DECISION MEMORANDUM

TO: COMMISSIONER KEMPTON
COMMISSIONER SMITH
COMMISSIONER REDFORD
COMMISSION SECRETARY
COMMISSION STAFF

FROM: DON HOWELL
DEPUTY ATTORNEY GENERAL

DATE: OCTOBER 21, 2009

SUBJECT: IDAHO POWER COMPANY'S APPLICATION FOR AN ACCOUNTING ORDER TO RECORD A POSSIBLE REVENUE DEFICIENCY FROM ITS TRANSMISSION OPERATIONS, CASE NO. IPC-E-09-21

On July 20, 2009, Idaho Power Company filed an Application requesting that the Commission issue an accounting order authorizing the deferral of costs associated with the Company's transmission services. The Company is requesting authority to record and possibly recover in Idaho rates its unrecovered transmission costs that were denied in a recent transmission rate case before the Federal Energy Regulatory Commission (FERC), Docket No. ER06-787. The Company requested and Staff concurred that the Application for an accounting order be processed under Modified Procedure.

On September 1, 2009, the Commission issued a Notice of Modified Procedure requesting that interested persons file comments regarding the Application no later than September 29, 2009. The only comments received were submitted by Commission Staff. The Company did not file reply comments.

BACKGROUND

In March 2006, Idaho Power filed an Application with FERC requesting an increase in its transmission rates subject to FERC's jurisdiction. In its filing, the Company proposed to revise its Open Access Transmission Tariffs (OATT) from "stated" rates to "formula" based rates. Formula rates would be updated annually based upon Idaho Power's total cost to own, operate and maintain its transmission facilities for its transmission customers. *Order on Initial*

Decision, 126 FERC ¶ 61,044 (Jan. 15, 2009). The "formula" rate methodology would be calculated using data reported annually in the Company's FERC Form 1.

In its FERC Application, Idaho Power noted that it had not adjusted transmission rates since 1996. Nevertheless, several of the Company's transmission customers opposed the FERC rate application. Although the parties settled most of the issues, they were unable to resolve the proper ratemaking treatment of the "Legacy Agreements." *Id.* at ¶ 11.

Starting in the 1960s, Idaho Power entered into three long-term transmission service contracts (commonly referred to as the "Legacy Agreements") with PacifiCorp to provide transmission service from the Jim Bridger power plant in western Wyoming. Idaho Power and PacifiCorp jointly own the Bridger facility. Both companies built and now operate transmission power lines from Jim Bridger to their respective service territories. Under the terms of the Legacy Agreements, Idaho Power charges PacifiCorp "use of facility fees" to use Idaho Power's transmission facilities until 2025. *Id.* at ¶¶ 3-9.

The federal administrative law judge (ALJ) initially determined and FERC subsequently affirmed that Idaho Power's charges to PacifiCorp under the Legacy Agreement are significantly lower than the OATT rates Idaho Power proposed to charge other customers for similar transmission services. This rate "disparity" between the old Legacy Agreements and the OATT rates has grown over time. *Id.* at ¶ 127. The ALJ further found that under the Legacy Agreements, PacifiCorp's load accounted for 40% of the transmission lines' capacity, Idaho Power's load accounted for 45% of the capacity, and third-party transmission customers accounted for only 15% of the total firm capacity of the subject Idaho Power facilities. *Id.* at ¶ 128. Based upon the principles of cost causation and allocation, the Judge found that it was unreasonable for Idaho Power to over-allocate its cost recovery to its third-party transmission customers. Because of the longstanding Legacy Agreements, Idaho Power is contractually bound to provide transmission service to PacifiCorp at rates that are now considered below cost.

In affirming the ALJ, FERC found that Idaho Power cannot require its third-party OATT transmission customers to pay more than their prorate load share of Idaho Power's total transmission revenue requirement. *Id.* at ¶ 133. Because its revenue recovery is "locked in" by the long-term Legacy Agreements, FERC found that Idaho Power must bear the under-recovery of transmission costs on its own. *Id.* at ¶ 129.

The intervenors in the FERC docket also argued that Idaho Power has other options to make up for the revenue shortfall. The Company could avail itself of provisions in the Legacy Agreements that allow some transmission charges to be adjusted. *Id.* at ¶ 163. In addition, the ALJ observed that Idaho Power could seek to recover its revenue shortfall from its retail customers. *Id.* at ¶ 158. He concluded that Idaho Power "has other ways to lessen any financial blow . . . through appropriate rate changes at the retail level or through re-negotiations of its legacy agreements with PacifiCorp." *Id.* at ¶ 218.

THE APPLICATION

In response to FERC's Initial Decision, Idaho Power has taken three actions. First, on February 27, 2009, Idaho Power filed a Petition for Rehearing with FERC. On March 18, 2009, FERC granted rehearing so it could consider that matter in greater detail. Docket No. ER06-787-006. Second, Idaho Power has initiated actions to amend portions of the Legacy Agreements which are subject to change or re-negotiation. See FERC Docket No. ER09-1335-000. Third, Idaho Power has filed the present Application with this Commission for an accounting order to defer and account for unrecovered transmission costs associated with the above FERC Order. The Company estimates its unrecovered costs are $8,084,251 for the period March 2008 through May 31, 2010. Application at ¶ 9. If Idaho Power is able to reduce its revenue shortfall through the first two alternatives, then the Company "will reduce the deferral" request that is the subject of this Application. *Id.*

The Company seeks an accounting order authorizing the deferral of the unrecovered transmission-related costs associated with the outcome of FERC's Initial Decision. The Company proposes to amortize the unrecovered transmission revenues on a straight-line basis over a 36-month period beginning June 1, 2010, once these costs are included in rates. *Id.* at ¶ 10. Idaho Power proposes to account for the unrecovered transmission revenues by charging them to Account 182.3 (Other Regulatory Assets) and amortizing these amounts to Account 407.3 (Regulatory Debits) upon their inclusion in rates. Until such time as the Company begins to recover its deferred costs, it requests that the Commission authorize a carrying charge on the deferral balance based upon its latest authorized rate of return on rate base (i.e., 8.18% per Order No. 30722). *Id.* at ¶ 11.

STAFF COMMENTS

In its review of the Application, Staff's primary objective is to evaluate the appropriateness of the requested accounting order for deferral of unrecovered transmission-related costs. Staff does not object to the request for an accounting order. However, Staff believes the determination of revenue recovery from native load customers is appropriately determined in a future proceeding after the reconsideration issues at FERC have been finally decided, and after Idaho Power's efforts to re-negotiate provisions of its Legacy Agreements.

In Staff's view, the unrecovered transmission-related revenues are generally costs previously associated with and recovered from third-party transmission users until the recent FERC case described above. The revenues from these transmission users covered a portion of actual transmission costs and reduced the overall revenue requirement to Idaho customers through a revenue credit in each rate case. The FERC decision has the effect of reducing the revenue credit, thereby creating the unrecovered amount. With the FERC reconsideration and Legacy Agreement actions incomplete, Staff believes deferral accounting for these unrecovered transmission revenues is appropriate through May 2010 as requested by Idaho Power. The question whether the deferred amount should be recovered from Idaho ratepayers, is a matter that should be reserved for a future proceeding.

The estimated unrecovered transmission-related revenues through May 31, 2010 to be deferred were estimated by Idaho Power to be $8,084,251. As the contested issues are decided or resolved, the deferral will be reduced. Since this Application was filed, FERC increased the OATT revenues Idaho Power is authorized to collect and Idaho Power filed its annual OATT update to change rates effective October 1, 2009. These last actions reduce the estimated deferral by approximately $3.4 million. Consequently, the current unrecovered estimate to be deferred is approximately $4.675 million.

1. Deferral Period. Idaho Power is requesting to amortize the deferral over a three-year period beginning June 1, 2010, upon the inclusion in retail rates. Staff believes a three-year amortization period is reasonable. However, Staff does not believe the amortization should be timed to coincide with recovery of the amortization in retail rates. Rate case filings are made based on various considerations of the Company with amortizations being just one of many factors. With a deferral period through May 31, 2010, Staff recommends the amortization begin January 1, 2011, even if the Idaho ratemaking treatment is not fully decided. This provides time

for Idaho Power to resolve the FERC-contested issues and the Legacy Agreement actions along with its rate case reviews.

2. Deferral Accounts. Idaho Power proposes to account for the unrecovered transmission revenues by charging them to Account 182.3 (Other Regulatory Assets) and amortizing these amounts to Account 407.3 (Regulatory Debits). These accounts are appropriate and Staff recommends that the proposed accounting treatment be approved.

3. Carrying Charge. Idaho Power also proposes to accrue a carrying charge on the deferral at the most recent return on rate base (currently 8.18%). Staff believes deferral in itself provides adequate benefit to the Company without it earning a return on the deferral. Absent an accounting order authorizing deferral, Idaho Power would not recover any of the transmission-related revenues or receive a return on them. Staff recommends no carrying charge on the deferral be authorized.

The deferral as requested in the Application acknowledges the extraordinary nature of these unrecovered transmission-related revenues. Deferred accounting treatment for regulatory purposes is an appropriate, just and reasonable means of providing the Company the opportunity to request and litigate future recovery of unrecovered revenues caused by the FERC decision. Commission approval of this Application does not relieve Idaho Power of its obligation to demonstrate the prudence of its actions, or lack of actions with respect to the FERC cases and contracts. A deferral order in this case does not limit the right of Staff, other parties and the Commission to examine the lawfulness, reasonableness and prudence of the actual deferral amount for recovery in retail rates. This type of review is critical to protect customers before including unrecovered third-party transmission revenues once the contested issues before FERC are decided.

In summary, Staff recommends the following:

1. An accounting order authorizing deferral of the unrecovered transmission-related revenues through May 31, 2010 should be approved.

2. The proposed accounts should be utilized with the unrecovered transmission-related revenues charged to Account 182.3 (Other Regulatory Assets) and the amortization charged to Account 407.3 (Regulatory Debits).

3. An amortization period of three years should be approved.

4. The amortization period should begin on January 1, 2011.

5. No carrying charge should be authorized.

6. The ratemaking treatment and possible recovery should be addressed in a future proceeding.

COMMISSION DECISION

1. Should Idaho Power's Application for an accounting order to defer unrecovered transmission revenues/costs be granted?

2. If so, does the Commission wish to condition the accounting order as recommended by Staff?

Don Howell
Deputy Attorney General

bls/M:IPC-E-09-21_dh2