Order, the Commission favors a "two-part" mechanism where there would be both: a) a determination of whether a utility's overall return was outside a reasonable range, and b) a determination of whether the earnings impact of actual net power costs falls outside a deadband bracketing the range of reasonable total returns.

PacifiCorp Reply Brief at 2-3, footnote omitted.

We agree with the Commission that the combination of a power cost deadband and an earnings deadband is appropriate for a hydropower cost adjustment mechanism. We also feel this concept is appropriate for a comprehensive power cost adjustment mechanism. In its Reply Brief, PacifiCorp's confusion of the Commission's proposed deadbands makes it unclear if the Company shares our interpretation that the use of a two-part deadband system is appropriate for both hydropower and comprehensive mechanisms, as well as where the Company stands on the magnitude of deadbands for these different adjustment mechanisms, as the deadbands discussed in the Company's

Reply Brief differ so dramatically from what the Commission proposed in its Order in UE 165.

IV. Conclusion

We continues to recommend our proposed comprehensive power cost adjustment mechanism. PacifiCorp's Reply Brief, other than attempting to muddy the discussion surrounding the Commission's UE 165 Order, adds nothing to the examination of this docket.

Respectfully Submitted,
January 27, 2006

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CERTIFICATE OF SERVICE

I hereby certify that on this 27th day of January, 2006, I served the foregoing Closing Brief of the Citizens' Utility Board of Oregon in docket UE 173 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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