Exhibit No.___ (MCD-10)
Docket No. UE-130043
Witness: Michael C. Deen

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION,	)	
Complainant,	)	Docket Nos. UE-130043
v.	)	
PACIFICORP D/B/A PACIFIC POWER & LIGHT COMPANY,	)	
Respondent.	)	

EXHIBIT NO.___(MCD-10)

EXCERPT FROM UE 246 ORDER NO. 12-493

June 21, 2013

available for fixed costs, such as construction or acquisition costs, and not variable costs, such as NPC.[20]

ICNU and CUB support Staff's proposed deadband and earnings test. They recommend, however, a 75/25 sharing mechanism for costs outside the deadband, with Pacific Power absorbing 25 percent of the costs outside of the deadband and ratepayers absorbing 75 percent. ICNU and CUB argue a larger sharing mechanism is warranted because it will help insulate Oregon customers from subsidizing the outcomes of Pacific Power's services to other jurisdictions. ICNU and CUB also contend the Commission should limit any necessary collections to 6 percent of Pacific Power's revenues for the last calendar year, and that a PCAM should not apply to direct access customers, who already bear the risk of variable power costs through their pricing structure.

iv. Kroger

Kroger joins Staff, ICNU, and CUB in opposing Pacific Power's proposed PCAM with dollar-for-dollar pass-through of annual power cost variance. Kroger states that a 100 percent cost pass-through seriously reduces Pacific Power's incentive to manage its fuel and purchased power costs as well as it would manage them if the utility remained fully responsible for the energy cost risk between TAM filings. Kroger recommends a 70/30 sharing mechanism to provide a more equitable balance between customer and shareholder interests, with 70 percent of the difference between forecasted and actual NPC allocated to customers, and 30 percent allocated to Pacific Power. Kroger notes that such power cost sharing provisions are in place in Pacific Power's Utah and Wyoming jurisdictions. Kroger argues 70/30 sharing meaningfully aligns utility and customer interests through shared benefits and costs.

b. Resolution

In adopting a PCAM for PGE, we articulated general principles that form the basis of a well-designed PCAM: (1) any adjustment under a PCAM should be limited to unusual events and capture power cost variances that exceed those considered normal business risk for the utility; (2) there should be no adjustments if the utility's overall earnings are reasonable; (3) the PCAM's application should result in revenue neutrality; (4) the PCAM should operate in the long-term to balance the interests of the utility shareholder and ratepayer; and, implicitly, (5) the PCAM should provide an incentive to the utility to manage its costs effectively.[21]

Applying those principles, we adopted a PCAM structure for PGE as follows. First, we established a deadband so that PGE would absorb some normal variation of power costs. If the power cost variation fell within the deadband, there would be no power cost rate adjustment. We concluded a power cost deadband should be calculated based on PGE's overall rate base. To ensure the PCAM was revenue-neutral, we adopted an asymmetric deadband that did not change rates when excess power costs were less than the equivalent

[20] *Id.* at 10, citing ORS 469A.120.
[21] Docket Nos. UE 180, UE 181, UE 184, Order No. 07-015 at 26-27 (Jan 12, 2007).

of 150 basis points of authorized ROE or when power cost savings were less than the equivalent of 75 basis points of the utility's ROE.

Second, we adopted a sharing mechanism: for any power costs above or below the deadband, customers will bear 90 percent of the adjustment, and PGE will bear 10 percent of the adjustment. We concluded that the 10 percent share provides PGE "with an incentive to manage its costs effectively, while sharing costs that are beyond normal business risk."[22]

Third, we applied an earnings test to determine whether the utility is earning an acceptable ROE. As noted, an earnings test serves to protect customers from paying for higher-than-expected power costs when the utility's earnings are reasonable, while protecting the utility from refunding power cost savings when it is under-earning. We established an earnings test of +/- 100 basis points around the utility's allowed ROE. Thus, if PGE is earning within +/- 100 basis points of this authorized ROE, then there would be no power cost adjustment for that year. If the utility's earnings are more than 100 basis points below its authorized ROE, then it would be allowed to recover excess power costs, after application of the deadband and 90/10 sharing, up to an earnings level that is 100 basis points less than its authorized ROE. If the utility's earnings are more than 100 basis points above its authorized ROE, then it would be required to refund to customers power cost savings, after application of the deadband and sharing, down to the ROE plus 100 basis points threshold.

Finally, we limited amortization of deferred amounts under the PCAM in any one year to 6 percent of PGE's revenues for the preceding calendar year. Later, we adopted a stipulation that modified PGE's PCAM in one respect—changing the deadband from basis points to a set dollar amount. Under this modification, the negative annual power cost variance deadband was set at $15 million, and the positive annual power cost variance deadband was set at $30 million.[23]

After reviewing the factual record and the parties' arguments in this proceeding, we conclude that our reasoning used to establish a PCAM for PGE remains sound and applies equally with respect to establishing a PCAM for Pacific Power. We note that wind integration costs represent a small portion of all of Pacific Power's NPC, and even that portion is difficult to determine. While we acknowledge that ORS 469A.120(1) provides for recovery of prudently incurred SB 838 compliance costs, we find it unreasonable to adopt a straight dollar-for-dollar PCAM for the totality of Pacific Power's NPC to address appropriate recovery for costs that may amount to far less than 2 percent of that total—particularly when those costs may be difficult to quantify precisely. We find that the most prudent way to accomplish proper recovery is through a well-designed PCAM that complies with the principles we summarized above.

Accordingly, we adopt a PCAM for Pacific Power identical to that adopted for PGE. The PCAM will contain the following features:

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[22] *Id.* at 27.
[23] *In the Matter of PGE*, Docket No. UE 215, Order 10-478 (Dec 17, 2010).

1. *Deadband.* We adopt a deadband to require Pacific Power to absorb some normal variation of power costs. If the power cost variation falls within this deadband, there will be no power cost rate adjustment. To ensure the PCAM is revenue neutral, we adopt an asymmetric deadband, with a negative annual power cost variance deadband of $15 million, and a positive annual power cost variance deadband of $30 million. We base our adopted power cost deadband on Pacific Power's authorized rate base, rather than on the utility's net power costs. In determining an appropriate power cost deadband, we look to the size of the utility's rate base and to the utility's authorized ROE. Although Pacific Power's rate base is slightly larger than PGE's we find these amounts to be reasonable for use in the PCAM.

2. *Sharing Mechanism.* To provide Pacific Power the incentive to manage its costs effectively, we adopt a sharing mechanism. For any power cost variance above or below the deadband, customers will bear 90 percent of the adjustment and Pacific Power will bear 10 percent of the adjustment.

3. *Earnings Test.* To protect customers from paying for higher-than-expected power costs when the utility's earnings are reasonable, and to protect Pacific Power from refunding power cost savings when it is under-earning, we adopt an earnings test of +/- 100 basis points around Pacific Power's allowed ROE. If Pacific Power is earning within this range of its authorized ROE, there will be no power cost adjustment for that year.

4. *Amortization Cap.* To be consistent with our prior practice with use of similar mechanisms for other energy utilities, we limit amortization of deferred amounts under the PCAM in any one year to 6 percent of Pacific Power's revenues for the preceding calendar year.

5. *Direct Access.* The PCAM will not apply to direct access customers, because they already bear the risk of variable power costs through their pricing structure.

We conclude that the adoption of this PCAM will result in just and reasonable rates.

2. *Transition Adjustment Mechanism*

a. *Parties' Position*

i. Pacific Power

Pacific Power states that the TAM should be preserved. Pacific Power notes a key objective of the TAM is to update forecast NPC to account for changes in market