Office of the Secretary
Service Date
February 17, 2010

BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF THE APPLICATION OF IDAHO POWER COMPANY FOR AUTHORITY TO IMPLEMENT A TRACKING MECHANISM TO RECOVER ITS DEFINED BENEFIT PENSION EXPENSE	**CASE NO. IPC-E-09-29** **ORDER NO. 31003**

On October 20, 2009, Idaho Power Company (Idaho Power; Company) filed an Application with the Idaho Public Utilities Commission (Commission) requesting approval on or before February 12, 2010 of a mechanism to track and recover annually the Company's defined benefit pension expenses. The Application does not seek current approval of future expenses associated with the Company's qualified defined benefit pension plan, nor is it requesting that current rates be changed at this time. The Commission in this Order denies the Company's request for an annual tracking mechanism and provides clarification of pension expense recovery.

BACKGROUND

Idaho Power's defined benefit pension plan was established in 1943 and continues as part of the Company's total compensation package for eligible employees. As of January 1, 2009, Idaho Power had 2,085 active employees in the plan and a total of 3,533 plan participants.

In 1986, the Company adopted Statement of Financial Accounting Standard (SFAS) 87. The Standard addresses pension funding issues from an accrual perspective in an attempt to better match the compensation cost of an employee's pension benefits with the time period over which the employee earns those benefits and to provide for greater comparability between companies from year to year. Prior to the adoption of SFAS 87, pension expense was based on the amount a company chose to contribute to its plans during the year. After the adoption of SFAS No. 87 in 1986, the Company filed general rate cases in 1994 and 2003 that dealt with pension funding issues. With the Company's 1994 general rate case filing, the Company included pension costs based upon the SFAS 87 accrual perspective in test year O&M expenses rather than cash contributed to the plan. The amount approved was approximately $2 million per year.

In its 2003 general rate case, Case No. IPC-E-03-13, Idaho Power again included in its test year defined benefit pension plan expense derived from the accrual methodology provided for in SFAS 87. The Commission Staff recommended that the Commission reject the accrued SFAS 87 amount to be included in the Company's revenue requirement because the Company did not have any actual cash contribution requirements during the test year and would not be required to fund contributions for the foreseeable future. The Company in rebuttal testimony retracted its proposal.

In 2007, Idaho Power filed an application with the Commission (Case No. IPC-E-07-07) seeking clarification that the Company could expect to recover pension costs based on cash contributed to the plan and could account for defined benefit pension expenses on a cash basis rather than the accrual basis that the Company used from 1994 until 2003. In conjunction with the Company's request for clarification of its authority to utilize cash basis accounting for recovery of defined benefit pension expense, the Company also requested authority to defer future cash contributions it would make to its defined benefit pension plan and to record these future defined benefit pension plan cash contributions as regulatory assets.

On June 1, 2007, the Commission issued Order No. 30333 authorizing the Company to account for its defined benefit pension expense on a cash basis, and to defer and account for accrued SFAS 87 pension expense as a regulatory asset. As part of its Order, the Commission acknowledged that it is appropriate for the Company to seek recovery in the Company's revenue requirement of reasonable and prudently incurred defined benefit pension expense based on actual cash contributions. The Commission also stated "when the Company's actuaries notify the Company of Employee Retirement Income Security Act of 1974 (ERISA) minimum funding requirements, the Company can evaluate the circumstances for ratemaking purposes and make a filing requesting ratemaking treatment, if needed."

Idaho Power's actuary has informed the Company that a contribution is required for the tax year beginning January 1, 2009. The required contribution will be $5,418,662 if paid by October 15, 2009, but if not paid by October 15, 2009, interest will accrue until the extended due date for Idaho Power's federal income tax return of September 15, 2010. The Company did not make an October 15, 2009, payment.

TRACKING MECHANISM

Idaho Power contends the requirement to make cash payments is expected to continue over the next several years, but the amounts may vary dramatically from year to year. Therefore, the Company requests authorization to implement a defined benefit pension expense tracking mechanism that has similar components to those of the Power Cost Adjustment (PCA) mechanism. That is, the proposed mechanism will include a forecast component and true-up component.

As reflected in its Application, the Company will recover its forecasted annual cash payments toward defined benefit pension expense through rates based upon an actuarial determination of those anticipated required contributions. Each year, the Company will compare the revenue collected through the tracking mechanism's forecast component rate to the actual cash contributions to defined benefit pension expense during the year. Any difference will be refunded or collected from customers over the subsequent 12-month period in the true-up component. The Company recommends that a carrying charge equal to the Commission-approved interest rate for deposits be applied each month based on the balance in the regulatory asset account.

The Company proposes a March 1 through February 28 (February 29 in leap years) annual test period with rate adjustments becoming effective each June 1. The Company proposes to make an annual filing under the tracking mechanism on or before April 7 of each year with the associated rate adjustment effective June 1.

Idaho Power requests that it be allowed to recover its defined benefit pension expense as a percentage rate applied to all base revenue in a manner similar to the Energy Efficiency Rider, Schedule 91. Attachment 1 to the Application contains the Company's proposed Schedule 53 detailing the purpose and applicability of the proposed tracking mechanism.

ACCOUNTING TREATMENT

The Commission may require costs that are normally expensed to be deferred under SFAS 71, Accounting for the Effects of Certain Types of Regulation. SFAS 87 pension expenses were authorized for deferral under Commission Order No. 30333, Case No. IPC-E-07-07. In order to qualify for deferral, SFAS 71 requires that a utility be able to demonstrate that "future revenues will be provided to permit recovery of the previously incurred cost." In order to meet the conditions for deferring pension costs under SFAS 71, some mechanism must be in place that assesses whether the actual costs during the recovery period exceeded the amount in rates, tracks any shortfall or excess, and adjusts rates accordingly.

Idaho Power believes that the proposed tracking mechanism will meet those requirements. Absent such a tracking mechanism, inclusion of pension contributions as test year expense in a general rate case will most likely cause pension expense to become ineligible for deferral under SFAS 71. Derecognition of its deferred pension expense regulatory asset would result in serious negative consequences to Idaho Power. At a minimum, the Company contends it would be forced to write off the $33 million balance of deferred pension expense (as of September 30, 2009). Idaho Power's equity would also likely decrease by $92 million in addition to the retained earnings impact of derecognizing the regulatory asset for deferred pension expense. Both of these accounting changes could have negative impacts on customers.

On November 17, 2009, the Commission issued Notices of Application, Intervention Deadline, and Modified Procedure in Case No. IPC-E-09-29. The deadline for filing Petitions to Intervene was November 27, 2009. There were no petitions filed. The deadline for filing written comments was January 14, 2010. Commission Staff was the only party to file comments. Staff recommends that the Commission deny the Company's request for the proposed pension tracking mechanism. Following Staff comments, the Company requested a meeting with Staff to clarify Staff's position. On January 29, 2010, the Company filed reply comments setting forth specific language that the Company and Staff believes will satisfy SFAS 71 requirements if the proposed tracking mechanism is denied.

STAFF COMMENTS

On January 14, 2010, Staff filed comments. Staff's comments are intended to provide the Commission with additional background regarding the Company's treatment of pension expense, the purpose and effects of the Company's Application, as well as additional concerns regarding the Company's Application. Staff recommends that the Commission deny the Company's request for the proposed pension expense tracker. Recovery of pension expense, Staff contends, continues to be appropriately dealt with in rate cases. Staff supports a reasonable amortization of actual deferred cash contributions. This recovery method, Staff states, will meet the requirement of SFAS 71 to recover the deferral balance in future rates. The amortization can change as needed to recover the remaining deferral balance of actual cash contributions.

Staff generally prefers traditional regulation to cost trackers, limiting the use of cost trackers to extraordinary circumstances where it can be proven that a tracking mechanism is in the public interest. However, recognizing that situations do exist whereby a cost tracker may be necessary, Staff applies three distinct criteria to review a tracking mechanism:

1. The expense is largely outside the control of the utility;
2. The expense is unpredictable and volatile, and;
3. The expense is substantial and recurring.

The choice to sponsor and adopt a defined benefit pension plan over other available retirement plan alternatives is a choice that is made solely by management of a utility. The benefit formulas that calculate the projected benefits an employee will receive upon retirement, the actuarial assumptions regarding expected return on plan assets, turnover rates, and future pay increases, are all established with management input and have a significant effect on the amount of contributions that are required each year.

Furthermore, a defined benefit pension plan already places economic risk on utility customers. The primary element of a defined benefit plan is that the benefit at retirement is defined, thereby placing all the investment risk upon the employer. When the employer is a regulated utility that recovers the retirement expense through rates, then that risk is shifted to the customers. If a cost tracking mechanism is established that guarantees that a utility will be able to recover 100% of all contributions to a defined benefit pension plan, then all the economic, financial, and investment risk is borne by the customers of that utility. With the shift in risk from the utility to the customers, a corresponding decrease in return on equity would need to be evaluated.

The third criteria used by Staff to determine if a cost tracker is in the public interest is whether or not the expense is substantial and recurring. Although pension expense can be substantial and recurring, the differences between the test-year cost and the actual cost must have a material effect on the utility's rate of return. With the approved deferral accounting treatment, the difference will be minimal. Under traditional ratemaking, known and measurable adjustments to test year expenses are recognized to account for expenses that will occur beyond the test year. Any underrecovery or overrecovery of pension costs will not likely have a material impact on the utility's rate of return. For these reasons, Staff does not believe that the criteria cited as necessary to establish a tracking mechanism for pension expense have been met.

In supporting its argument for the implementation of a pension expense tracking mechanism, the Company contends that SFAS 71 requires a tracking mechanism because of the previously deferred SFAS 87 pension expense arising from Commission Order No. 30333 in Case No. IPC-E-07-07. In that Case, Idaho Power requested authorization to account for pension expense on a cash basis, i.e., remove SFAS 87 pension expense from its financial statements and to record it as a regulatory asset. Furthermore, Idaho Power requested authority to defer any future cash contribution to the pension plan.

In that case, Staff was concerned with the requirements of SFAS 71, the accounting standard that would allow the Commission to approve any deviations from generally accepted accounting principles (GAAP). SFAS 71 provides that before costs which would otherwise be expensed can be capitalized or deferred, it must be probable that the regulating entity will allow recovery of prudently incurred amounts in future rates. The concerns with the requirements of SFAS 71 in that case were discussed with the Company before proposing a solution that both the Company and Staff agreed would satisfy the requirements of SFAS 71. Staff stated in its filed written comments in that case:

> Over the life of a pension plan, the amount of SFAS 87 pension expense and the amount of cash contributions are theoretically equivalent and without interference, the SFAS 87 expense and the cash contributions over time will be comparable. Therefore, to address Staff's concerns about SFAS 71, Staff believes it would be [permissible] to allow the deferral of SFAS 87 pension expense as a regulatory asset if the cash contributions when made are credited as an offsetting entry to that regulatory asset. Given the presumption that the two expenses will ultimately be equivalent and the regulatory asset account will zero out on its own, then the SFAS 71 requirements will be satisfied.

The Company's reply comments in that case also confirm that the requirements of SFAS 71 will have been met "if the Commission concurs that it is reasonable to assume that the Company's actual cash contributions to its defined benefit pension plan are reasonable expenses for ratemaking purposes, then the Company and its outside auditors can reasonably conclude that it is probable that the Commission will allow recovery of prudently incurred cash contributions in future rates."

During the course of the IPC-E-07-07 proceedings, Staff had frequent communications with Idaho Power regarding SFAS 71 and future recovery of pension contribution in rates whenever the time came that the Company was again required to fund the pension plan. At that time, Staff informed the Company that it was not supportive of a tracking mechanism.

In the current filing, Idaho Power contends that, without a tracking mechanism, the Company will not likely be able to apply the SFAS 71 methodology to the deferral of SFAS 87 pension expense. This will require it to derecognize approximately $33 million, the balance of the regulatory asset account created by the deferral of SFAS 87 pension expense as of September 30, 2009. The Company also contends that it will be required to derecognize an additional $92 million in equity related to the accumulated other comprehensive income (AOCI) in the equity section of the balance sheet for SFAS 158. SFAS 158 requires the Company to record a liability for its unfunded projected benefit obligation, which is defined as the difference between the market value of the plan's assets and the actuarially determined projected benefit obligation. The accounting entries to record the unfunded projected benefit obligation also include a corresponding decrease, net of deferred taxes, in the AOCI on the balance sheet.

SFAS 71 states that before a utility can capitalize or defer a cost that would have otherwise been expensed, two conditions must be met. The first condition is that it must be "probable that future revenue in an amount at least equal to the capitalized cost will result from the inclusion of that cost in allowable costs for rate-making purposes." The footnotes of the statement define the term "probable" with its "usual general meaning, rather than in a specific technical sense, and refers to that which can be reasonably expected or believed on the basis of available evidence or logic but is neither certain nor proved." The second criterion of SFAS 71 states that "Based on available evidence, the future revenue will be provided to permit recovery of the previously incurred cost rather than to provide for expected levels of similar future costs."

Staff's assertion in Case No. IPC-E-07-07 still holds true today. Because the agreed-upon accounting entries in that case use the cash contribution as an offset to the regulatory asset created by deferral of SFAS 87 pension expense and because, over time, the cash contributions and the accrued pension expense under SFAS 87 will be similar, the regulatory asset will trend toward zero. SFAS 71 requires only that it will be probable that future revenues will be allowed to recover the capitalized cost; a specific recovery mechanism is not dictated. With amortization of the deferred cash contributions and because the capitalized cost will tend to zero-out over time, it is more than probable that future revenues will be allowed to recover those costs.

Staff applies the same logic to the second criterion of SFAS 71 because future revenue will be provided to permit the recovery of the previously incurred cost. Staff continues to believe that the deferral of cash contributions and the amortization of those costs in rates through the normal ratemaking process is an appropriate recovery mechanism. It meets the requirements of SFAS 71 and allows the Company to recover reasonably incurred pension costs. An additional tracking mechanism is not necessary. Staff believes a mechanism with forecast and true-up provisions is inappropriate for these expenditures. The three criteria for a tracking mechanism discussed above have not been met. Staff supports a reasonable amortization period of actual deferred balances. As stated by the Company in its IPC-E-07-07 reply comments, page 9 ". . . a carrying charge rate and amortization period for the deferred expense associated with the cash contributions would be determined in a future proceeding." To restate, Staff does not believe the cost tracker meets this intent, nor is the proposed cost tracker necessary or appropriate.

Staff Recommendation

After reviewing the Company's Application and all other available information, Staff recommends that the Commission deny the Company's request for the proposed pension tracking mechanism. In doing so, Staff recommends that the Commission reaffirm its commitment in Order No. 30333 that reasonable and prudently incurred cash contributions based on the ERISA minimum funding requirements may be properly included in the Company's revenue requirement. Staff also recommends that in a future rate case the Company be allowed to recover a reasonable amortization of the deferred balance associated with the cash contributions of its defined benefit pension plan after the costs are actually incurred and deferred.

IDAHO POWER REPLY

On January 29, 2010, Idaho Power Company filed reply comments. The Company relates that on January 21, 2010, Company representatives met with Staff to seek clarification on a number of issues raised by Staff in its comments. Specifically, the Company sought to confirm its understanding of Staff's recommendations with regard to the Company's future recovery of pension expenses and to explore how Staff's recommendation would be implemented.

As a result of the January 21, 2010 discussion the Company represents that Staff would support the following treatment of deferred pension expense:

1. The Company will establish a balancing account that would track, on a cumulative basis, the difference between cash amounts contributed to the pension plan and amounts included in rates.

2. An appropriate amortization period for deferred cash contributions will be evaluated during a revenue requirement proceeding and will begin simultaneously with the approved period for recovery.

3. There may be circumstances where the Company could choose to contribute in excess of the minimum amount required by ERISA or prior to the final due date of the minimum payment; such contributions, while potentially subject to longer amortization, will not be disallowed solely because they are made sooner than legally required.

4. The Company will not be expected to expense its prudently incurred cash contributions prior to the Commission's review during a revenue requirement proceeding and inclusion in rates.

5. As part of a revenue requirement proceeding, the Company may request the inclusion of imminent, but as yet unpaid, contributions that have been finally determined by the Company's actuary as "known-and-measurable" expenses to be incurred.

6. The Company should earn a carrying charge on the unamortized balance of deferred cash contributions at the Commission-approved interest rate for deposit.

The Company has evaluated Staff's recommendation as stated in its comments and as clarified at the meeting on January 21, 2010, and is satisfied that the recommendation meets both of the requirements for continued deferral under SFAS 71. SFAS 71 provides that a previously incurred cost may be deferred if: (1) it is "probable that future revenue in an amount at least equal to the capitalized cost will result from inclusion of that cost in allowable costs for ratemaking purposes" and (2) "future revenues will be provided to permit recovery of the previously incurred cost rather than to provide for expected levels of similar future costs. . . ." The use of a balancing account that tracks the difference between cumulative cash contributions and amounts collected in rates, the Company contends, will provide adequate evidence to conclude that it expects future revenue equal to the amount capitalized. Recovery that is derived from amortization of the deferred cash contributions provides recovery of previously incurred costs and satisfies the second requirement.

While the Company continues to believe that its proposed tracking mechanism better matches recovery of pension costs with the Company's cash outlays to fund the pension, the Company is not opposed to the recommendations included in Staff's comments as clarified in the Company's reply. Further, the Company is satisfied that Staff's proposed methodology would meet the deferral requirements of SFAS 71. Should the Commission choose to adopt Staff's recommendations, the Company requests that the Commission provide the following clarifications:

1. The regulatory asset account previously authorized for the deferral of cash contributions will be considered a balancing account for the purpose of tracking the difference between cumulative cash contributions to the pension plan and amounts recovered in rates; and

2. The timing of the amortization of the deferred cash contributions as well as the amounts will be matched to the collection of those costs in rates; and

3. The amounts contributed in excess of the ERISA minimum, while potentially subject to longer amortization, will not be disallowed solely because they are made sooner than they are legally required to be paid; and

4. The unamortized balance of deferred cash contributions will earn a carrying charge at the Commission-approved interest rate for deposit.

COMMISSION FINDINGS

Idaho Power has requested approval of an annual tracker mechanism for recovery of defined pension benefit expenses. Staff contends that the requirements for justifying establishment of a tracking mechanism have not been satisfied and recommends that the Company's tracker proposal be denied. Staff recommends instead the deferral of cash contributions and the amortization of those costs in rates through the normal ratemaking process. The Company agrees that Staff's proposal (as clarified in reply comments) would satisfy SFAS 71 requirements.

The Commission has reviewed and considered the filings of record in Case No. IPC-E-09-29, including the comments and recommendations of Commission Staff and the Company's reply. We have also reviewed Order No. 30333 in Case No. IPC-E-07-07 wherein we authorized Idaho Power to account for its defined pension expense on a cash basis and to defer and account for accrued SFAS 87 pension expense as a regulatory asset. The Commission continues to find that the public interest may not require a hearing to consider the issues presented in this case and that the issues raised by the Company's filing may be processed by Modified Procedure, i.e., by written submission rather than by hearing. IDAPA 31.01.01.204.

It appears from Idaho Power's reply that although the Company prefers an annual tracker mechanism, it agrees that the accounting treatment of SFAS 87 pension expense recommended by Staff will satisfy SFAS 71 requirements, if clarified as it requests. We find the tracking mechanism recommended by the Company is not justified nor required. We authorize the clarified treatment of defined pension expense as detailed above in our summary of the Company's reply. We find this approach satisfies the SFAS 71 requirements. Furthermore, we adopt the four points of clarification requested by the Company in its reply comments, as set forth above.

CONCLUSIONS OF LAW

The Idaho Public Utilities Commission has jurisdiction over Idaho Power Company, an electric utility, pursuant to the authority and jurisdiction granted in Title 61, Idaho Code, and the Commission's Rules of Procedure, IDAPA 31.01.01.000 *et seq.*

ORDER

In consideration of the foregoing and as more particularly described and qualified above, IT IS HEREBY ORDERED and the Commission does hereby deny Idaho Power Company's request for a tracking mechanism to recover its defined benefit pension expense.

IT IS FURTHER ORDERED that the Company's cash contributions to its defined benefit pension plan will be deferred and the amortization of those costs will be reflected in rates as clarified above.

THIS IS A FINAL ORDER. Any person interested in this Order may petition for reconsideration within twenty-one (21) days of the service date of this Order. Within seven (7) days after any person has petitioned for reconsideration, any other person may cross-petition for reconsideration. See *Idaho Code* § 61-626.

DONE by Order of the Idaho Public Utilities Commission at Boise, Idaho this 17th day of February 2010.

JIM D. KEMPTON, PRESIDENT

MARSHA H. SMITH, COMMISSIONER

MACK A. REDFORD, COMMISSIONER

ATTEST:

Jean D. Jewell
Commission Secretary

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