PUBLIC UTILITY COMMISSION
OF OREGON

UM 1623

In the Matter of PORTLAND GENERAL ELECTRIC COMPANY Application for Deferral Accounting of Excess Pension Costs and Carrying Costs on Cash Contributions.	STAFF REPLY BRIEF

I. Introduction.

The question presented in this docket is whether the Commission should allow Portland General Electric Company (PGE) to defer for later inclusion in rates FAS 87 pension expense incurred in 2012 and 2013 that exceeded the $5.1 million of annual expense assumed in PGE's rates. The Citizens' Utility Board of Oregon (CUB), the Industrial Customers of Northwest Utilities (ICNU), and Staff recommend that the Commission deny PGE's request, asserting that PGE's deferral application fails to meet either the statutory or discretionary criteria applied to deferral requests.

As explained by each party in filings previously submitted in this docket, the Commission applies a two-stage analysis when considering requests to defer expenses – first determining whether statutory criteria are met and if so, whether the Commission's discretionary criteria are satisfied.[1] Staff has addressed how PGE's application does not meet the statutory criteria because PGE did not establish the deferral would match costs and benefits or minimize the frequency of rate changes.[2] Staff has also explained that the

[1] ICNU Opening Brief 6, CUB's Opening Brief 2, PGE's Opening Brief 6, Staff Prehearing Memorandum 2-3.

[2] Staff Prehearing Memorandum 4-5; Staff/100, Bahr/6.

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deferral does not satisfy the Commission's discretionary criteria primarily because the amounts at issue are not "substantial." Because the issues in this docket have been addressed in the previously-filed testimony and opening briefs, Staff limits the arguments in this reply brief to responses to two arguments made by PGE, one concerning Staff's application of the statutory criteria and the other regarding whether PGE satisfied the discretionary criteria.

A. Statutory criteria.

PGE states in its opening brief that "Staff appears to be claiming that FAS 87 expense is not an actual cost to the company" because it is an accrual cost.[3] PGE suggests that this belief underlies Staff's argument that the deferral does not appropriately match ratepayer costs and benefits.[4] PGE's understanding of Staff's argument is incorrect.

Staff's conclusion the deferral application does not appropriately match ratepayer benefits and costs is based on the disconnect between FAS 87 expense accrued in any one year and the long-term benefits and costs of PGE's pension program. PGE asserts that deferring two years of FAS 87 expense matches the costs of PGE's pension program with program's benefits.[5] PGE fails to recognize that pension expense calculations under FAS 87 represent a long-term method of accounting and the costs and benefits should be considered over the long-term.[6]

As the Commission noted in its final order in its recent investigation into pension cost recovery, "[b]ecause FAS 87 expense is based on an accrual, not cash basis, the amount of pension costs recorded is generally different than the actual amount of annual contributions made. Over the life of the plan, however, total contributions are expected to

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[3] PGE's Opening Brief 4.

[4] PGE's Opening Brief 4.

[5] PGE's Opening Brief 3.

[6] See e.g., ICNU/100, Mullins/7.

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equal total FAS 86 expense[.]"[7] ICNU makes the same argument as Staff and explains it very well in its opening brief,

> [S]imply because FAS 87 expense in a given year is higher than that included in customer rates does not mean that customers are underpaying for the costs of the Company's pension plan. One year's FAS 87 expense is merely a predication of the ultimate costs of the benefits earned in that year. Thus, whether customers are underpaying or overpaying for the costs of the pension plan must be viewed over the long term - when the effects of interest rates, rates of return, and other components of FAS 87 can be discerned - not isolated in annual segments. * * * Whether customers have ultimately overpaid or underpaid for the costs of PGE's pension plan will not be known until all of the costs of the pension plan have been paid. [8]

B. Discretionary criteria.

The type of event—modeled in rates or not, foreseeable or not—will affect the amount of harm that must be shown by the utility. If the event was modeled or foreseen, without extenuating circumstances, the magnitude of harm must be substantial to warrant the Commission's exercise of discretion in opening a deferred account.[9] If the event was neither modeled nor foreseen, or if extenuating circumstances were not foreseen, the Commission has explained that the "magnitude of harm that would justify deferral likely would be lower."[10]

PGE asserts that the event leading to the deferral application was "an unexpected, significant, and continuing decline in the discount rate used to determine annual pension expense[,]"and is a scenario rather than stochastic risk.[11] In support of this assertion, PGE

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[7] *In the Matter of Public Utility Commission of Oregon Investigation into Treatment of Pension Costs in Utility Rates,* (Docket No. UM 1633), Order No. 15-226 at 2.

[8] ICNU Opening Brief 10 (citations to record omitted).

[9] *In the Matter of Public Utility Commission of Oregon Staff Request to Open an Investigation Related to Deferred Accounting*, (Docket No. UM 1147), Order No. 05-1070 at 7.

[10] *Id.*

[11] PGE's Opening Brief 6.

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observes that pension expense, like other expenses, are put into rates based on a point estimate.[12] PGE notes that the point estimate is not based on stochastic modeling with assumptions that divergence from the point estimate could be as large as that presented by PGE's deferral application.[13]

Staff agrees that the amount of pension expense that is included in PGE's rates is not based on stochastic modeling. However, the risk that the actual FAS 87 expense will sometimes exceed and sometimes be less than the amount of FAS 87 expense assumed in rates is a type of risk that the Commission has characterized as "stochastic" risk for purposes of analyzing deferral applications. "A 'stochastic risk' can be predicted to occur as part of the normal course of events, whereas a scenario risk is not susceptible to prediction or quantification."[14]

The Commission has explained that the financial harm from a stochastic risk must be "substantial" before deferred accounting is warranted because stochastic risk events cause costs to swing above and below the average included in rates, so the effect of stochastic risk events should average out.[15] In contrast, financial harm from a scenario risk need only be material because there is no likelihood that a cost swing related to a scenario risk event will be balanced out over time.[16]

While there may be circumstances in which the difference between the actual discount rate or actual FAS 87 expense and the discount rate or FAS 87 expense embedded in rates is so great as to be beyond what can be expected in the normal course of events (a scenario risk event), these circumstances are not found here. FAS 87 expense has swung

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[12] PGE's Opening Brief 9.

[13] PGE's Opening Brief 9.

[14] *In the Matter of Portland General Electric company Application for Deferred Accounting of Excess Power Costs Due to Plant Outage* (Docket No. 1234), Order No. 07-049 at 9.

[15] *In the Matter of Portland General Electric Company Application for an Order Approving Deferral of Hydro Replacement Power* Costs (Docket No. 1071), Order No. 04-108 at 8.

[16] *Id.*, at 9.

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above and below the amount included in rates since at least 1997, which is what occurs with stochastic risk events.[17]

For example, CUB testified that from 1997 to 2004, PGE collected from ratepayers for pension expense, $84 million in excess of its actual pension expense.[18] In 2008, PGE collected from customers approximately $1.1 million for FAS 87 expense when its actual FAS 87 Expense was - $2.4 million. In the other years between 2005 and 2011, PGE's actual FAS 87 Pension Expense totaled approximately $15.7 million while PGE collected approximately $7.3 million for FAS 87 Expense from ratepayers.[19] PGE over recovered for its pension expense in 2014 and at the time it filed testimony, expected this over recovery by a $3.6 million under recovery in 2015. [20]

Evidence regarding the historical swings in PGE's FAS 87 expense shows that the under recovery of $2.9 million of FAS 87 pension expense in 2012 and of $13.5 million in 2013 is not so significant that is it beyond what can be expected in the normal course of business. Or put another way, it is not so large that it has not been, and cannot be, offset by over recovery of FAS 87 expense in other years. With respect to offsetting over recovery in future years, CUB testified that it is clear from confidential information obtained from PGE that PGE expects for actual pension expense to fall below zero by 2020 and continue to drop.[21] However, PGE is currently collecting $13.8 million in rates per year for pension expense and will continue to do so until another rate change.[22]

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[17] CUB/100, McGovern/7.
[18] CUB/100, McGovern/7.
[19] CUB/103.
[20] PGE/100, Batzler-Hager/5.
[21] CUB/100, McGovern/9, CUB/104.
[22] CUB/100, McGovern/9.

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CONCLUSION

Staff recommends that the Commission deny PGE's application to defer.

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Respectfully submitted,

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