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BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

**IN THE MATTER OF THE APPLICATION OF)
PACIFICORP FOR AN ACCOUNTING ORDER)
REGARDING TREATMENT OF CERTAIN ASSET)
RETIREMENT OBLIGATIONS.)
)
)**

**CASE NO. PAC-E-03-8
COMMENTS OF THE
COMMISSION STAFF**

COMES NOW the Staff of the Idaho Public Utilities Commission, by and through its Attorney of record, Weldon B. Stutzman, Deputy Attorney General, in response to the Notice of Application and Notice of Modified Procedure in Case No. PAC-E-03-8 issued on August 22, 2003, submits the following comments.

BACKGROUND

On May 27, 2003, PacifiCorp dba Utah Power & Light Company (PacifiCorp; Company) filed an Application seeking an accounting order authorizing the Company to record regulatory assets or liabilities associated with implementation of Statement of Financial Accounting Standards (SFAS) 143. PacifiCorp's Application asks for an accounting order authorizing the Company to (1) record, as a regulatory asset or a regulatory liability, the cumulative financial statement impact resulting from the Company's implementation of SFAS 143, and (2) record on an ongoing basis, as a regulatory asset or a regulatory liability, an amount equal to the difference between the annual SFAS 143 depreciation and accretion expenses and the annual depreciation expenses based on Commission approved depreciation rates and coal mine reclamation accruals.

PacifiCorp also requests confirmation by the Commission that (1) asset removal costs, in the form of negative net salvage, are currently accrued through annual depreciation expense which is recoverable in rates; (2) these costs are based on estimates of the final removal costs; and (3) such costs are trued-up for ratemaking purposes at the time the related assets are retired and the actual removal costs are determined. On July 9, 2003, PacifiCorp provided Staff with additional information about its Application. Attachment A to these comments is PacifiCorp's "Reasons Why FAS 143 is not Appropriate for Ratemaking."

DISCUSSION OF SFAS 143 AND PACIFICORP'S APPLICATION

In June 2001, the Financial Accounting Standards Board (FASB) issued SFAS 143, Accounting for Asset Retirement Obligations, effective for fiscal years beginning after June 15, 2002. PacifiCorp will be implementing SFAS 143 in its 2004 fiscal year (April 1, 2003 through March 31, 2004).

The FASB issued SFAS 143 to address the inconsistencies in accounting practices for asset retirement obligations. FASB noted that obligations that meet the definition of a liability were not being recognized when incurred or the recognized liability was not consistently measured or presented. PacifiCorp is required to implement SFAS 143 in order to comply with Generally Accepted Accounting Principles.

Historically, under the accounting method currently used by PacifiCorp, the reasonable cost of removing a tangible long-lived asset at retirement is included in the calculation of depreciation rates and is recovered over the useful life of the asset. Because the cost of removal is included in depreciation expense, it is included in the Company's revenue requirement. In its Application, PacifiCorp is not requesting any changes to its currently approved depreciation rates or any change in the level of asset removal included in the Company's revenue requirement through depreciation expense.

SFAS 143 Asset Retirement Obligations (AROs)

As noted in PacifiCorp's Application, SFAS 143 requires entities to recognize and account for certain asset retirement obligations in a manner different from the way PacifiCorp has traditionally recognized and accounted for such costs. Specifically, if a legally enforceable

asset retirement obligation (ARO) as defined by SFAS 143¹ is deemed to exist an entity must measure and separately account and report the liability for the ARO (ARO Liability) on its books. This recognizes the entire cost of removal up-front while in ratemaking the cost of removal is included in depreciation expense over the life of the asset. The liability must be recorded at fair market value in the period in which the liability is incurred. SFAS 143 also provides that if market prices are not available, estimates of fair value can be calculated by discounting (using a credit-adjusted, risk-free interest rate) the estimated cash flows associated with the ARO to their present value at the date the liability is recorded. PacifiCorp will use the expected present value method to determine its ARO Liabilities and corresponding ARO Assets (see next section re: ARO Assets). If a company has chosen to remove assets for reasons other than legal obligations, then the future costs of removing those assets do not have to be recognized under SFAS 143.

PacifiCorp has determined that it will need to record AROs under SFAS 143 for certain generation and mining assets. The Company has also identified AROs for transmission and distribution assets. However, the timing of those obligations is indeterminate and the liability cannot be measured and recorded at this time according to PacifiCorp's Application. PacifiCorp states that there are no material AROs related to general plant assets.

SFAS 143 ARO Assets, Depreciation and Accretion Expenses

Under SFAS 143, at the same time the ARO Liability is recorded, a corresponding and equivalent Asset is also recorded on the entity's books as part of the cost of the associated tangible asset. The ARO Asset is then depreciated over the life of the associated tangible asset. In addition, a period-to-period increase in the carrying amount of the liability (accretion expense) is added to the ARO Liability annually to account for the time value of money, so that at the time of retirement the recorded ARO Liability will be sufficient to meet the legal obligation. Any gain or loss when the actual liability is paid in the future will be recognized in the Company's accounting records.

¹ According to SFAS 143, "it applies to legal obligations associated with the retirement of a tangible long-lived asset that result from the acquisition, construction, or development and (or) the normal operation of a long-lived asset, except...for certain obligations of lessees. As used in this Statement, a legal obligation is an obligation that a party is required to settle as a result of an existing or enacted law, statute, ordinance, or written or oral contract or by legal construction of a contract under the doctrine of promissory estoppel."

Cumulative Effect at Implementation Date

Upon initial implementation of SFAS 143, entities must establish in their financial statements all of the amounts that would have been recorded had the new requirements always been in place. PacifiCorp records this cumulative impact as transition entries. As part of these transition entries, PacifiCorp will reverse the costs already contained in its financial statements for legally obligated removals. This is done so that the Company will not have two different removal costs (costs required by SFAS 143 and costs required for ratemaking) included in its financial statements.

The initial implementation of SFAS 143 for PacifiCorp will create a regulatory asset for those tangible assets with a positive cumulative effect adjustment and a regulatory liability for those tangible assets with a negative cumulative effect adjustment. If the Commission authorizes the accounting order, the total net cumulative adjustment at this time will be a regulatory liability.

Rate-Regulated Entities, Regulatory Assets and Regulatory Liabilities

SFAS 143 applies to rate-regulated entities that meet the criteria for application of FASB Statement No. 71, Accounting for the Effects of Certain Types of Regulation. SFAS 143 recognizes that differences may exist between its requirements and the treatment of AROs for regulatory purposes. SFAS 143 provides that a regulated entity subject to SFAS 71 recognize differences between the two approaches as a regulatory asset or a regulatory liability as opposed to a charge or credit to net income if the requirements of SFAS 71 are met. PacifiCorp is requesting such treatment. The regulatory asset or regulatory liability will be removed at the time the related tangible long-lived asset is removed.

SUMMARY

SFAS 143 requires entities to separately account and report the liability for asset retirement obligations, capitalize the asset retirement costs, charge earnings for the depreciation of the asset and the accretion of the liability. Under SFAS 71, a public utility is permitted to record a regulatory asset or regulatory liability for differences between SFAS 143 and regulatory accounting for asset retirement obligations rather than recording such differences as a charge or credit to net income.

The Company's proposed accounting treatment will use SFAS 143 for reporting on its financial statements but retain its current methodology for ratemaking purposes. As a result,

there should be no rate change, now or in the future, associated with the application of the requested accounting treatment. Neither the SFAS 143 transition entries nor the annual accounting entries will change the level of costs included in rates.

STAFF RECOMMENDATIONS

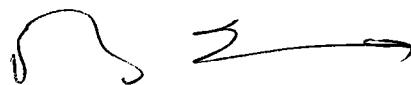
Staff recommends approval for PacifiCorp to record, as a regulatory asset or liability, the cumulative financial statement impact resulting from the implementation of SFAS 143, and to record the ongoing annual differences between the SFAS 143 depreciation and accretion expenses and the annual depreciation and reclamation expenses that are currently authorized by the Commission in depreciation rates and reclamation accruals.

Staff also recommends that the Commission require in its accounting order that PacifiCorp file annually and as part of its rate case filings, all journal entries made under the requirements of SFAS 143, including documents supporting the determination of regulatory assets and liabilities and related dollar amounts.

Staff acknowledges that PacifiCorp has a reasonable opportunity to recover prudently incurred removal costs. Staff recommends that the reasonableness of differences between actual and estimated costs should be addressed when those events occur. Staff recommends that no further confirmation be included in the Commission's accounting order.

Because these new accounting entries will not change the level of the costs included in rates, Staff is making no recommendation regarding the treatment of SFAS 143 Regulatory Assets and Regulatory Liabilities in future rate cases. If the assets and liabilities have an unanticipated affect on rates, then the ratemaking treatment should be determined at the time of the next rate case.

DATED at Boise, Idaho, this 22nd day of September 2003.



Weldon B. Stutzman
Deputy Attorney General

Technical Staff: Patricia Harms
Michael Fuss

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REASONS WHY FAS 143 IS NOT APPROPRIATE FOR RATEMAKING

PacifiCorp believes that it is not appropriate to apply the requirements of FAS 143 in determining asset retirement obligations (AROs) for ratemaking purposes. Rather, the Company believes that AROs (i.e., removal costs) should continue to be established through traditional depreciation studies and recovered through the application of Commission-approved depreciation rates. FAS 143 should not be used for ratemaking for the following reasons:

1. The primary focus of FAS 143 is on financial statement presentation rather than cost recovery.
 - The FASB provided the following two reasons for issuing FAS 143: (1) Users of financial statements indicated that the diverse accounting practices that have developed for obligations associated with the retirement of tangible long-lived assets make it difficult to compare the financial position and results of operations of companies that have similar obligations but account for them differently; and (2) Obligations that meet the definition of a liability were not being recognized when those liabilities were incurred or the recognized liability was not consistently measured or presented.
 - The provisions of FAS 143 are primarily focused on determining the appropriate amount of the ARO liability to be reflected in the financial statements.
 - For ratemaking purposes the issue with asset removal cost is not balance sheet presentation. The ratemaking issue is how to properly estimate removal costs and how to recover them in a fair and equitable manner from the utility customers being served by the assets. This process of estimation and recovery is best accomplished through traditional utility depreciation procedures that are subject to regulatory review and oversight.
2. Adoption of FAS 143 for ratemaking effectively transfers the determination of the appropriate amount of asset removal cost from regulators to the FASB.
 - When removal costs are determined through a depreciation study, if a regulatory Commission disagrees with the Company's estimates, the estimates are simply changed and the depreciation rates adjusted accordingly.
 - If the FAS 143 estimates of removal cost are to be used for ratemaking, then the Commission must accept whatever amount is calculated by the Company and determined by its external auditors to be in compliance with FAS 143.
3. Under the provisions of FAS 143, the recognition of removal cost in period expense over the life of the asset is "back-end loaded".
 - As a result of the application of present value techniques, FAS 143 results in removal expense that is lower in the early years of asset life and greater in the final years.

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- In contrast, for ratemaking purposes the goal of a depreciation study is to recover the cost of an asset, including removal cost, on a straight-line basis over the productive life of the asset.
4. The methods for determining the amount of removal cost required by FAS 143 are different than those traditionally used in utility depreciation analysis and adopted for ratemaking purposes, leading to potentially higher cost estimates.
- FAS 143 requires that the value of the removal liability be determined based on "fair value", which would ideally be based on a market price. In other words FAS 143 assumes that asset removal would be accomplished by a third party engaged by the utility. Use of a third party involves recognizing a profit margin in the removal cost estimate.
 - As a practical matter, utilities would normally use their own workforces to the extent possible to remove and dispose of utility assets. Thus the requirement by FAS 143 to include a third-party profit margin could lead to higher removal cost estimates than would be included in a traditional depreciation study.
5. Use of FAS 143 for ratemaking would create additional regulatory oversight issues.
- Under current procedures, all changes in asset lives as well as changes in asset salvage and removal costs are contained in a single comprehensive depreciation study that is prepared and submitted for regulatory review and approval at periodic intervals (normally five years).
 - If FAS 143 were adopted for ratemaking, it would still be necessary to prepare a depreciation study and submit it for review and approval. In addition, for assets that qualify for FAS 143 treatment, regulators would need to conduct a separate review of ARO calculations, interest rate determinations, the calculation of annual accretion and ARO asset amortization expense, etc.
 - When the recovery of asset removal costs is approved through a depreciation study, it remains in effect until the next study is prepared, typically five years. Potentially, under the provisions of FAS 143, new AROs could be added and the amounts of existing AROs could be updated each year; requiring virtually continuous regulatory oversight.

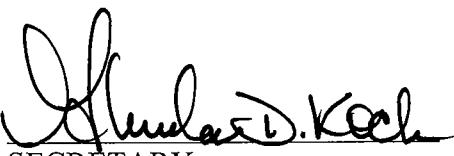
Attachment A
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CERTIFICATE OF SERVICE

I HEREBY CERTIFY THAT I HAVE THIS 22ND DAY OF SEPTEMBER 2003, SERVED THE FOREGOING **COMMENTS OF THE COMMISSION STAFF**, IN CASE NO. PAC-E-03-08, BY MAILING A COPY THEREOF, POSTAGE PREPAID, TO THE FOLLOWING:

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