KARL KLEIN
DEPUTY ATTORNEY GENERAL
IDAHO PUBLIC UTILITIES COMMISSION
PO BOX 83720
BOISE, IDAHO 83720-0074
(208) 334-0320
IDAHO BAR NO. 5156

Street Address for Express Mail:
472 W. WASHINGTON
BOISE, IDAHO 83702-5918

Attorney for the Commission Staff

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BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF THE APPLICATION OF IDAHO POWER COMPANY FOR AN ORDER APPROVING THE TRANSFER AND SALE OF CERTAIN ASSETS TO THE CITY OF MERIDIAN, IDAHO	)	**CASE NO. IPC-E-17-17** **COMMENTS OF THE COMMISSION STAFF**

The Idaho Public Utilities Commission's Staff comments as follows on Idaho Power Company's Application for approval of an asset sale to the City of Meridian, Idaho.

BACKGROUND

On December 6, 2017, Idaho Power Company applied to the Commission for an order approving transfer of certain assets to the City of Meridian (City) under Idaho Power's Rule M,[1] and *Idaho Code* §§ 61-328 and 61-524. Rule M governs the sale of Company-owned assets or facilities that are—as here—beyond the "point of delivery." The point of delivery (POD) is the point at which the customer's power-usage is measured, and "beyond the POD" refers to the customer side, rather than the utility side, of the POD. Order No. 33470 at 1.

[1] Idaho Power's Rule M Facilities Charge Service is on the Commission's website at: http://www.puc.idaho.gov/fileroom/tariff/electric/Idaho%20Power%20Company.pdf.

The assets serve the City's wastewater treatment facility. Application at 2. Idaho Power and the City agree the City will buy the assets and "obtain title to and assume ownership, operation, maintenance, and all liabilities associated with" them. *Id.*

Idaho Power initially said the sale price of the assets is $761,693. But the Company later revised the price down to $668,805. The Company reached these sales prices as follows.

In the Application, the Company stated the total sale price of the assets is $761,693. Exhibit B at 16, to Application. The Company explained that it "provided the methodology and resulting sale price to the City and answered the City's inquiries prior to execution of the Agreement." Application at 6. The methodology has five components: (1) net book value ($353,091); (2) true-up of past levelized rate of return ($81,280); (3) near-term rate of return impact resulting from the sale ($63,903); (4) near-term operational impact resulting from the sale of assets ($83,783); and (5) net tax gross-up ($161,432). *Id.* at 6-8. In addition, Idaho Power would collect "$480 in estimated work order closing costs [and] . . . $17,724 for costs associated with a sectionalizer" that Idaho Power "will reprogram to become the wastewater facility's POD." *Id.* at 8.

On January 19, 2018, after the Company had filed the Application and initial sales price, the Company made a supplemental filing to provide the Commission with an updated price, found in Section 3 of the Asset Purchase and Transfer of Title Agreement. As described in paragraph 9 of the Company's Application, the price is subject to change depending on the actual closing date of the sale. The Company explained the total transaction amount of $761,693 presented in the Company's Application was based on the sale closing in 2017. Because the sale is now expected to close in 2018, Idaho Power updated various elements of the purchase price calculation including those elements impacted by federal corporate income tax rate changes effective January 1, 2018. The updated price is $668,805, as shown in the following table. The updated price results primarily from the change in tax rates, but also reflects an additional year of depreciation in the net book value of the assets, an additional year of the true up of the past levelized rate of return, and other updates. The updated purchase is subject to change if Idaho Power replaces any assets before the transaction closes.

The Company included a table summarizing the proposed updates, which are subject to acceptance by the City of Meridian, as shown below:

Description	Revised Amount	Original Amount	Net Change
Purchase price components			
Net book value	$ 338,287	$ 353,091	$ (14,804)
True up of past levelized rate of return	90,486	81,280	9,206
Near-term rate of return impact resulting from sale of assets	63,319	63,903	(584)
Near-term operational impact resulting from sale of assets	83,016	83,783	(767)
Total Purchase Price - before tax	575,108	582,057	(6,949)
Net Gross-up for tax	77,266	161,432	(84,166)
Total Purchase Price -after tax	652,374	743,489	(91,115)
Work order closing costs	480	480	
Total Purchase Price	652,854	743,969	(91,115)
Sectionalizer Components			
Sectionalizer book value	9,321	9,882	(561)
Sectionalizer True up of past levelized rate of return	4,908	4,776	132
Total Price - before tax	14,229	14,658	(429)
Net gross up for tax	1,722	3,066	(1,344)
Sectionalizer Total	15,951	17,724	(1,773)
Total Amount Due	$ 668,805	$ 761,693	$ (92,888)

STAFF ANALYSIS

Commission Staff reviewed the Application, and believes it meets the Rule M's requirements. Staff thus recommends the Commission approve the sale.

Rule M

Idaho Power owns and operates certain transformers and other facilities beyond the POD for the sole purpose of meeting the City's service requirements. Rule M allows the City to purchase these facilities if the transaction satisfies the following provisions:

a. No mixed ownership of facilities. A Customer purchasing the Company-owned facilities installed beyond the POD must purchase all facilities listed on the Distribution Facilities Investment Report for that location.

b. The Customer must provide the operation and maintenance of all facilities installed beyond the POD after the sale is complete.

c. The Customer must prepay engineering costs for sales determinations taking greater than 16 estimated hours of preparation. Sales determinations equal to or less than 16 estimated hours of preparation will be billed to the Customer as part of the sales

agreement, or after the engineering is completed in instances where the sale is not finalized.

Staff believes that no mixed ownership of facilities will occur because of this transaction. Idaho Power and the City agreed that the City would purchase the assets and assume ownership, operation, maintenance, and all liabilities associated therewith. Therefore, Staff agrees with Idaho Power that this transaction satisfies the requirements of Rule M.

Under Rule M, the factors in *Idaho Code* § 61-328(3) will guide the sale of Company-owned facilities installed beyond the POD to the customer served by those facilities. *See* Order No. 33514 at 8-9, Case No. IPC-E-15-26.[2] The statutory factors most relevant to this case include: (a) the transaction is consistent with the public interest; and (b) the cost of and rates for supplying service will not be increased by reason of such transaction. Based upon the following analysis, Staff believes the transaction between Idaho Power and the City meets these two requirements specified in *Idaho Code* § 61-328(3).

Analysis of Sales Price Methodology

Idaho Power states that its sales price methodology ensures that the transaction will not negatively affect the Company or its other customers. The Company applied the methodology from Case Nos. IPC-E-15-26 and IPC-E-16-31 to calculate the sale price for the City. In its Application, the Company describes its five-component methodology for establishing the assets' price. These components, and the updated amounts associated with each component, are listed below:

Net Book Value	$338,287
True-up of Past Levelized Rate of Return	$90,486
Near-Term Rate of Return Impact Resulting from Sale of Assets	$63,319
Near-Term Operational Impact Resulting from Sales of Assets	$83,016
Net Tax Gross-up	$77,266
Subtotal	$652,374
Work Order Closing Costs	$480
Total	$652,854

[2] In its Order on Reconsideration, the Commission found that §§ 61-327 and -328 do not strictly apply because the property being transferred serves only a single customer and thus is not "devoted to public service." Order No. 33514 at 8-9. However, the Commission determined that the factors in § 61-328 are "an effective means of protecting the public interest and ensuring that ratepayers will not be harmed by such transactions," therefore they would be used for guidance. *Id.*

The Company's treatment of each component relies on an approach used to compute the Rule M monthly Facilities Charge rate, which was established in the Company's last general rate case and approved in Commission Order Nos. 32426 and 32481. This approach allows the Company to recover its authorized rate of return, book depreciation, operation and maintenance expenses, administrative and general expenses, income taxes, property taxes, regulatory fees, working capital, and insurance through a flat monthly Facilities Charge equal to 1.41% of the original costs of Company-owned equipment installed. The approach established a fixed, 31-year depreciation life for all Schedule 19 assets subject to the monthly Facilities Charge. After 31 years, the monthly Facilities Charge rate decreases to 0.59% because the Company is not authorized to recover either depreciation or a rate of return on fully depreciated capital assets.

Net Book Value

The assets include facilities installed between 1979 and 2017. The Company has determined the net book value for each asset as original investment cost less accumulated depreciation. Staff agrees with the Company's method for computing net book value, and believes its inclusion in the sales price to be appropriate.

True-up of Past Levelized Rate of Return

Depreciation causes the net book value of assets, the authorized return on those assets, and associated income taxes to decrease continuously over 31 years. To avoid the need for imposing an annually decreasing Facilities Charge, the 1.41% Rule M flat rate charge is computed to include a "levelized," time-value equivalent for these revenue requirement components. This allows a single Facilities Charge over the life of the equipment even though net book value decreases over time. Under the resulting levelized payment schedule, Facilities Charge customers effectively underpay the Company for the first ten years of an asset's life, but then overpay for the remaining period, so the Company fully recovers its revenue requirement over the asset's depreciable life. Thus, a customer who purchases a facility from the Company before it is fully depreciated still owes the Company a "true up" for the difference between the Company's authorized rate of return and the levelized rate recovered in the monthly Facilities Charge. Staff believes that the true up and the Company's methodology for computing this component are appropriate.

Near-term Rate of Return Impact Resulting from the Sale of Assets

Idaho Power states that, when a customer buys an asset subject to the Facilities Charge, the Company foregoes the return it would have earned through the Facilities Charge. The Company has limited opportunity to re-invest those funds in other assets, and cannot earn its authorized rate of return until an alternate investment is recognized in a future rate case. To offset this loss, the Company has included the present value of three years of the levelized rate of return component of the Rule M Facilities Charge. Consistent with prior cases, three years was used as an estimate of the average interval between general rate cases.

Staff agrees that the asset sale could cause lost return until an alternate investment is made and recognized in a future general rate case. Staff continues to believe this revenue loss could discourage the Company from selling its facilities. Staff thus maintains it is reasonable to include a revenue loss component in the asset evaluation methodology. Staff believes that including the near-term rate of return impact in the asset sales price is consistent with *Idaho Code* § 61-328.

Near-term Operational Impact Resulting from Sale of Assets

Part of the monthly Facilities Charge paid by the City is intended to recover costs associated with Operations & Maintenance ("O&M") and Administrative & General ("A&G") expenses. After the sale, the Company will no longer receive this revenue.

Idaho Power's pricing methodology includes three years of monthly Facilities Charge components related to O&M and A&G to offset the foregone revenue associated with costs related to regulatory fees, O&M, A&G, and working capital incurred on behalf of the facilities being purchased by the City. The Company explains that during a general rate case, the revenue requirement for the Schedule 19 customer class includes a revenue credit, or reduction, equal to the Facilities Charge revenue to be collected from Schedule 19 customers. Because the Company will not have an opportunity to recalculate the revenue requirement and reset rates until the next general rate case, it believes there will be a near-term operational impact resulting from the sale.

Staff believes that once the facilities are sold, Idaho Power will no longer be responsible for any O&M or A&G expenses or working capital associated with these facilities. Once the O&M and A&G expenses go away after the sale, Idaho Power should no longer need to receive a component of Facilities Charge revenue to cover these expenses. Because Schedule 19

customers should not be hurt, Staff might not have included this cost component in the sales price due to any near-term operational impact resulting from the sale. But Staff recognizes that the City has agreed to the sale price, and Staff believes the agreement does not violate *Idaho Code* § 61-328. Given the agreement is based upon its arms-length bargaining with Idaho Power, and for this case, Staff believes the transaction is reasonable.

Net Tax Gross-up

There is a mismatch between the straight-line depreciation methodology used to determine book value and the accelerated depreciation methods used for assessing income taxes. This mismatch will generally result in some, or all, of the asset's book value being treated as a gain for income tax purposes. Accordingly, it is necessary to "gross-up" this portion of the book value, and any other gain resulting from the sale. Staff agrees that the Company's net tax gross-up methodology is appropriate, but believes that the computation of the gross-up amount should be based only on the components in the assets' sales price.

Sectionalizer Compensation

The agreement provides the City must compensate the Company for certain costs associated with a sectionalizer at the wastewater treatment facility. The Company plans to reprogram the sectionalizer to allow it to become the wastewater facility's new POD. Although part of the transaction, the sectionalizer is not being sold to the City. Instead, the Company will continue to own, operate, and maintain the sectionalizer as the POD. Costs related to reprogramming the sectionalizer will not be part of the agreement.

Before the sale, and under Rule M, the sectionalizer was originally installed solely to benefit the City, with the City paying a monthly Facilities Charge based on a percentage of the Company's initial investment. Because the City will no longer pay a monthly Facilities Charge on this investment, the Company plans to recover its book value and the true up for the past levelized rate of return. This approach ensures customers are not harmed by the transaction. Because Idaho Power will continue to own, operate, and maintain the sectionalizer after the sale, the amounts related to the sectionalizer are separately presented from the assets to be sold to the City.

Updated Sectionalizer Book Value	$9,321
Updated Sectionalizer True-up of Past Levelized Rate of Return	$4,908
Net Tax Gross-up	$1,722
Total	$15,951

Staff agrees that the Company's treatment of the Sectionalizer book value, true up of the levelized rate of return, and net tax gross-up (based on an adjusted sales price) are appropriate and protects customers.

Summary

Staff agrees that the Company's treatment of net book value, true-up of the levelized rate of return, loss of near-term return, and net tax gross-up (based on an adjusted sales price) are appropriate and protect customers as required by *Idaho Code* § 61-328. Staff acknowledges that both Idaho Power and the City have signed the Agreement, agreeing to the updated sales price of $652,854 and other terms. The parties' mutually agreed upon sales price will not harm other customers or cause rates to increase. Staff thus concludes the proposed transaction satisfies *Idaho Code* § 61-328 and Idaho Power's Rule M.

Accounting Treatment

The Company's Application outlines the accounting treatment it will apply to the transaction if approved by the Commission. The Company's proposed accounting treatment will remove the assets from the Company's books, record the gain on the sale of the assets, and record the impact on the Company's income taxes. Staff has reviewed the proposed accounting treatment and believes it is reasonable.

RECOMMENDATIONS

Upon review of the Company's Application and following the Staff's investigation, Staff recommends that the Commission approve Idaho Power Company's Application to sell assets to the City of Meridian as proposed. Staff believes that the proposed sale meets the requirements of Idaho Power's Rule M. Should the Commission approve the Application, Staff further recommends that the Commission not endorse the Company's pricing methodology as precedent

going forward. Although the methodology often may be appropriate for establishing asset sales prices, Staff believes each proposed sale is unique, and that different circumstances may warrant different pricing methods or contract terms.

Respectfully submitted this 25th day of January 2018.

Camille Christen for
Karl Klein
Deputy Attorney General

Technical Staff: Kathy Stockton
Bentley Erdwurm
Richard Keller

i:umisc/comments/ipce17.17djhklsberk comments

CERTIFICATE OF SERVICE

I HEREBY CERTIFY THAT I HAVE THIS 25TH DAY OF JANUARY 2017, SERVED THE FOREGOING **COMMENTS OF THE COMMISSION STAFF,** IN CASE NO. IPC-E-17-17, BY MAILING A COPY THEREOF, POSTAGE PREPAID, TO THE FOLLOWING:

LISA D NORDSTROM
SHELLI D STEWART
REGULATORY DOCKETS
IDAHO POWER COMPANY
PO BOX 70
BOISE ID 83707-0070
E-mail: lnordstrom@idahopower.com
sstewart@idahopower.com
dockets@idahopower.com

MARK ANNIS
IDAHO POWER COMPANY
PO BOX 70
BOISE ID 83707-0070
E-mail: mannis@idahopower.com

SECRETARY