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IDAHO PUBLIC UTILITIES COMMISSION

ICAN

Idaho Community Action Network

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The Idaho Community Action Network opposes approval of the Stipulation in Case No. IPC-E-04-15 concerning the "Fixed Cost Adjustment Mechanism" (FCA or "Decoupling"). Decoupling is contrary to the interests of Idaho Power's customers; instead it favors the utility and its shareholders. Worse, the general public is completely unaware of this significant change in the way their rates will be set in the future. Before considering the Stipulation, the Idaho Public Utilities Commission (IPUC) should hold public hearings so that diverse stakeholders may explain decoupling to customers and allow customers to comment on the proposal.

While the Stipulation declares that it is in the public interest and that all of its terms and conditions are fair, just, and reasonable, all evidence is to the contrary. Customers will see an increase in their rates and customer charges without any evidence whatsoever that Idaho Power requires these increased revenues.

When the IPUC determines the revenue requirement and the rate of return for a utility in a rate case proceeding, all revenues and expenses are on the table. If costs exceed income and the Company is not earning a reasonable rate of return, the IPUC is likely to grant a rate increase. In 2005, the IPUC set a revenue requirement for Idaho Power and a rate of return of 8.1%.

The Stipulation, contrary to this long-standing approach to ratemaking, allows Idaho Power to receive revenue in excess of the revenue requirement set in 2005. It would receive these monies through a decoupling mechanism, which allows future rate surcharges even though the Company cannot currently prove any need.

What makes this scheme patently unfair, unjust and unreasonable is that it ignores the economic conditions of the utility at the time the surcharge is incurred or imposed. For instance, Idaho Power's income could go up for other reasons or its costs could go down. Decoupling imposes surcharges regardless, and therefore ignores any other income or cost savings by the utility. Finally, because it is likely that Idaho Power's financial picture has and will continue to change since 2005, to its benefit, it may receive additional monies through surcharges that would result in earnings above its authorized rate of return of 8.1%. A utility earning above its rate of return would be unlawful absent the FCA.

In addition to rate increases, recent Idaho Power rate cases have attempted to shift recovery for fixed costs from volumetric energy charges to monthly minimum basic charges. To its credit,

the Commission has repeatedly rejected these attempts because of the impact high monthly charges have on customers and the perverse incentive such charges have on energy conservation. This FCA is a method of accomplishing that revenue recovery shift from volumetric energy charges to fixed monthly charges without the public process that a rate case affords and contrary to the Commission's express policy statements.

Decoupling is clothed in the banner of conservation. At first blush, this seems a compelling argument. The goal of energy efficiency is a worthy one, supported and advanced by many, including ICAN. It seems self-evident that Idaho Power currently has no incentive to promote conservation because it results in lower sales and coverage of fixed costs. And if decoupling is instituted, Idaho Power will allegedly promote conservation efforts because those efforts will be recovered through the FCA rather than through volumetric energy charges. The identified problem and the proposed solution seem logical. While attractive on the surface, these assertions should be examined carefully before decoupling is adopted.

In its evaluation of the Stipulation in this case, the Commission should seek answers to at least the following serious questions: (1) What is the actual amount of revenue lost due to Idaho Power's own energy efficiency efforts and the significance of the financial impact on the company?; (2) What proportion of declining customer use is attributable to company conservation efforts, as compared to other causes not related to company actions (e.g. better housing codes, appliance standards, price elasticity)?; (3) What is Idaho Power's track record on energy efficiency?; (4) Are there reasons why Idaho Power has pursued energy efficiency without a decoupling mechanism and can it be expected to do so in the future?; (5) What specific additional energy efficiency programs will Idaho Power customers see if decoupling is adopted (separate from the program proposed in IPC-E-06-32)? (6) Are customers compensated for their increased risk and the reduction of risk to shareholders (i.e., is the shift reflected in a downward adjustment to the Company's Return on Equity)?; and (7) Are there alternatives to decoupling?

By way of some answers to these questions, the most striking problem with the Stipulation's analysis of Idaho Power's potential loss of income due to declining use is that it completely ignores the economic reality of the electric power market. The wholesale price of electricity in the Northwest is significantly higher than Idaho Power's current retail rates. Idaho Power's residential retail rates vary, depending on season and usage, between $.054251 and $.061060. Meanwhile wholesale prices on the spot market are currently higher and are predicted to remain higher than average retail rates in the future.[1] If customers use less energy, that extra energy can be sold by Idaho Power on the spot market for more of a profit than it would receive selling it to residential customers. Shareholders would then benefit from the added wholesale sales, and from the FCA, resulting in double recovery. That is why the Company does not lack an incentive to pursue conservation. Pursuing conservation allows every saved kWh to be sold at a higher cost to someone else. Decoupling is even more likely to result in a revenue windfall

[1] Rebuttal Testimony of Jim Lazar (Jl-1t) On Behalf of Public Counsel Before the Washington Utilities & Transportation Commission, WUTC V. Pacificorp D/B/A Pacific Power & Light Company, Docket Nos. UE-050684 and UE-050412.

because the Company is recovering revenue for lost sales through the surcharge while making even more money selling power on the wholesale market.

In the area of natural gas decoupling, which does not have the same kind of resale market as electric, the Washington Utilities and Transportation Commission (UTC) recently acknowledged that decoupling can lead to windfall profits for utility companies if allowed to collect revenues for non-utility sponsored conservation.[2] Steve Weiss, who submitted testimony on behalf of the Northwest Energy Coalition in that case, acknowledged in testimony that decoupling could lead to windfall profits for a company, including through decreases in demand, like individual sponsored conservation, that are unrelated to the company's conservation efforts.

The FCA fails to take into account a downward trend in usage (sometimes called "attrition") by both existing and new customers. For example, housing built today has higher efficiency standards than older housing, and new appliances are more efficient than old appliances. Even houses that do not meet the standards that Idaho Power will be promoting in the DSM incentive mechanism pilot project are more efficient than housing built in the past.

The FCA also disregards the effect of increases in the cost of power to consumers. Some consumers will be forced to reduce their use of electricity. ICAN leaders have testified in the past to the Commission about the hard choices they are forced to make when they are faced with higher utility bills. People reduce their usage by choosing not to heat their homes in the winter, endangering their health and standard of living. Pricing consumers out of the electricity market can have environmental impacts as well. Last winter, a survey ICAN conducted of low-income Idahoans around the state found that 63 percent of respondents were using fuels other than electricity or gas, including wood, pellets, fuel oil, and propane, to heat their homes. Idaho Power should not receive a bonus payment for driving people out of the electricity market.

Moreover, the calculation Idaho Power will be using to determine the FCA is inherently inaccurate, and will become more inaccurate every year. Idaho Power will use data from the 2005 general rate case to determine the aggregated costs per customer for residential customers and compare these with the aggregated revenue for 2005 per customer. As the gap between the cost and the revenue grows, as it will, the surcharge is calculated on the difference and then collected by the Company.

Since both the customer usage and revenue figures are based on the number of customers and the revenue existing in 2005, the gap between the two could be significantly larger than reality and result in much larger surcharges.[3] Using the revenue calculation from 2005 is especially biased since Idaho Power's service territory covers a region that is rapidly growing. Growth means more sales and more sales means more revenues. In other words, a "real time" comparison of customer usage declines and income would likely result in no surcharges.

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[2] Washington Utilities and Transportation Commission, Docket UG-060256, Order 05, Final Order Accepting Settlement, Subject To Conditions; Rejecting Tariff Sheets; Authorizing And Requiring Compliance Filing, section 79.

[3] Direct Testimony of David Youngblood, Case No. IPC-E-04-15.

Nor has Idaho Power made a real commitment, with measurable goals and accountability, to engage in conservation programs that will decrease usage independently of conservation efforts by government regulations and programs and individual efforts. It is not at all clear what revenue losses Idaho Power can attribute to its own conservation efforts. Idaho Power currently has conservation programs and one of these has been determined to be at least sufficient to form the basis of the Stipulation in IPC-E-06-32. Yet the lost usage from these programs should be credibly established before decoupling is considered.

The Stipulation also fails to account for the shift in risk associated with the Company's return on equity ("ROE"). The utility's cost of equity capital will decrease if decoupling is adopted.[4] This decreasing cost of equity will benefit the shareholders, not the customers, unless the Commission reduces the return on equity it allows Idaho Power. Since the 2005 rate case was settled by Stipulation without an ROE, it is difficult to establish an adjustment, especially in the absence of a rate case. However, it is possible to reduce the rate of return to reflect what would otherwise be a change to the ROE. ICAN believes that the reduction in ROE should be at least 50 basis points.

Finally, decoupling does not promise conservation. And the Stipulation, while talking about conservation, actually offers no real programs with benchmarks and targets to achieve it.

Before considering the Stipulation, the Idaho Public Utilities Commission should hold public hearings so that diverse stakeholders may explain decoupling to customers and allow customers to comment on the proposal. Ultimately, the Commission should reject the FCA pilot project because is contrary to the public interest.

Should the Commission approves the pilot project, it should take steps to limit the potential liability of consumers, and to ensure that the project accomplishes what it is intended to accomplish.

1. Mandatory Cap on Fixed Cost-Adjustment

In its application, Idaho Power proposed a discretionary three percent revenue cap on the FCA. The Stipulation did not include any mention of the cap. As recognized by the Washington Utilities and Transportation Commission, this is this is the only way to curb the possibility of overearning. If the pilot project is designed to test the mechanism, in the absence of any proof that there is a problem to be solved, the Commission should limit the potential risk shift to consumers by instituting a mandatory three percent cap. Idaho Power has acknowledged in its application, and in the supplementary direct testimony of John R. Gale, and in the direct testimony of Michael Youngblood, that capping the FCA at three percent is reasonable, citing the precedent of the PCA cap provision. If Idaho Power believes that a three percent FCA is insufficient, a general rate case would be the appropriate remedy to prevent overearning.

[4] Testimony of David Parcell, Washington UTC staff, Docket NO. UG-060256.

2. Establish Clear Conservation Plan with Real Accountability

The Stipulation does not outline clear conservation goals or accountability measures. The commitment it describes is extraordinarily vague – it will "support" and "promote" changes in housing codes, but has no authority to ensure that those changes occur. There are no set conservation targets or benchmarks. The Commission should require Idaho Power to commission a third party to perform a Conservation Study; develop a Conservation Plan with targets and benchmarks; create an advisory group to review the Conservation Study and Plan; issue requests for proposals to implement the Plan; and demonstrate to the Commission, within a year of approval of the pilot program, that it will meet the Plan's targets. The Plan should include increased levels of Low-Income Weatherization Assistance to mitigate the impact of the FCA on low-income customers. If Idaho Power fails to meet these deadlines, the Commission should terminate the pilot program.

3. Create a Separate Line Item for the FCA on Billing Statements to Increase Transparency and Public Education about the Program

The Stipulation states that the FCA would be combined with the Conservation Program Funding Charge on customer bills. There is no justification for doing so. Idaho Power consumers have a right to know how this program impacts their monthly bills. At the end of the three year pilot program, the Commission will review the program before deciding whether to continue it, and consumers must have a role in that review process. One way to inform consumers about the pilot is to clearly label the charge on their monthly bills. Consumers are more likely to read their bills than any other communication from the Company. If this program is really in the public benefit, and fair, just and reasonable, Idaho Power should not have any reason to fear adding a clearly labeled line item on customers' billing statements.

4. Extension of the Pilot Programs

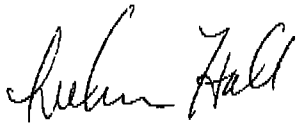
The Washington UTC recently ordered that a decoupling mechanism in a natural gas case "may only be extended as part of a general rate case, and only after a thorough evaluation of the mechanism performed by an independent consultant." The Commission should make extension of the Pilot Programs conditional on a general rate case to allow the revenue distortions caused by the FCA to be evaluated and eliminated. A third party evaluation should also be required.

5. Return on Equity

The Stipulation does not state that the Commission will adjust Idaho Power's return on equity. Since the 2005 rate case settled by Stipulation without a ROE, it is difficult to establish an adjustment, especially in the absence of rate case. However, it is possible to reduce the rate of return to reflect what would otherwise be a change to the ROE. The Commission should reduce Idaho Power's ROE at least 50 basis points. Otherwise, shareholders are doubly benefiting from stable revenue and a lower cost of capital at the expense of the customers.

6. The Use of 2005 Numbers for Setting Recovery Benchmarks.

The real solution is to evaluate the utility on its overall revenue instead of simply per customer usage. However, absent that, in order to avoid the growing gap caused by using Idaho Power's 2005 general rate case established aggregated residential customer revenue and subtracting the 2005 general rate case aggregated residential customer usage, revenue should be based on actual income for residential customers and then offset by the 2005 per customer usage.



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