Portland General Electric Company
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August 28, 2013

Email/US Mail
puc.filingcenter@state.or.us

Oregon Public Utilities Commission
Attention: Filing Center
3930 Fairview Industrial Dr. SE
Salem, OR 97302-1166

RE: **UE 262 PGE 2014 General Rate Case**

Attention: Filing Center

Enclosed for filing in the captioned docket are an original and five copies of:

Surrebuttal Testimony of Portland General Electric Company:

- **PGE Exhibit 2000**

Also enclosed are an original and three copies of:

- **Exhibits on CD (non-confidential portions)**
  - **Exhibit 2001**
  - **Exhibit 2002**
  - **Exhibit 2003**
  - **Exhibit 2005**
- **Exhibits on CD (confidential portion)**
  - **Exhibit 2004 (Subject to Protective Order No. 13-042)**

These documents are being served upon the UE 262 service list. Confidential portions are subject to Protective Order No. 13-042 and therefore not to be posted on the OPUC website.

This document is being filed by electronic mail with the Filing Center. An extra copy of the cover letter is enclosed. Please date stamp the extra copy and return to me in the envelope provided.

Thank you in advance for your assistance. If you have any questions or require further information, please call Chris Liddle at (503) 464-7458. Please direct all formal correspondence and requests to the following email address: pge.opuc.filings@pgn.com.

Sincerely,

Patrick G. Hager

Patrick G. Hager
Manager, Regulatory Affairs

cc: UE 262 Service List
Encls:

CERTIFICATE OF SERVICE

I hereby certify that I have this day caused **UE 262 SURREBUTTAL TESTIMONY AND EXHIBITS** to be served by electronic mail to those parties whose email addresses appear on the attached service list for OPUC Docket No. UE 262 .

DATED at Portland, Oregon, this 28th day of August 2013.

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Before the Public Utility Commission

of the State of Oregon

UE 262
General Rate Case Filing

Portland General Electric Company

Surrebuttal Testimony and Exhibits

August 28, 2013

Table of Contents

I. Introduction

Q. Please state your names and positions with Portland General Electric ("PGE").

A. My name is Patrick G. Hager. I am a Manager of Regulatory Affairs at PGE. I am responsible for analyzing PGE's cost of capital.

My name is Jardon Jaramillo. My position is Senior Investment Analyst in the Corporate Finance Department.

Our qualifications were previously provided in PGE Exhibits 500 and 1100.

Q. What is the purpose of your testimony?

A. The purpose of our testimony is two-fold. First, we respond to the proposals made by the OPUC Staff (Staff), CUB and ICNU. Second, we provide additional detail regarding pension costs, PGE's pension history, and our pension proposal, to clear up some misconceptions presented by other parties.

Q. What is PGE's request in this docket regarding pension cost recovery?

A. PGE requests that the Commission authorize the use of a balancing account as originally requested in our direct testimony (PGE Exhibit 500). This balancing account will track the differences between forecasted and actual pension expense and include the carrying costs of the prepaid pension asset. The balancing account would be formally revisited during a general rate case. Alternatively, if the Commission rejects making any changes to the regulatory treatment of pension costs at this time, then PGE believes that Staff's proposal in its rebuttal testimony should be used.

Q. What is Staff's proposal?

A. Staff's proposal is to allow PGE to recover our forecasted 2014 test year FAS 87[1] pension expense of $23.6 million and allow for deferred accounting treatment to address the difference between forecasted and actual pension expense in 2014. However, by reverting to FAS 87 expense recovery (i.e., removing the prepaid pension asset) PGE would also remove the associated accumulated deferred tax benefit from rate base.

Q. Why should this deferred tax benefit be removed from rate base?

A. If PGE is not allowed to earn a return on company financed cash contributions then the associated tax benefit should be removed from PGE's 2014 rate base. Both the costs and benefits associated with the prepaid pension asset should either be included in rate base or removed from rate base. It is inappropriate regulatory treatment for customers to benefit from this deferred tax offset to rate base, while the prepaid pension asset that has created this benefit is excluded from ratemaking.

Q. How much does this accumulated deferred tax benefit represent for 2014?

A. The forecast of average accumulated deferred taxes related to the prepaid pension asset for 2014 is approximately $33 million, or approximately $3.9 million in revenue requirement.

Q. Have other Oregon utilities removed this accumulated deferred tax benefit?

A. Yes. PGE understands that PacifiCorp has excluded this benefit from their rate base for a number of years. Again, because PacifiCorp is not earning a return on their company financed cash contributions comprising its prepaid pension asset, it has removed the corresponding deferred tax offset in rate base to create an appropriate matching of costs and benefits.

[1] As defined in PGE Exhibit 500, page 27, PGE records its pension expense based on Accounting Standards Codification (ASC) 715, "Compensation – Retirement Benefits," which prior to July 1, 2009, was known as Statement of Financial Accounting Standards No. 87 or "FAS 87."

Q. How is the remainder of your testimony organized?

A. In Section II, we discuss the proposals made by CUB, ICNU and Staff and how they compare to PGE's proposal. Section III addresses several issues with CUB's analyses as presented in their rebuttal testimony.

II. Parties' Proposals

Q. What do the parties propose regarding PGE's expected pension costs in 2014?

A. As stated in their opening and rebuttal testimonies, CUB proposes that, beginning in 2014, the recovery of pension costs in prices should be based on a five-year amortization of cash contributions to the plan and that FAS 87 pension expense would no longer be used to set prices. As an alternative, CUB proposes using a three-year average of historical pension expense to calculate PGE's test year pension costs.

Similar to CUB's alternative proposal, ICNU continues to support using PGE's 2012 pension expense for the 2014 test year. They also state that they would be supportive of CUB's proposal to use a historical three-year average.

Staff's proposal is to include PGE's forecasted 2014 FAS 87 test year expense in retail prices (as has been done in previous general rate cases), with the variance between forecasted and actual 2014 FAS 87 expense subject to deferred accounting.

Q. Do any of these proposals resolve all regulatory issues with PGE's pension costs?

A. No. As we discuss below, CUB's and ICNU's proposals have fatal flaws, creating significant problems and issues. Staff's proposal, however, appears to resolve the immediate FAS 87 expense issue, assuring that PGE collects only its actual pension expense in 2014. Staff proposes that the prepaid pension asset issue be resolved in the generic pension docket, UM 1633.

A. CUB's Proposal

1. <u>Cash-based recovery</u>

Q. Please explain the issues with CUB's proposal.

A. As discussed in PGE Exhibit 1800, if we were to switch to a 'cash-based' pension cost recovery, then PGE's prepaid pension asset would have to be addressed quickly. If PGE were to move from including FAS 87 expense in prices to cash-based recovery, as CUB proposes, without a regulatory remedy, PGE would forego recovery of the prepaid pension asset (that would otherwise be recovered over time through FAS 87 expense) and incur a $316 million charge to the equity component of its balance sheet. This would, of course, significantly increase PGE's debt-to-equity ratio, which could cause the rating agencies to lower PGE's bond rating. It also creates a mismatch between PGE's regulatory recovery and what is reflected on PGE's income statement, creating earnings volatility. Put simply, CUB's proposal to use a cash-based method is incomplete and would cause significant financial harm to PGE and our customers.

Q. CUB mentions that their proposal is similar to the way Idaho Public Utility Commission regulates the Idaho Power Co. (IPC). Is this relevant to PGE's UE 262 filing?

A. No. The regulatory environment and history of pension treatment in Idaho is very different from Oregon. In Idaho, cash-based pension cost recovery has been the norm for many years. In addition, when Idaho made the switch to cash-based recovery, IPC did not have a significant prepaid pension asset or liability on its balance sheet. Trying to relate any proposal for PGE with how IPC is regulated in a different state involves many different variables. CUB provides no analysis or support for how Oregon regulatory treatment of pension relates to Idaho.

2. <u>Historical FAS 87 expense recovery</u>

Q. Are there problems with CUB's and ICNU's historical FAS 87 expense proposals?

A. Yes. CUB and ICNU each propose the use of historical FAS 87 expense, reasoning that FAS 87 expense can be difficult to forecast. As we discussed in PGE Exhibit 1800, this kind of historical treatment ignores known and measurable changes in the status of PGE's pension plan, such as significant changes in the pension plan discount rate and/or the rate of return on the plan's investments – both of which have occurred in recent years. In addition, using a test year forecast for FAS 87 expense has been the regulatory treatment in Oregon since FAS 87's inception. Furthermore, any variance between forecast and actual cost is addressed by PGE's balancing account proposal as well as Staff's proposal for deferred accounting treatment.

Not only are CUB's and ICNU's historical expense proposals an erosion of test year ratemaking, they are 'results based'. That is, CUB and ICNU rely on a single or an average of historical values, completely ignoring independent professional forecasts based on current market and company data. As with previous uncontested test year pension expense forecasts, PGE's 2014 FAS 87 expense was calculated by a third-party professional actuary with expansive education and experience in the field of pension accounting.

B. ICNU's Proposal

Q. What other support does ICNU offer for their proposal?

A. ICNU states that any change in current regulatory treatment of pension expense would "pre-judge the results of the UM 1633 proceeding," effectively predetermining the outcome of the UM 1633 docket (ICNU Exhibit 200, page 3, lines 7-8). ICNU's position effectively restricts PGE from the opportunity to recover a return on its prepaid pension asset. In addition, ICNU's argument is inconsistent when they themselves propose a change to the current regulatory treatment of pensions (i.e., averaging historical actual expenses).

ICNU also discusses in direct testimony that their estimate for pension expense is "in line" with PGE's long-term forecast of expense from 2013 through 2028 (ICNU Exhibit 100, pages 3-4). ICNU wants the benefit of a balancing account (i.e., stable expense forecast), but leaves PGE with all of the risks (i.e., volatile actual expense). Fairness would require that the benefits and risks go together.

Q. ICNU describes PGE's earnings as "robust" (ICNU Exhibit 200, page 4, line 8). Is this description accurate?

A. No. As presented in PGE Exhibit 2001, PGE's regulated adjusted earnings in the last decade (2003-2012) have averaged approximately 116 basis points below our Commission-authorized return on equity (ROE) and from 1987 to 2012 PGE's regulated adjusted earnings on average are approximately 84 basis points below our authorized level.

Q. ICNU asserts that Staff's pension survey does not support PGE's request in this case (ICNU Exhibit 200, page 4, lines 9-12). Is this a reasonable interpretation of the survey results?

A. Not really. ICNU claims their position is supported because Staff's survey of pension recovery methods found that 46% of all utility commissions allow some form of return on the prepaid pension asset. Given how recently these issues have developed, to have approximately half of utility commissions address the prepaid pension asset is a significant percentage. Furthermore, if states (such as Idaho) that do not use FAS 87 as a basis for recovery (negating the need for the return on a prepaid pension asset) are removed, the percentage increases to 55%. In addition, Staff's survey indicated that 15 commissions have recently performed, or are currently performing, investigations into pension related costs. In other words, a significant number of commissions are investigating pension-related costs. It is clear that the prepaid pension asset issue is significant and gaining importance among state commissions.

C. Staff's Proposal

Q. What is Staff's proposal?

A. Staff's proposal is to include PGE's forecasted 2014 FAS 87 test year expense in retail prices, with any variance between the forecasted and the actual 2014 FAS 87 expense to be subject to deferred accounting.

Q. Does Staff's proposal address the concerns raised by CUB and ICNU regarding forecasting FAS 87 expense?

A. Yes. Both CUB and ICNU are concerned that the 2014 forecasted FAS 87 pension expense will be different than the 2014 actual FAS 87 pension expense. Staff's proposal would grant PGE the opportunity to recover its projected cost for the test year, but any variance would be subject to a deferral.

Q. Are there issues with Staff's proposal?

A. Yes. Staff's proposal does not address the prepaid pension asset and it is only relevant to 2014 costs. However, they do indicate that UM 1633 will allow for continued review and will ultimately decide the proper cost recovery method going forward. Consequently, if the Commission determines in UM 1633 that pension recovery should be changed to address the prepaid pension asset, Staff's proposal offers a reasonable alternative for both PGE and customers during the interim.

Q. Has Staff defined the parameters of their proposed deferred accounting treatment?

A. No. Again, PGE agrees with Staff's deferred accounting treatment in principle with an earnings test that allows variances to be collected or refunded such that PGE's regulated adjusted ROE does not exceed (for collections) or fall below (for refunds) PGE's Commission-authorized return on equity. This is consistent with the earnings test specified for PGE's four capital project deferrals in UE 215[2].

[2] See OPUC Order No. 10-478.

III. Detailed Response to CUB's Analysis

Q. Can you summarize what is discussed in this section?

A. Yes. Throughout their rebuttal testimony, CUB provides information and analyses that are, at times, skewed and misleading and, at other times, simply incorrect. This section attempts to address the issues in CUB's rebuttal testimony, demonstrating that CUB's rebuttal does not accurately depict PGE's pension plan, pension costs, or pension history.

A. Pension Accounting

Q. Is the term "prepaid pension asset" a misnomer, as CUB suggests (CUB Exhibit 200, page 2, line 10)?

A. No. The prepaid pension asset refers to the current status of a set of three entries or components that together form the prepaid pension asset at any given point in time. The prepaid pension asset is calculated as:

(1a) Defined benefit pension plan assets
+ (1b) Amounts included in accumulated other comprehensive loss (AOCL)
- (2) Pension Benefit Obligation (PBO)
= (3) Prepaid pension asset (or liability)

If the resulting balance is negative, it is a liability; if the balance is positive (as it is for PGE), it is an asset.

Q. Has PGE previously discussed the differences between FAS 87 expense and PPA (Pension Protection Act) required cash contributions?

A. Yes. PGE's direct testimony (PGE Exhibit 500) discusses in detail the difference between funding rules for Generally Accepted Accounting Principles (GAAP) purposes and those for PPA purposes. The reason the prepaid pension asset has grown is due to the differences in funding requirements of FAS 87 and the PPA. CUB's confusion with this fundamental issue is evidenced by their statement that GAAP is represented by the PPA (CUB Exhibit 200, page 5, line 7). This is simply incorrect. The two requirements are quite different. For example, the PPA is a federal law, whereas FAS 87 was issued by the Financial Accounting Standards Board (FASB) in 1985, whose primary purpose is to develop Generally Accepted Accounting Principles (GAAP) within the United States.

Q. Is FAS 87 still relevant?

A. Yes. A fundamental objective of FAS 87 is to recognize the compensation cost of an employee's pension benefits over the employee's approximate service period. The FASB believes that the understandability, comparability, and usefulness of pension information is improved by narrowing the past range of methods for allocating or attributing the cost of an employee's pension to individual periods of service[3]. FAS 87 is currently the best way to match the annual experience (i.e., market changes, employee changes, benefit payments, etc.) of a plan with its annual accounting expense.

Q. CUB appears to believe that PGE is seeking pension treatment based on its cash contributions minus FAS 87 amounts (CUB Exhibit 200, page 16, lines 7-8). Is this what PGE is requesting?

A. No. PGE is <u>not</u> asking for a change in the current FAS 87 recovery method and we are <u>not</u> asking for the return of previous cash contributions to the plan. As we have discussed in our previous testimony, the prepaid pension asset will eventually be amortized through FAS 87 expense with or without a change in the treatment of pension costs[4]. PGE is asking to be compensated through a return on the prepaid pension asset, as we are for any other capital investments funded through long-term sources of debt and equity. This does not change or

[3] http://www.fasb.org/summary/stsum87.shtml
[4] PGE Exhibit 1800, pages 9-10.

confuse our accounting structure as CUB suggests. Our accounting would remain "accrual based" with or without the return on the prepaid pension asset.

Q. Does PGE's balancing account proposal change the basis of PGE's accounting structure?

A. No. It would remain accrual based.

Q. CUB asserts that incurred[5] and accrued or accrued vs. cash accounting costs cannot/should not be mixed and would cause double-counting (CUB Exhibit 200, page 16, line 7). Is this correct?

A. No. PGE is not mixing methodologies. In fact, CUB has misconstrued what PGE is requesting and appears to mix accounting terminologies, which creates further confusion. Again, at its simplest, PGE is requesting recovery of its FAS 87 expense and a return on its prepaid pension asset both of which are based on accrued accounting under GAAP. There will be no change to PGE's accounting structure, with or without PGE's proposed change in pension recovery, and no double-counting of pension-related costs.

Q. Does CUB confuse balance sheet and income statement accounting (CUB Exhibit 200, page 4, lines 17-19), resulting in false conclusions?

A. Yes. CUB confuses the differences between what is reported on a company's balance sheet and income statement. In their testimony, CUB argues that both FAS 87 *expense* and the prepaid pension *asset* should be on a single financial report (either the balance sheet <u>or</u> income statement) to warrant the pension recovery treatment PGE is requesting in this docket. Yet, nearly every component of a utility's rate base has a balance sheet (e.g., net plant) and income statement (e.g., depreciation or amortization) component. Just as there is

[5] An expense that has occurred (e.g., products or services have been delivered) is incurred. An expense recognized in the books before it is paid for is accrued.

no double counting of "return on" and "return of" plant investment, there is no double counting of pension costs in PGE's proposal. A company's balance sheet (assets, liabilities, and equity) and income statement (sales, expenses, and earnings) do not report the same items, or the same time period[6]. PGE reports pension accounting (income statement) and funding (balance sheet) consistent with SEC requirements.

Q. CUB states that PGE's request in this case is contrary to its arguments in Docket No. UE 79 (1991 test year) (CUB Exhibit 200, page 3, lines 14-19). Is this correct?

A. No. The PGE testimony (provided as PGE Exhibit 2002) that CUB references is over twenty years old and before the PPA was enacted. In addition, the testimony was written soon after FAS 87 was issued. Finally, that testimony did not even discuss pension costs. CUB draws conclusions from this brief section of dated testimony but the testimony discusses a change in accounting treatment for postretirement costs <u>other than pensions</u>, as CUB points out later in their testimony (CUB Exhibit 200, page 16). Furthermore, the "used and useful" standard is never mentioned, nor is matching the timing of service with the timing of rate cases.

B. Prudence

Q. Several times in their testimony[7], CUB suggests that maybe PGE has mismanaged its pension plan. Have PGE's actions related to its pension been prudent?

A. Yes. PGE's actions have and continue to be prudent and Staff Exhibit 500 (pages 6-7) supports the fact that PGE's pension costs were prudently incurred. PGE has prudently managed its pension plan, with its pension assets performing at the top of their class to the benefit of customers. As discussed in PGE's Exhibit 1800, we have outperformed similar

[6] The balance sheet provides financial information at a <u>point</u> in time (e.g., end of month, end of quarter), while the income statement provides financial information for a <u>period</u> of time (e.g., during a month, during a quarter).
[7] CUB Exhibit 200, pages 7-10.

sized pension plans for the last five years, being in the top 1% of funds over the five years ending March 31, 2013 (PGE Exhibit 1800, page 6, lines 7-8). Additionally, as seen in PGE Exhibit 2003, from the period beginning January 1, 1995 through June 30, 2013 (18.5 years), PGE's total pension fund is in the top 17% of similar sized plans.

Q. CUB argues that PGE is attempting to circumvent the regulatory process by not subjecting costs to OPUC approval at the time that they were incurred (CUB Exhibit 200, page 14, lines 20-21). Is this true?

A. No. As we previously noted, there have been numerous general rate cases since FAS 87 was introduced in 1987 during which PGE included its pension expense. Parties have had opportunities to pursue discovery on any aspect(s) of PGE's pension plan with which they were concerned. Furthermore, similar to a generating plant that begins operations prior to a test period, PGE is not precluded from subsequently asking for a return on its investment. For example, the first phase of PGE's Biglow Canyon wind farm came online in 2007 and PGE began cost recovery in 2008 without regulatory treatment of the interim period.[8]

C. Retroactivity

Q. What does CUB suggest by their argument of "ex-post" returns (CUB Exhibit 200, page 8, line 6) and retroactive ratemaking policy (CUB Exhibit 200, page 5)?

A. CUB suggests that providing a return on the prepaid pension asset would be retroactive ratemaking; as though PGE would be recovering its carrying costs related to historical periods. This is incorrect. PGE is simply requesting a return on its prepaid pension asset <u>beginning in 2014</u>. Contrary to CUB's belief (CUB Exhibit 200, page 5, line 11), PGE previously addressed this issue of retroactive ratemaking in PGE Exhibit 1800 (page 13,

[8] See Docket No. UE 188.

lines 16-21). Past carrying costs for pension expenses are not included in PGE's request in this case.

Q. Has PGE in fact absorbed the carrying costs associated with the prepaid pension asset for years 2013 and prior?

A. Yes. However, we note that PGE did file for a deferral of its excess pension costs and carrying costs associated with the prepaid pension asset in 2012, but any action on this deferral has been delayed until the generic pension docket (UM 1633) is concluded.

Q. Is CUB accurately depicting the buildup and status of PGE's prepaid pension asset?

A. No. In their analyses of PGE's prepaid pension asset, CUB considers the prepaid pension asset growth only on a net basis (i.e., cash vs. expense), which skews the perception of the underlying activity and events in the recent past. For example, while cash contributions will increase the prepaid pension asset, pension expense can grow (through negative expense) and reduce (through positive expense) the size of the prepaid pension asset. This occurs because FAS 87 expense effectively amortizes the prepaid pension asset. Consequently, the greater the pension expense for the year, the more the prepaid pension asset will shrink.

Q. Can you provide an example of how the numbers are skewed in CUB's analysis?

A. Yes. An example is when CUB states the prepaid pension asset (cost) grew by $5 million per year on average following the PPA (2008 forward) or a total of $25 million (CUB Exhibit 200, page 5, lines 17-18). In reality, though, PGE contributed more than twice CUB's estimate (approximately $56 million or $11.2 million per year on average) in the years following the PPA's enactment.

Q. What are the components of PGE's prepaid pension asset in 2014?

A. As we noted above, PGE has contributed $56 million in cash to its prepaid pension asset in the last couple of years and $66 million since 2005. Over that same time period, negative pension expense has totaled only $2.4 million. PGE's projected prepaid pension asset balance for 2014 is $74 million, a difference of only $8 million between the level of the prepaid pension asset and what PGE has contributed in cash payments since 2005.

D. Shareholder Risk

Q. CUB argues that there is no shareholder risk involved if PGE is allowed an opportunity to earn a return on its prepaid pension asset (CUB Exhibit 200, page 8). Is that accurate?

A. No. As with any other investment, shareholder risk is influenced by PGE's prudence and ability to manage its assets. CUB's insistence that shareholders should not have the opportunity to earn on a prudently incurred investment (CUB Exhibit 200 page 8, lines 11-12) is counter to the regulatory compact. Shareholders will be required to continue to fund cash payments into the pension plan for a considerable length of time with or without the opportunity for a return on the prepaid asset.

E. Prepaid Pension Asset vs. Depreciating Asset

Q. Please discuss CUB's arguments regarding the prepaid pension asset being different from a depreciating "revenue producing" asset.

A. CUB makes four arguments that we address individually:

1. "Prepaid pension cost [asset] is not an asset at all. Rather, it is an accounting expense" (CUB Exhibit 200, page 12, line 22). Here CUB has confused the balance sheet and income statement. The prepaid pension asset (or "prepaid pension cost" as CUB refers to it), which appears on the balance sheet, is indeed an asset and is

comprised of the defined benefit pension plan assets, PBO, and amounts included in AOCL. An expense (such as FAS 87 expense) appears on the income statement. PGE has asked for a return on the prepaid pension asset, as it receives for any asset in its regulated ratebase.

2. "[The prepaid pension asset] is not an income producing asset, or an asset providing current service to ratepayers" (CUB Exhibit 200, page 13, lines 3-4). PGE is not aware of any definition for "income producing asset", nor does this term have any meaning or bearing on the comparison. The pension plan is providing current service to customers in the form of PGE employees (who are the beneficiaries of the plan and for whom the pension is a vital component of their total compensation).

3. "[T]he capital assets that are generally included in rate base have demonstrated useful lives, with parameters that are reviewed and agreed upon by industry standards, the utility, the Commission and interested parties" (CUB Exhibit 200, page 13, lines 6-7). The pension plan certainly has a "useful life". The plan, closed to participants in February 2009, will inevitably reach the end of its life when the last participants are paid out, or if the plan is terminated earlier (e.g., lump sum payouts or annuitization). It has been reviewed and agreed upon by industry standards.

4. CUB also argues that the "Company has provided no evidence that the prepaid pension cost will ever 'depreciate' to zero" (CUB Exhibit 200, page 13, lines 14-16). This argument is incorrect. PGE provided this information in PGE Exhibit 1800, page 10, lines 4-7 and discussed this in PGE's response to CUB Data Request No. 276. Attachment 276-A of PGE's response to CUB Data Request No. 276 is provided as PGE Confidential Exhibit 2004.

Q. Will the prepaid pension asset eventually reach a zero balance?

A. Yes. As we discussed previously, FAS 87 expense does amortize the prepaid pension asset. So as PGE's cash contributions begin to taper off and PGE continues to incur FAS 87 expense, the prepaid pension asset will continue to shrink in size, eventually reaching a zero balance.

F. FAS 87 Projections

Q. Are long-term projections subject to some unpredictability?

A. Yes. There is some unpredictability to these forecasts, which supports the need for PGE's requested balancing account treatment or Staff's deferred accounting proposal. For its annual and test year FAS 87 expense, PGE uses a forecast of near-term expense that is more accurate than the long term projections provided in PGE Exhibit 503C. Elements of future liabilities are included in the FAS 87 expense in order to reflect the time-value of money related to a company's current liabilities. Consistent with GAAP and FASB recommendations, PGE's annual expense is meant to reflect annual experience. PGE's pension plan obligations do fluctuate from year to year dependent on participant experience and market returns among other things, but this does not alter whether PGE is required to make a cash contribution during the year. Once pension expense has been recognized on PGE's income statement, it affects PGE's earnings for that year.

Q. Please explain the yearly variance between PGE's expected return on pension assets and the actual return on plan assets.

A. The purpose of having an expected return on assets is not to accurately forecast the real market returns for the year. No one, not CUB, not PGE, or any expert can accurately forecast asset returns from year to year, over the long term. The proper way of deriving an expected return on assets is through estimating an average of the peaks and troughs. CUB seems to be suggesting that not only are PGE's market estimates inaccurate, but that they are low, inflating the forecasted amount of FAS 87 expense (CUB Exhibit 200, page 20, lines 5-11). PGE's current forecast of long-term pension asset returns is actually higher than the market benchmarks and higher than what our actuary has recommended, supporting our better than average market returns over the last 18+ years. CUB averages our returns from 1989 to 2012 in order to show that we have beaten our estimates. However, their analysis is skewed because it does not include any year that had negative returns. As shown in PGE Exhibit 2005, if these negative return data are included, the average return is lowered by over 400 basis points from 15.4% on average to 11.1%. In addition, in years where there are negative returns, pension assets shrink, which reduce the earnings potential in future years, even when returns are high.

G. Other Items

Q. Are there issues with other analyses performed by CUB in their rebuttal testimony?

A. Yes. First, throughout CUB Exhibit 200, CUB is selective in their use of data, presenting a variety of analyses using PGE numbers that attempt to illustrate their points. In a number of these analyses, CUB discusses points in time when the prepaid pension asset grew, but fails to recognize that the prepaid both grows and contracts from year to year due to the interplay between pension expense and cash contributions.

Second, in their historical analyses, CUB generalizes that PGE has over-recovered on its pension costs, but CUB fails to use or even mention an earnings review for any of the periods they discuss (CUB Exhibit 200). As evidenced in PGE Exhibit 2001, from 1987-2012, PGE under-earned by an average of almost 85 basis points and during the Enron period, which CUB mentions, PGE under-earned by an average of over 125 basis points. Also within their analysis covering the period of Enron ownership, CUB seems to be inferring that PGE's asset-to-liability ratio was reduced due to Enron's ownership. However, at that point in time, PGE's pension assets were still greater than the liabilities. More important to the plan becoming underfunded (and one of the reasons PGE has repeatedly mentioned) was the market crash of 2008, which affected all pensions across the nation.

Third, in yet another CUB analysis[9], it is unclear what PGE could have done differently from the steps taken in 1999-2000. Had PGE made a cash payment (as CUB seems to be suggesting), expense would have been even lower. Both of these concurrent events would have caused the prepaid pension asset to grow even larger.

Q. Are there issues with CUB's statement that under PGE's proposed treatment customers would be paying more to invest in the plan than the plan is earning (CUB Exhibit 200, page 20, lines 15-16)?

A. Yes. First of all, PGE is required by the federal government to make these cash contributions. These are not optional payments or investments into PGE's pension plan, they are mandatory. Second, PGE's pension assets are invested in a basket of securities, bonds, and mutual funds that earn a variety of different rates. Because a large portion of these assets are invested in the bond market, the average expected return is reduced for the entire asset pool. So while PGE's expected asset return for 2014 is 7.5%, there are a variety of risk profiles and expected returns (some higher and some lower) that make up this forecast.

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[9] CUB Exhibit 200, Table 1 and discussed in CUB Exhibit 200, pages 11-12.

Q. Please discuss CUB's arguments regarding timing (CUB Exhibit 200, page 14).

A. As CUB suggests, timing is important and at the crux of the issue with pension costs. PGE is using investor supplied funds to meet federally required cash contributions, increasing the prepaid pension asset. These contributions will eventually amortize through FAS 87 expense, but in the meantime, PGE is incurring the uncompensated carrying costs involved in making these contributions. This is the timing issue that is integral to pension costs. However, in their discussion of timing, CUB once again attempts to obfuscate the issue by discussing the components of pension expense and how they relate to the current period (CUB Exhibit 200, page 14). All five components of pension expense are a reflection of the pension cost for the current period. That is the purpose of FAS 87 expense as discussed above. Finally, it is unclear how several decades of returns are automatically generated for PGE (CUB Exhibit 200, page 14, line 19) when we are seeking a return on the prepaid pension asset on a prospective basis, beginning in 2014.

IV. Summary of PGE's Proposal

Q. Please summarize PGE's proposal.

A. PGE's original proposal for a balancing account addresses concerns raised by CUB and ICNU, and provides PGE with the opportunity to recover prudently incurred costs. We believe our proposal is the correct one but given that there is a generic docket on pensions (UM 1633), a reasonable alternative would be to use Staff's method, which has precedence, while UM 1633 is resolved.

Staff's proposal of using PGE's forecasted 2014 test year FAS 87 pension expense of $23.6 million (including the removal of the accumulated deferred tax benefit associated with the prepaid pension asset) and deferred accounting treatment provides PGE with a reasonable opportunity to recover its FAS 87 expense, while eliminating the risk to customers that the actual expense incurred for 2014 will be different than forecasted.

Q. Does this conclude your testimony?

A. Yes.

List of Exhibits

PGE Exhibit	Description
2001	PGE Earnings Test
2002	UE 79 PGE Exhibit 3D, Pages 15-16
2003	Pension Fund Performance (1/1/95 - 6/30/13)
2004C	Projection of Prepaid Asset (2013 - 2100)
2005	Average Return on Pension Assets (1989 - 2012)

Earnings Test from 1987 to 2012

Year	Regulated Adjusted*	Allowed per Rate Case*	Difference
1987	11.93%	12.75%	-0.82%
1988	12.46%	12.75%	-0.29%
1989	11.14%	12.75%	-1.61%
1990	13.15%	12.75%	0.40%
1991	9.32%	12.50%	-3.18%
1992	8.68%	12.50%	-3.82%
1993	7.67%	12.50%	-4.83%
1994	8.27%	12.50%	-4.23%
1995	18.06%	11.60%	6.46%
1996	15.00%	11.60%	3.40%
1997	15.31%	11.60%	3.71%
1998	12.75%	11.60%	1.15%
1999	9.83%	11.60%	-1.77%
2000	11.17%	11.60%	-0.43%
2001	9.65%	11.60%	-1.95%
2002	8.09%	10.50%	-2.41%
2003	7.69%	10.50%	-2.81%
2004	11.67%	10.50%	1.17%
2005	6.64%	10.50%	-3.86%
2006	5.02%	10.50%	-5.48%
2007	11.58%	10.10%	1.48%
2008	10.19%	10.10%	0.09%
2009	8.27%	10.00%	-1.73%
2010	9.06%	10.00%	-0.94%
2011	11.00%	10.00%	1.00%
2012	9.48%	10.00%	-0.52%
1987-2012	**10.50%**	**11.34%**	**-0.84%**
1998-2012	**9.47%**	**10.61%**	**-1.13%**
2003-2012	**9.06%**	**10.22%**	**-1.16%**

*As reported in PGE's Results of Operations Reports, 1987-2012

Q. How does PGE assure that it receives competitive contracts for provision of employee medical benefits?

A. One way in which we accomplish this is through our Pay Choices program. PGE offers its non-union employees a "menu" of health care options from competing providers. These include two indemnity plans and four different Health Maintenance Organization (HMO) plans. Each HMO plan is competitively bid each year and offers a unique mix of services and costs. Participating health care providers must provide competitive rates to retain "market share" of the PGE work force.

Q. Please explain the increase to non-medical benefits.

A. We project that an increase of $3.3 million will be necessary in 1991 to bring employees up to market median. We project increases in Company contributions for retirement benefits.

Post-Retirement Benefits

Q. Please explain PGE's proposed accounting change in 1991 for post-retirement benefits other than pensions.

A. We plan to adopt, effective January 1, 1991, the Financial Accounting Standards Board's (FASB) proposed Statement of Financial Accounting Standards (SFAS) No. 87, "Employers' Accounting for Post-Retirement Benefits Other Than Pensions". In brief, the new guidelines change the method for recognizing post-retirement benefits other than pensions from a cash basis to an accrual basis. PGE will recognize the cost associated with providing such benefits (primarily post-retirement medical and life insurance) during the years that its employees provide service to the Company. In the past, PGE has recognized such costs (when paid) during an employee's retirement years.

Q. Is the proposed change consistent with industry standards?

A. Yes. The accrual basis of accounting is generally preferable to cash basis accounting. The new method better matches costs with benefits and is similar to PGE's accounting method for pensions.

Q. What is the effect of the change on PGE in 1991?

A. Adoption of the new guidelines will increase recorded expenses by $1.5 million. The amount is based on actuarial estimates.

Q. When does PGE expect FASB to issue the new guidelines and what is the expected effective date?

A. We expect FASB to release SFAS 87 during the latter part of this year, with an effective date of January 1992.

Q. Why is PGE proposing to adopt the statement early, and what financial effect will that have on customers?

A. We support the proposed statement and note that early adoption of statements is always encouraged by FASB. Early adoption will more closely match the costs of current service with the benefits received by our current customers. By starting in 1991, we also need to accrue slightly less money on an annual basis to reach the same end result than if we waited until 1992.

PGC Allocable Billing to PGE

Q. What change is the Company proposing for PGC costs allocated to PGE?

A. PGC provides PGE and other PGC subsidiaries with certain services, such as investor relations, legal advice, and management, that are more efficiently performed by the holding company than by each company individually. For many of these services, PGC directly bills PGE the fully allocated cost on the basis of the amount of service used, usually expressed as a function of employee time. For other services, however, direct billing of these costs is not possible and allocation is necessary. In 1986, when the holding company was formed,

	Ending June 30, 2013 1/1/95 - 6/30/13	Rank
Total Fund	9.70%	17
Total Plan Policy Index	8.90%	42
Corporate $250M-$1B Median	8.70%	
Total Plan w/o PE	9.50%	20
Total Plan w/o PE Policy Index	8.90%	41
Corporate $250M-$1B Median	8.70%	

Average Return on Pension Assets 1989-2012

Year	Actual %	Expected %
1989	23.59%	8.50%
1990	0.45%	8.50%
1991	24.77%	8.50%
1992	9.26%	8.50%
1993	21.58%	8.50%
1994	-2.07%	8.50%
1995	26.34%	8.50%
1996	15.09%	8.50%
1997	24.03%	9.00%
1998	10.41%	9.00%
1999	18.22%	9.00%
2000	0.99%	9.00%
2001	-1.69%	9.00%
2002	-10.93%	9.00%
2003	29.78%	9.00%
2004	11.13%	9.00%
2005	7.47%	9.00%
2006	13.71%	9.00%
2007	8.74%	9.00%
2008	-26.66%	9.00%
2009	26.90%	8.50%
2010	15.02%	8.50%
2011	3.46%	8.25%
2012	17.51%	8.25%
Actual Average 89-12	**11.13%**	
CUB's Average	**15.42%**	