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September 26, 2016

Via Electronic Filing

Public Utility Commission of Oregon
Attn: Filing Center
201 High St. SE, Suite 100
Salem OR 97301

Re: In the Matter of PACIFICORP, dba PACIFIC POWER
2017 Transition Adjustment Mechanism
Docket No. UE 307

Dear Filing Center:

Enclosed for filing in the above-captioned proceeding, please find the redacted Response Brief of the Industrial Customers of Northwest Utilities ("ICNU") in the above-referenced docket.

The confidential portions of ICNU's brief are being handled in accordance with the general protective order issued in this proceeding and will follow via Federal Express.

Thank you for your assistance. If you have any questions, please do not hesitate to call.

Sincerely,

/s/ Jesse O. Gorsuch
Jesse O. Gorsuch

Enclosure

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that I have this day served the confidential pages of the **Response Brief of the Industrial Customers of Northwest Utilities** upon the parties shown below by mailing copies via First Class U.S. Mail, postage prepaid.

Dated at Portland, Oregon, this 26th day of September, 2016.

Sincerely,

/s/ Jesse O. Gorsuch
Jesse O. Gorsuch

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BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

UE 307

In the Matter of	)	RESPONSE BRIEF OF THE
	)	INDUSTRIAL CUSTOMERS OF
PACIFICORP, dba PACIFIC POWER	)	NORTHWEST UTILITIES
	)	
2017 Transition Adjustment Mechanism	)	(REDACTED)
	)	

I. INTRODUCTION

Pursuant to the Administrative Law Judge's July 8, 2016 Ruling, the Industrial Customers of Northwest Utilities ("ICNU") files this Response Brief in the above-captioned proceeding. PacifiCorp's (or the "Company") Transition Adjustment Mechanism ("TAM") is intended to forecast the Company's net power costs ("NPC") for the following year and set transition charges for customers electing direct access.[1/] In accordance with these goals, ICNU agrees with the Company that the TAM should produce the most accurate NPC forecast possible.[2/] The Commission's review of the Company's application, however, also must ensure that this NPC forecast, regardless of its accuracy, yields fair and reasonable rates for PacifiCorp's Oregon customers.[3/]

ICNU disputes that the Company's application produces the most accurate NPC forecast possible. In the 2016 TAM, ICNU challenged the Company's modeling change related to day-ahead and real-time system balancing transactions (the "DART" adjustment).[4/] ICNU

1/ Docket No. UE 296, Order No. 15-394 at 1 (Dec. 11, 2015).
2/ PacifiCorp Opening Br. at 1
3/ ORS 756.040(1).
4/ Docket No. UE 296, ICNU/100 at 5:5-20:22 (June 29, 2015).

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argued that the DART adjustment did not address the alleged problems the Company was attempting to resolve, namely that the Company incurs greater costs for daily system balancing than is reflected in its GRID model because it purchases on the market more frequently when prices are high and sells more frequently when prices are low.[5/] ICNU continues to believe that the DART adjustment is not an appropriate method of addressing this issue.[6/] However, if the Commission retains the DART adjustment, it should, at a minimum, remove the costs associated with day-ahead (or inter-hour) wind and load integration costs because they are necessarily being double-counted. The Company attempts to obfuscate the issue by making an irrelevant distinction between the cost of gas plant commitments and the cost of market purchases, but ICNU's recommendation is straightforward – the DART adjustment incorporates actual historical transactions; if the Company incurs real costs associated with day-ahead wind and load integration, then those costs must be included in the historical transactions used in the DART adjustment. Therefore, no additional adjustment for day-ahead integration costs is needed.

ICNU also disputes that the Company's application results in fair and reasonable rates for its Oregon customers. The record in this case is clear that the cost of coal the Company purchases from its affiliate, Bridger Coal Company ("BCC"), is well above the cost of coal available on the market for comparable coal supplies. The Company does not deny that prices for coal from the Power River Basin ("PRB") are below the prices PacifiCorp proposes to pay for BCC coal in 2017,[7/] and admits that PRB mines are potential market suppliers to the Jim

5/ PAC/100 at 17:8-11.
6/ ICNU/100 at 5:15-7:8.
7/ PAC/500 at 3:15-22; PAC/500 at 26, Confidential Figure 4 ("Total Comparative Price Per Ton" row, "Mullins/Kaufman Corrected" column and "Bridger Coal Company Total" column).

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Bridger Plant.[8/] ICNU, therefore, recommends that the Commission reduce the costs the Company has included in its application related to coal deliveries to Jim Bridger from BCC based on the Commission's lower-of-cost-or-market affiliate pricing rules. The Company's position that these rules cannot apply to PRB coal because Jim Bridger requires capital upgrades in order to receive the volumes of PRB coal required to substitute it for BCC coal is self-serving, allowing the Company to delay these upgrades indefinitely, and does not reflect a necessary reading of the rules. Additionally, the Commission is not estopped from treating BCC as a PacifiCorp affiliate for purposes of lower-of-cost-or-market pricing merely because it has consolidated BCC with PacifiCorp for regulatory purposes in the past. This was originally done to ensure customers pay fair and reasonable rates for BCC coal. A lower-of-cost-or-market adjustment for BCC coal in this case would effectuate the same fundamental statutory responsibility by ensuring that customers do not pay costs that are well above the going rate for a comparable product.

Finally, given the complexity of recent TAM proceedings and the large number of modeling changes the Company has recently incorporated into GRID, ICNU recommends that the Commission extend the moratorium it imposed in the 2016 TAM on the Company's ability to make additional GRID modeling changes until PacifiCorp files its next general rate case.

8/ PAC/1000 at 3:3-5.

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II. ARGUMENT

A. If the Commission Retains the DART Adjustment, It Should Remove Costs Associated With Day-Ahead Wind and Load Integration.

ICNU's testimony proposes that, if the Commission retains the DART adjustment, then day-ahead wind and load integration costs should be removed from NPC because they are being double-counted.[9/] Unless, contrary to its claims, the Company does not incur day-ahead integration costs in actual operation, then the DART adjustment must double-count these costs. ICNU's proposal results in a decrease to NPC of approximately $1.9 million on an Oregon-allocated basis.[10/]

The Company introduced the DART adjustment in the 2016 TAM as a new modeling adjustment meant to account for the costs of "day-ahead and real-time system balancing."[11/] As the Company describes it, the GRID model "calculates the least-cost solution to balance the Company's load and resources each hour."[12/] To do this, the GRID model "uses monthly average prices, and the same prices were used for purchases and sales."[13/] The Company claims that this results in an unrealistic NPC forecast because, in reality:

> the Company has historically bought more during higher-than-average price periods and sold more during lower-than-average price periods. As a result, the average cost of the Company's daily and hourly short-term firm purchases has been consistently higher than the average actual monthly market price, while the average revenue from its daily and hourly short-term firm sales has been consistently lower than the average actual monthly market price.[14/]

9/ ICNU/100 at 3:4-5:13; ICNU/200 at 2:20-7:7.
10/ ICNU/100 at 2 (table 1).
11/ PAC/100 at 15:22-16:6.
12/ *Id.* at 15:15-16.
13/ PAC/400 at 21:17-18.
14/ PAC/100 at 17:9-14.

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To address this issue, the DART adjustment "uses the historical differences between the average market prices over each month and *actual prices* for the Company's day-ahead and real-time balancing transactions in that month, for both purchases and sales."[15/] In other words, the DART adjustment looks at the actual "short-term firm transactions at a given market hub" that the Company made and compares the average price of these actual transactions to the average market price.[16/] The Company calculates the DART adjustment "outside of the GRID model."[17/]

Meanwhile, the Company separately calculates a charge for "inter-hour integration costs,"[18/] also known as "day-ahead integration costs."[19/] These costs are described in the Company's 2014 Wind Integration Study and relate to "day-ahead forecast variances … which affects how dispatchable resources are committed to operate, and subsequently, *affect daily system balancing*."[20/] That is, the Company determined its system balancing costs associated with both load and wind first by "committing resources based on a day-ahead [load or wind] forecast and [then] committing resources based on *actual* [load or wind generation]."[21/] The difference in production costs between these scenarios represents day-ahead integration costs.[22/] Like the DART adjustment, these costs "are not included within the GRID model."[23/] The Company's witness agrees that the 2014 Wind Integration Study fairly describes how day-ahead wind and load integration costs are calculated.[24/]

15/ PAC/400 at 21:12-15 (emphasis added).
16/ PAC/100 at 18:10-19:12.
17/ PAC/400 at 22:7-10; ICNU/200 at 4:11-5:8.
18/ PAC/400 at 39:5-15.
19/ *Id.* at 38:7-17.
20/ ICNU/300 at 4 (emphasis added).
21/ *Id.* at 26; PAC/400 at 39:5-15 (emphasis added).
22/ ICNU/300 at 26.
23/ ICNU/301 at 6:11-13
24/ Public Tr. at 9:8-11.

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Because the DART adjustment and day-ahead integration costs are calculated outside of the GRID model and are based on actual historical transactions the Company has made, ICNU's witness, Bradley Mullins, recommended that day-ahead integration costs be removed from the NPC calculation.[25/] Mr. Mullins argued that "the Company includes all historical day-ahead and real-time transactions in its DART modeling adjustment."[26/] Yet, "when the DART modeling calculates the ultimate $/MWh cost of system balancing outside of the GRID model, it does not make any adjustment to remove the transactions that were made for the purpose of day-ahead load and wind integration."[27/]

In response, the Company's testimony concedes that historical transactions used in the DART adjustment include day-ahead load and wind integration costs.[28/] It argues, however, that these integration costs are "related to the commitment of gas plants" and have "nothing to do with market prices, as ICNU implies."[29/] Meanwhile, the Company's opening brief spends one paragraph addressing ICNU's adjustment and merely reiterates the distinction it makes between the cost of market transactions and the cost of gas plant commitments.[30/]

Strictly speaking, Mr. Mullins never testified that day-ahead integration costs are related to market prices, although this is frankly irrelevant. It does not matter whether one characterizes these costs as related to market transactions, gas plant commitment, or anything else. If the Company is correct that it incurs day-ahead integration costs associated with wind and load in actual operation, then the historical transactions it uses to establish the DART

25/ ICNU/100 at 4:5-5:13.
26/ *Id.* at 5:10-11.
27/ ICNU/200 at 5:3-5.
28/ PAC/800 at 30:3-6.
29/ *Id.* at 30:14-22.
30/ PacifiCorp Opening Br. at 49-50.

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adjustment, which are derived from those actual operations, must, *by definition*, include those day-ahead integration costs. That is why it is a double-count to apply both the DART adjustment and a separate adjustment for day-ahead wind and load integration costs. Again, the purpose of the DART adjustment is to account for the actual cost of *day-ahead* and real-time *system balancing*. The Company uses the complexity of the DART adjustment and day-ahead integration costs to confuse what is, in fact, a simple issue.

B. The Commission Should Reprice BCC Coal Deliveries Under Its Affiliated Interest Rules.

ICNU recommends in testimony that the Commission reduce NPC by $6 million, Oregon-allocated, by repricing PacifiCorp's coal deliveries from BCC at the market rate under the Commission's lower-of-cost-or-market affiliate regulations.[31/] Mr. Mullins demonstrates that, even after accounting for capital upgrades necessary to receive and burn PRB coal and amortization of the undepreciated mine investment, PRB coal is still a cheaper alternative to BCC coal.[32/]

The Commission's affiliated interest rules require that, "[w]hen services or supplies … are transferred or provided to a regulated activity by a nonregulated activity, transfers shall be recorded in regulated accounts at the nonregulated activity's cost or the market rate, whichever is lower."[33/] The "market rate" is defined as "the lowest price that is available from nonaffiliated suppliers for comparable services or supplies."[34/] PacifiCorp owns 66.7% of

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31/ ICNU/100 at 8:1-15:21; Errata to ICNU/200 at 7:8-12:19.
32/ Errata to ICNU/200 at 9, Confidential Table 1R.
33/ OAR 860-027-0048(3)(e).
34/ *Id.* 860-027-0048(1)(i).

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BCC,[35] and therefore, PacifiCorp has an "affiliated interest" with BCC under the law.[36] Thus, the Commission's "lower-of-cost-or-market" affiliated interest rule facially applies to PacifiCorp's purchases of coal from BCC.

The Company makes three primary challenges to ICNU's proposed adjustment. First, it argues that the definition of "market rate" precludes using PRB coal as the comparator when applying the lower-of-cost-or-market pricing rule to coal PacifiCorp purchases from BCC.[37] Second, it argues that the Commission historically has not treated BCC as a PacifiCorp affiliate.[38] Third, it disputes ICNU's calculations that derive a $6 million cost savings.[39]

1. <u>The Commission's lower-of-cost-or-market rule does not require that Jim Bridger currently be capable of burning PRB coal</u>.

With respect to the first issue, the Company argues that a lower-of-cost-or-market adjustment is inappropriate because the Commission's rules require the "market rate" to be "the lowest price that is available from nonaffiliated suppliers for comparable services or supplies."[40] The Company notes that, in order to receive sufficient deliveries of PRB coal to replace BCC coal, it must make capital upgrades to Jim Bridger.[41] Thus, it argues that PRB coal currently is not "available" to Jim Bridger and, therefore, a comparison of the price for BCC coal with the market price for PRB coal is not appropriate.[42] The Company, however, does not present a

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[35] ICNU/102 at 3.
[36] ORS 757.015.
[37] PacifiCorp Opening Br. at 27.
[38] *Id.* at 26.
[39] *Id.* at 28.
[40] OAR 860-027-0048(1)(i); PacifiCorp Opening Br. at 27.
[41] PacifiCorp Opening Br. at 27.
[42] *Id.*

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required interpretation of the definition of "market rate" based on the rule's language. Moreover, its interpretation does not reflect the intention of the rule and is self-serving.

Fundamentally, the Commission's task is to ensure fair and reasonable rates.[43/] The lower-of-cost-or-market rule facilitates this by preventing cross-subsidization between a public utility and its affiliate.[44/] It allows the Commission to assess the reasonableness of the price a utility is paying to its affiliates for a particular service or supply based on a comparison with the price on the market for "comparable services or supplies."[45/] When the Commission applies the lower-of-cost-or-market rule to an affiliate transaction, it does not require the utility literally to substitute the market product for the affiliate's product. It merely requires the utility to substitute the market *price* for the affiliate's price. Thus, the fact that Jim Bridger currently is not able to receive enough PRB coal to substitute it for BCC coal should not matter for purposes of the lower-of-cost-or-market analysis, which, again, ultimately is focused on an assessment of whether the affiliate's price to the utility is fair and reasonable.

What matters for purposes of the lower-of-cost-or-market rule, then, is whether PRB coal is "comparable" to BCC coal; that is, that a price comparison between PRB coal and BCC coal is a fair comparison. The record in this case demonstrates that the PRB is one of the "potential market suppliers to the Jim Bridger plant."[46/] The Company's Opening Brief further notes that Jim Bridger could burn PRB coal without any deration.[47/] Indeed, five percent of the coal delivered to Jim Bridger today comes from the PRB.[48/] Therefore, PRB coal is a

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43/ ORS 756.040(1); *American Can Co. v. Davis*, 28 Or. App. 207, 221-24 (1977).
44/ *GTE Northwest, Inc. v. Pub. Util. Comm'n*, 120 Or. App. 401, 406 (1993).
45/ OAR 860-027-0048(1)(i).
46/ PAC/1000 at 3:3-5.
47/ PacifiCorp Opening Br. at 7.
48/ PAC/500 at 7:14-18.

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"comparable service[] or suppl[y]" to BCC coal for purposes of fueling Jim Bridger. The record also shows that customers are paying a price for BCC coal that is well above the market price for this comparable product.[49/] Consequently, the amount that PacifiCorp proposes customers pay for BCC coal in the 2017 TAM is not fair and reasonable and should be repriced under the Commission's lower-of-cost-or-market affiliate rules.

The Company also relies on the Commission's order in the 2014 TAM, which rejected a similar adjustment ICNU proposed by substituting BCC coal for Black Butte coal.[50/] The Commission found that, "[o]n the record presented in this docket, ICNU fails to persuade us to adopt its proposed adjustment."[51/]

Relying on its position that the market substitute must be physically available, the Company suggests that the Commission rejected ICNU's adjustment in the 2014 TAM because ICNU did not demonstrate that Black Bute coal was an available substitute for BCC coal.[52/] The Commission's order, however, does not specifically rely on this position as the basis for its decision. The Commission also notes that PacifiCorp contested ICNU's calculation of a savings from Black Butte coal and, thus, that ICNU did not demonstrate that Black Butte coal was a lower cost alternative to BCC coal.[53/]

Therefore, the Company infers too much when it argues that the Commission rejected ICNU's adjustment in the 2014 TAM because it found that the definition of "market rate" required Black Butte coal to be physically capable of replacing BCC coal.[54/] Indeed, to

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49/ ICNU/100 at 12:11-13:2; Staff/400 at 23:1.
50/ Docket No. UE 264, Order No. 13-387 at 6-7 (Oct. 28, 2013).
51/ *Id.* at 6.
52/ PacifiCorp Opening Br. at 27.
53/ Order No. 13-387 at 7.
54/ PacifiCorp Opening Br. at 27.

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ICNU's knowledge, the Commission has never specifically found that the lower-of-cost-or-market rule requires the market alternative to be physically available to the utility asset in question.

As argued above, such a finding would be inconsistent with the intent of the rule, which is designed to establish a fair and reasonable price for supplies purchased from an affiliate in order to prevent cross-subsidization. Moreover, PacifiCorp's interpretation of the rule is self-serving. It allows the Company to avoid application of the lower-of-cost-or-market rule by simply deferring investments in the plant that would otherwise be in the best interest of customers. It can, then, continue to earn a return for its shareholders on its investment in BCC.

2. The Commission has discretion to treat BCC as an affiliate.

PacifiCorp also argues that application to BCC of the lower-of-cost-or-market rule is inappropriate because the Commission treats BCC as a regulated asset, not as a utility affiliate.[55/] The Company points to Order 79-754, in which the Commission determined that it "will limit the return to [PacifiCorp] on its Bridger investment to that level allowed on other [PacifiCorp] operations. Whether owned by the company or its affiliate, in setting rates no asset may earn a rate of return greater than that either authorized or earned by [PacifiCorp]."[56/] The Company argues that, through this and subsequent orders, "BCC is not treated as an affiliate at all; it is treated as if PacifiCorp itself were mining the coal."[57/]

55/ PacifiCorp Opening Br. at 26.
56/ Docket No. UF 3508, Order No. 79-754 at 20 (Oct. 29, 1979).
57/ PAC/600 at 8:8-10.

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The Commission's Order No. 79-754 is based on the "result of the proposed coal price in this case."[58/] The Commission found that a purported market price of $7.78 per ton of BCC coal would "enable [PacifiCorp's] shareholders to earn a return of 18 percent overall and a 36 percent return on Bridger Coal's common equity from sales to [PacifiCorp] at the expense of ratepayers."[59/] Consequently, the Commission repriced this coal at a level "allowed on other [PacifiCorp] operations."[60/]

Such treatment of affiliated utility operations has been upheld in a number of courts, including in Oregon.[61/] In *Pacific Northwest Bell Telephone Co. v. Sabin*, the Oregon Court of Appeals affirmed a Commission decision that reduced Pacific Northwest Bell's ("Bell") rate base to account for the "excess earnings" of the utility's affiliated supplier, Western Electric Co. ("Western").[62/] The Commission found that "Oregon ratepayers should not be required to pay rates which yield a greater return on the assets of (or investment in) one part of the Bell System than on another simply because the assets are employed in a function undertaken by a non-jurisdictional arm of the system …."[63/] The *Sabin* Court's decision upholding this order was based largely on the unique position Bell held as a subsidiary of American Telephone and Telegraph Co. ("AT&T"), which, at the time, allowed Western to control 80% of the domestic market in telecommunications products.[64/] This rendered a comparison of Western's prices to

58/ Order No. 79-754 at 19.
59/ *Id*.
60/ *Id.* at 20.
61/ *Pacific Northwest Bell Telephone Co. v. Sabin*, 21 Or. App 200 (1975); *Smith v. Illinois Bell Tel. Co.*, 282 U.S. 133, 153 (1930); *Pacific Tel. & Tel. Co. v. Pub. Util. Comm'n*, 401 P.2d 353 (Cal. 1965); *Chesapeake & Potomac Tel. Co. of West Virginia v. Pub. Serv. Comm'n of West Virginia*, 300 S.E.2d 607, 614 (1982).
62/ *Sabin*, 21 Or. App. at 224.
63/ *Id.* at 208.
64/ *Id.* at 206.

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the "market price" inadequate, even if Western's prices were lower, because there was no developed competitive market.[65] Thus, the Court held that where, (1):

> A utility has purchased the bulk of its necessary equipment and supplie[s] from an "affiliated" manufacturer, and (2) that due to the affiliated relationship the manufacturer enjoys a unique position of market power which renders a comparison of the prices and profits with those of "peripheral" manufacturers inadequate as a measure of the "reasonableness" of the utility's payments to it, the failure by the utility to provide additional evidence as to their reasonableness may be relied upon by the Commissioner as a basis for disallowing from the utility's rate base and operating expenses those portions of the utility's payments which represent a return to the manufacturer greater than that allowed the utility itself.[66]

The *Sabin* Court relied in part for its holding on the U.S. Supreme Court's decision in *Smith v. Illinois Bell Tel. Co.*, which rejected the Illinois Company's:

> [M]ere comparison of the prices charged by [Western] to the Illinois Company with the higher prices charged by other manufacturers for comparable material, or by [Western] to independent telephone companies. The point of the appellants' contention is that [Western], through the organization and control of [AT&T], occupied a special position with particular advantages in relation to the manufacture and sale of equipment to the licensees of the Bell system, including the Illinois Company, that is, that it was virtually the manufacturing department for that system, and the question is as to the net earnings of [Western] realized in that department and the extent to which, if at all, such profit figures in the estimates upon which the charge of confiscation is predicated. We think that there should be findings upon this point.[67]

In the 1979 docket that repriced BCC coal to align this price with the Company's authorized return, Commission Staff relied on *Sabin* for its recommendation that the

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[65] *Id.* at 224.
[66] *Id.*
[67] 282 U.S. 133, 153 (1930).

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Commissioner take this action.[68] The Commissioner himself appears to have relied on this case, noting that "[b]ecause of its affiliated relationship and the volume of its purchases, [PacifiCorp] does enjoy a position of dominance with regard to Bridger Coal which renders a comparison of prices of non-affiliated market transactions inadequate as a measure of reasonableness of [PacifiCorp's] payments to Bridger Coal."[69]

ICNU agrees with the Commissioner's decision in this order because it was within his discretion in establishing fair and reasonable rates.[70] However, ICNU's reading of *Sabin* and *Smith* differs slightly from how it is invoked in Order No. 79-754. Those cases rejected market pricing for Western because it enjoyed a position of dominance over the *entire market* for domestic telecommunications products.[71] Thus, a price comparison with competitors would not necessarily demonstrate a fair price because there was no developed competitive market. Conversely, while PacifiCorp may hold a position of dominance over BCC, the correct analogy is whether BCC holds a position of dominance over the market for coal that could be used to fuel Jim Bridger. As Jim Bridger can burn coal from BCC, Black Butte, Southwest Wyoming, and the PRB, there plainly is a robust market for such coal with which the price PacifiCorp pays for BCC coal can be compared in order to determine whether it is fair and reasonable.[72]

Nor does the fact that the Commission has treated BCC as consolidated with PacifiCorp's regulated operations in the past preclude it from treating BCC as an affiliate for

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[68] Order No. 79-754 at 17.
[69] *Id.* at 19-20.
[70] *American Can Co. v. Davis*, 28 Or. App. 207, 221 (1977).
[71] *Sabin*, 21 Or. App. at 224; *Smith*, 282 U.S. at 153.
[72] PAC/1000 at 3:3-11.

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purposes of the lower-of-cost-or-market rule in this docket. Again, the reason BCC was consolidated with PacifiCorp in the first place was because the result of this treatment yielded fair and reasonable rates, unlike the rates that would have resulted from a comparison with the market price at that time.[73/] As the *Sabin* Court stated: "When the purpose is one of regulatory action, as distinguished from merely applying law or policy to past facts, an agency must at all times be free to take such steps as may be proper in the circumstances, irrespective of it[s] past decisions."[74/] The Court found that "applying a doctrine of 'estoppel' to the acts of the Public Utility Commissioner would deprive him of an essential flexibility and appear to be inconsistent with his regulatory role …."[75/] If the Commission has the discretion to consolidate an affiliate of a public utility in order to achieve fair and reasonable rates, then the corollary should also be true – the Commission should be able to treat an affiliate it has consolidated in the past to achieve fair and reasonable rates as unconsolidated in order to achieve the same objective.

Consequently, that the Commission has consolidated BCC with PacifiCorp's regulated operations in the past does not preclude it from treating BCC as an affiliate of PacifiCorp in this docket in order to apply lower-of-cost-or-market pricing to BCC's coal deliveries to Jim Bridger. The ultimate question for the Commission under the statute and legal precedent is which treatment yields fair and reasonable rates.[76/] In 1979, consolidation of BCC and PacifiCorp resulted in fair and reasonable rates because application of the market price would have yielded an excessive return. Today, both ICNU's and Staff's testimony demonstrate

73/ Order No. 79-754 at 19-20.
74/ *Sabin*, 21 Or. App. at 225 (quoting K. Davis, Administrative Law Treatise, 605, 610 § 18.09 (1958)).
75/ *Id.* at 225-26.
76/ ORS 756.040(1); *Sabin*, 21 Or. App at 213-14, 224.

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that BCC coal is well above market prices and is unlikely to equal market prices in the future.[77/] Under these circumstances, PacifiCorp has an incentive to avoid lower-of-cost-or-market ratemaking in order to ensure that it continues to earn a return for its shareholders on its investment in BCC, just as it had an incentive to avoid consolidation with BCC in 1979 when a comparison with market prices would have similarly benefitted its shareholders.

Regardless of its prior decisions, the Commission has a statutory duty to treat PacifiCorp and BCC in a manner that best balances the interests of customers and investors and ensures fair and reasonable rates.[78/] In this case, the record demonstrates that this can be accomplished through the application of the lower-of-cost-or-market pricing rule.

3. PacifiCorp's critiques of ICNU's calculations are without merit.

ICNU recommends a $6 million reduction to NPC based on its lower-of-cost-or-market analysis for BCC coal.[79/] The calculation of this adjustment is explained in Mr. Mullins' Rebuttal Testimony, as modified by an errata ICNU filed on August 19, 2016, and includes costs associated with capital investment to enable Jim Bridger to burn PRB coal and amortization of the undepreciated investment in BCC.[80/] The Company takes exception to the following aspects of ICNU's calculation: (1) the length of the amortization period ICNU assumed for the regulatory asset created to recognize the undepreciated investment in BCC; (2) the return ICNU assumed on this regulatory asset; (3) the heat content ICNU assumed for PRB coal; and (4) ICNU's decision to analyze BCC in isolation rather than total-plant fueling costs.[81/]

77/ ICNU/100 at 11:5-13:2; Staff/200 at 27:18-47:9.
78/ ORS 756.040(1).
79/ Errata to ICNU/200 at 9.
80/ *Id.* at 7-12.
81/ PacifiCorp Opening Br. at 28.

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a. The Commission should use a 13-year amortization period for the undepreciated investment in BCC and capital investments in Jim Bridger.

In its analysis, ICNU assumed a regulatory asset amortization period of 13 years, which would fully amortize this asset by the end of 2029,[82] corresponding to when Jim Bridger must be depreciated out of Oregon customers' rates pursuant to Senate Bill ("SB") 1547, the State's new "coal-to-clean" and 50% renewable portfolio standard legislation. This is in contrast to the Company's proposed four-year amortization schedule.[83]

The Company argues that a four-year amortization schedule is "reasonable" but provides no basis for this assumption other than the Commission's 2002 decision related to the Trail Mountain mine and its 2005 decision related to the Company's capital investment in the BCC underground mine.[84] Ultimately, the Commission has the discretion to determine the regulatory asset amortization period (including extending it beyond 2030, as SB 1547 does not prohibit the inclusion of coal mine investments in Oregon rates beyond this date), so the Company's position that its four-year amortization period is somehow more "reasonable" than ICNU's or Staff's is baseless.

In a more recent docket involving a mine closure, the Commission authorized a four-year amortization period for PacifiCorp's undepreciated investment in the Deer Creek Mine.[85] It did so, however, because this period "closely mirrors the current depreciable life of the mine."[86] Currently, Jim Bridger is set to depreciate out of Oregon rates in 2025.[87]

82/ ICNU/200 at 9:6-10:3.
83/ PAC/1000 at 24:7.
84/ *Id.* at 24:7-14.
85/ Docket No. UM 1712, Order No. 15-161 (May 27, 2015).
86/ *Id.* at 8.
87/ PAC/1000 at 24:3.

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[redacted][88] [redacted][89] Meanwhile, SB 1547 allows the Commission to extend the depreciation date for Jim Bridger to the end of 2029.[90] It may be in customers' best interest to do this, particularly considering that SB 1547 allows PacifiCorp to seek recovery of decommissioning and remediation costs from Oregon customers associated with Jim Bridger *even if those costs are incurred after the plant is depreciated out of Oregon rates*.[91] Thus, the longer customers continue to receive the benefits of Jim Bridger, the less likely it will be that they will need to pay costs that are incurred after they stop receiving these benefits. An amortization period for the undepreciated investment in BCC that extends through 2029, therefore, is most consistent with recent Commission precedent by balancing the depreciation dates of the underground and surface mines, and better aligns the costs and benefits to customers of the Jim Bridger plant.

Similarly, the Commission should also use a 2029 date for amortization of the capital investment necessary to receive and burn PRB coal. Although the Company's Opening Brief did not address this issue in its response to ICNU, the Company's surrebuttal testimony modified its assumed capital investment amortization period from 2029, which Mr. Ralston used in his rebuttal testimony, to 2025 in order to align it with the current depreciable life of Jim Bridger.[92] As noted above, however, the Company has the option of extending this depreciable life through 2029, and given the fact that SB 1547 may result in customers paying for

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[88] ICNU/102 at 7.
[89] *Id.*
[90] SB 1547 § 1(2).
[91] SB 1547 § 1(6)
[92] PAC/1000 at 29:15-30:2. In his Rebuttal Testimony, Mr. Mullins used Mr. Ralston's capital investment amortization assumptions. ICNU/200 at 9, Confidential Table 1R.

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decommissioning and remediation costs incurred after Jim Bridger is depreciated out of Oregon rates, extending the plant's depreciable life would appear to be in customers' best interest.

b. The Commission should apply a carrying charge of 3.31% to the undepreciated balance.

ICNU also assumes a carrying charge of 3.31% on the balance of the Company's undepreciated investment in BCC, which is the same rate the Commission applied to the undepreciated balance of the Deer Creek Mine.[93/] The Commission selected this rate because it "reasonably reflects the time value of money, and does not represent a return on the undepreciated investment."[94/]

The Company's Opening Brief supports a return at its weighted average cost of capital and argues that ICNU's proposed carrying charge is "unreasonable for the reasons discussed above regarding Staff's similar position."[95/] The Company disagrees with Staff's proposal to use a rate of 3.43% (based on reasoning similar to ICNU's) because it argues that, if the Company had made the decision in 2013 to close the mine by 2017, "it would seek to amortize the mine closure costs and undepreciated investment *before closure in 2017*."[96/] The Company, however, did *not* decide to close the mine in 2013, which is the very basis for Staff's position that the Company acted imprudently.[97/] The assumption of a regulatory asset to account for the undepreciated investment in the BCC mine presupposes that the mine is closed.[98/] If the Company is correct that it should continue to earn a return on its investment in the BCC mine at

93/ ICNU/200 at 10:3-6; Order No. 15-161 at 8.
94/ Order No. 15-161 at 8.
95/ PacifiCorp Opening Br. at 28.
96/ *Id.* at 22 (emphasis in original).
97/ Staff/400 at 2:16-3:6.
98/ PAC/500 at 24:14-19

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its weighted average cost of capital,[99] then there is no basis also to assume the costs associated with the creation of a regulatory asset to recover the Company's undepreciated investment.

c. The Company does not substantiate its claim that ICNU did not adjust PRB coal for heat content.

PacifiCorp also claims that ICNU did not adjust PRB coal volumes for heat content.[100] Other than this blanket statement, however, the Company does not substantiate this claim and does not identify the impact this purported error has on ICNU's calculations.[101] In developing its adjustment, ICNU used the data and workpapers the Company provided. Indeed, Mr. Mullins testified that he prepared his adjustment based on "the data in Mr. Ralston's [Confidential Figure 4]."[102] Accordingly, the Company has not supported this critique of Mr. Mullins' calculation.

d. The Company's argument that BCC should be analyzed in the context of total plant-fueling costs is baseless and leads to an inaccurate analysis.

Finally, the Company criticizes ICNU for analyzing "BCC in isolation, instead of analyzing total plant-fueling costs."[103] Again, the Company makes this assertion without providing any rationale for why its method is preferable. The Company's witness, Mr. Ralston, testifies that "the most accurate and complete way to analyze Jim Bridger plant fuel costs is to look at the total fueling costs not just one element of the fueling plan."[104] Mr. Ralston does not, however, state *why* this is a more "accurate and complete" method.

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[99] PacifiCorp Opening Br. at 22.
[100] *Id.* at 28.
[101] PAC/1000 at 36:2-3.
[102] Errata to ICNU/200 at 9:1-2.
[103] PacifiCorp Opening Br. at 28.
[104] PAC/1000 at 36:4-6.

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It certainly does not explain Mr. Ralston's own assumptions in his calculations. In Confidential Figure 4 on page 26 of Mr. Ralston's Rebuttal Testimony (PAC/500), Mr. Ralston "corrects" ICNU's calculation of the benefits of PRB coal relative to BCC coal. He does so, however, by assuming that *all* coal delivered to Jim Bridger comes from the PRB.[105/] ICNU's adjustment, however, is limited only to the coal that comes from BCC – ICNU does not take issue with the cost of Black Butte or PRB coal that currently is being delivered to Jim Bridger.[106/] Thus, Mr. Ralston's method of calculating the cost of PRB coal to Jim Bridger is not responsive to ICNU's proposed adjustment. Moreover, it results in an inaccurate comparison of the cost of fueling Jim Bridger. Mr. Ralston's Confidential Figure 4 compares the current cost of fueling Jim Bridger – through a combination of BCC, Black Butte, and PRB coal – with the cost of fueling Jim Bridger exclusively with PRB coal, a scenario ICNU has not advocated for in this case. Nevertheless, even Mr. Ralston's figure demonstrates that the cost of fueling Jim Bridger exclusively with PRB coal is still less per ton than customers are paying for BCC coal.[107/]

C. The Commission Should Impose a Moratorium on Modeling Changes in the TAM Until PacifiCorp's Next General Rate Case

Finally, ICNU recommends that the Commission impose a moratorium on modeling changes PacifiCorp can propose in future TAM proceedings until the Company files its next general rate case.[108/] The complexity of the issues raised in this proceeding, as well as the 2016 TAM proceeding, coupled with the relatively brief time frame parties and the Commission

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105/ PAC/500 at 26, Confidential Figure 4, "Mullins/Kaufman Corrected" column, "Tons" row.

106/ ICNU/200 at 9:4-6.

107/ PAC/500 at 26, Confidential Figure 4, "Mullins/Kaufman Corrected Column" and "Bridger Coal Company Total" columns, "Total Comparative Price Per Ton" row, showing a price of $[redacted] for PRB coal and $[redacted] for BCC coal.

108/ ICNU/100 at 16.

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have to evaluate these issues demonstrates that the TAM has outgrown the narrow proceeding it was originally intended to be, particularly when filed separately from a general rate case.[109/] Mr. Mullins testifies that, with the number of additions and work-arounds the Company has introduced, it now can take "over a day of intensive manual financial analysis just to complete a single run from the GRID model."[110/]

Recognizing the complexity of the modeling changes PacifiCorp proposed in the 2016 TAM, the Commission imposed a one-year moratorium on modeling changes.[111/] With the number of issues that have been raised in this proceeding, it is evident that a one-year moratorium is insufficient to ensure that parties are comfortable enough with how the Company models its NPC that they can focus on relatively narrow issues that can adequately be resolved in a nine-month time-frame.

The Company objects to ICNU's proposal, arguing that "rapidly changing circumstances in the energy industry and the power markets require modeling flexibility to ensure the forecast accuracy."[112/] Any "changing circumstances" that are material enough to require yet another change to the GRID model, however, also should be material enough to require the Company file a general rate case.

109/ Docket No. UE 199, Order No. 09-274 at 2 (July 16, 2009) ("When filed on a stand-alone basis, the TAM is intended to be more narrow and streamlined than when the TAM is filed in or processed concurrently with a general rate case").

110/ ICNU/100 at 16:17-18.

111/ Docket No. UE 296, Order No. 15-353 at 2 (Oct. 26, 2015).

112/ PAC/400 at 17:10-11. PacifiCorp's Opening Brief did not discuss ICNU's recommendation regarding an extended moratorium on modeling changes.

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III. CONCLUSION

For the foregoing reasons, ICNU recommends that the Commission reduce PacifiCorp's 2017 forecasted Oregon-allocated NPC by $8 million at a minimum. The Company's application presents an inaccurate NPC forecast because it double-counts day-ahead wind and load integration costs, unnecessarily increasing NPC by $1.9 million. It also proposes unfair and unreasonable rates because it projects deliveries of coal to Jim Bridger at a price that is well above what is available in the market for comparable coal supplies, increasing costs to Oregon customers by $6 million. ICNU also recognizes that other parties have proposed additional adjustments that would result in a further reduction to the Company's NPC. A number of these adjustments are similar to ones ICNU has recommended in prior proceedings. ICNU, therefore, reserves the right to respond to, and potentially support, the recommendations of other parties in this proceeding in its cross-answering brief.

Dated this 26th day of September, 2016.

Respectfully submitted,

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