

**BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA**

In the Matter of the Application of PACIFICORP (U 901 E), an Oregon Company, for an Order Authorizing a Rate Increase Effective January 1, 2011 and Granting Conditional Authorization to Transfer Assets, pursuant to the Klamath Hydroelectric Settlement Agreement.

Application No. 10-03-015
(Filed March 18, 2010)

**REPLY OF PACIFICORP (U-901-E) TO PROTEST OF DIVISION OF RATEPAYER
ADVOCATES**

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Date: May 6, 2010

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Pursuant to Rule 2.6(e) of the Rules of Practice and Procedure (“Rules”) of the California Public Utilities Commission (“Commission”), PacifiCorp, d.b.a. Pacific Power (“PacifiCorp” or “Company”), respectfully submits this reply to the Protest of the Division of Ratepayer Advocates (“DRA”) to PacifiCorp’s Application for an Order Authorizing a General Rate Increase Effective January 1, 2011 (“Application”). By separate filing submitted concurrently with this reply, PacifiCorp also submits a response to DRA’s Motion to Hold in Abeyance the Application (“Motion”).

I. INTRODUCTION AND BACKGROUND

A. DRA’s Motion and Protest

DRA’s Protest and Motion of April 26, 2010 do not dispute any authority for PacifiCorp’s requests under the Application.¹ Rather, both pleadings argue that consideration of

¹ PacifiCorp’s Application requests the Commission to authorize three items that are required to facilitate implementation of the Klamath Hydroelectric Settlement Agreement: (1) implementation of a rate surcharge to begin collection of California’s share of a dam removal trust; (2) establishment of an accelerated depreciation

PacifiCorp's Application is premature until California voters pass the Safe, Clean, and Reliable Drinking Water Supply Act of 2010 ("Bond Measure"). The primary difference between the two pleadings is that the Motion requests that PacifiCorp's Application be held in abeyance until after the Bond Measure has passed or California has secured alternative financing for its share of the dam removal costs; whereas the Protest recommends that the Commission deny the Application without prejudice and direct PacifiCorp to file a new application after the Bond Measure has passed or California has secured alternative financing for its share of the dam removal costs.

As discussed in more detail below, PacifiCorp asserts that its Application is not premature and the potential for delay and frustration of the Klamath Hydroelectric Settlement Agreement ("KHSA") far outweigh the few potential benefits that DRA asserts would arise from postponing consideration until after a decision on the Bond Measure.

B. Klamath Hydroelectric Settlement Agreement

The execution of the KHSA furthers the long standing policy preference of the federal government and the states of Oregon and California that the Company's dams on the Klamath River be removed. The process leading up to its execution was extremely complex and challenging, requiring the cooperation and agreement of 28 parties, including the states of California and Oregon, the federal government, Klamath Basin Tribes, counties, conservation groups, fishing groups, and farming and ranching organizations. Ultimately, the parties negotiated terms under the KHSA that resulted in a fair and balanced outcome for PacifiCorp's customers and other stakeholders.

schedule that will depreciate the rate base associated with the dams and related relicensing and settlement costs on a straight-line basis over the expected period of generation, which could end as early as December 31, 2019; and (3) conditional approval to transfer the dams and related property to the entity that will remove the dams.

The KHSA outlines the multiple conditions precedent and obligations of certain parties necessary to accomplish the removal of the dams. Significantly, these conditions are interrelated and highly dependent on parties fulfilling their respective obligations. Any delay or failure to meet such obligations has the potential to jeopardize the trust, cooperation and momentum achieved thus far among the parties.

Pursuant to the KHSA, PacifiCorp was required to request that the Commission establish a non-bypassable customer surcharge to generate funds for California customers' 8 percent share of the customer contribution to dam removal costs. The surcharge amount for California customers is capped at approximately \$16 million. Under the Application, the surcharge is designed to spread \$13.76 million equally over a 9-year period beginning on January 1, 2011, resulting in an annual collection rate of approximately \$1.53 million per year. Significantly, the KHSA limits the surcharge to never exceed two percent of the revenue requirement set by the Commission for PacifiCorp as of January 1, 2010.²

The KHSA also requires PacifiCorp to transfer ownership of the dams and related property once the Dam Removal Entity notifies PacifiCorp that all necessary permits and contracts for removal have been accomplished.³ PacifiCorp's Application represents the first and necessary step in what will be a series of dependent and interrelated obligations by other parties to the Agreement.

II. DISCUSSION

A. Surcharge

DRA's Protest requests the Commission to deny or, as argued in its Motion, delay its consideration of PacifiCorp's request for approval to begin collecting the surcharge on January 1,

² KHSA at p. 23-24.

³ KHSA at p. 51.

2011.⁴ In short, DRA argues that PacifiCorp’s request is premature because: (1) passage of the Bond Measure is a condition precedent under the KHSA for going forward with dam removal; and (2) the Bond Measure will be decided in November and therefore, the Commission should delay consideration of the Application until after the Bond Measure is decided or other dam removal funding mechanisms are secured.⁵ DRA contends that such a delay “. . . would be a small price to pay to avoid the possibility of parties submitting additional testimony, participating in hearings and briefing, followed by a Commission decision, in the event the Bond Measure is not approved and given the future uncertainty of securing ‘other appropriate financing mechanisms.’”⁶

1. PacifiCorp’s request for approval to begin collecting the surcharge on January 1, 2011 is not premature and any further delay could frustrate the ultimate objective of the KHSA—removal of the dams

PacifiCorp submits that delaying consideration of its request to begin collecting the surcharge until after the Bond Measure is decided is unwarranted and, contrary to DRA’s suggestion, could potentially come at an extremely high price—frustration of the implementation of the KHSA and increased costs for the California customers of PacifiCorp. Multiple parties, including the state of California, worked for over a decade to achieve the delicate balance of compromise embodied in the KHSA. The success of the KHSA is wholly dependent on the cooperation of all parties in meeting the obligations set forth in the KHSA. Moreover, each obligation is interrelated, and sequentially dependent on the successful completion of other parties’ obligations. PacifiCorp’s obligation to file an application to obtain Commission approval of the surcharge is the first in a series of multiple conditions and obligations. Delay in consideration of this important initial request could potentially result in a cascading loss of trust

⁴ Protest at p.7; Motion at p.7.

⁵ Protest at p.7; Motion at pp. 1-2.

⁶ Protest at p.7; *See also*, Motion at pp. 1-2.

and momentum among the parties in meeting the obligations under the KHSA. The Commission must take into consideration the fact that the state of California, through the action of Governor Schwarzenegger signing the KHSA, has expressed its support for the settlement and the implementation of the steps necessary to effectuate it.

In Section 7.3 of the KHSA, a target date of December 31, 2020 is established for completion of Facilities Removal. In order to achieve this target date, the parties agreed to implement the settlement based on a specified approach, including the following steps related to the collection of funds from PacifiCorp customers:

- A. Collect \$172 million of the total Customer Contribution by December 31, 2019, consistent with Section 4;
- B. Earn approximately \$28 million on the Klamath Trust Accounts to provide Value to Customers, which results in a total of \$200 million in the accounts available for Facilities Removal costs as illustrated in Appendix H to this Settlement.

Appendix H to the KHSA assumed that collection of the surcharges would begin in January 2010 and would continue for 10 years. The Appendix also assumed that interest would accrue over the ten-year period at an interest rate of 3.5 percent. The accrual of interest was used to decrease the surcharge amount from a total of \$200 million to \$172 million. Any further delay in beginning surcharge collection will decrease the amount of interest earned in the surcharge accounts and could result in the need to increase the amount of the surcharge to be collected from customers. PacifiCorp strongly opposes a delay in the creation of the surcharge because it will increase the out-of-pocket contribution of its customers to the cost of implementing the KHSA.

By comparison, DRA's concern focuses not on customer impacts, but on a concern that DRA's time and resources might be wasted in the event the Bond Measure fails. The Commission must remember that the Bond Measure is not the only means by which California

can fund the remainder of the dam removal costs to be contributed in addition to the customer funds obtained through the surcharge. For example, a legislative appropriation could supply the funds. Thus the ultimate source and timing of this portion of California's contribution is not dependant solely on the results of the Bond Measure voting. As a result, irrespective of the election results, it is important for the Commission to continue processing PacifiCorp's Application which addresses other equally important preconditions of the settlement.

While none of the parties to the KHSA can be absolutely certain that all the preconditions will be met so as to permit removal of the dams on schedule, PacifiCorp firmly believes that it is not a waste of time for the Commission to address the key aspects of the KHSA over which it has jurisdiction in a timely manner, and thereby demonstrate that both California and PacifiCorp are actively working to fulfill their obligations under the KHSA. The Commission should also be aware that by virtue of a statute already passed by the Oregon Legislature, Oregon customers of PacifiCorp have already begun to contribute to the dam removal costs.⁷ It is important for California to keep pace with the implementation steps already underway in Oregon. PacifiCorp asserts that the risks of frustrating or delaying the KHSA far outweigh any concern that DRA would be required to participate in a hearing while the ultimate outcome of the settlement implementation remains subject to further contingencies.

⁷ On July 14, 2009, the Oregon Legislature passed Senate Bill 76, codified at ORS §§757.732 through 757.744. Pursuant to ORS § 757.736(2), the Company was required to file the KHSA along with tariffs with immediate effective dates on March 18, 2010 (within 30 days of execution of the KHSA) for the collection of two non-bypassable surcharges for the costs of removing the Klamath dams. At its March 30, 2010 public meeting, the Public Utility Commission of Oregon approved PacifiCorp's request to allow the surcharges to remain in effect until such time as the Public Utility Commission of Oregon determines that the surcharges result in rates that are fair, just, and reasonable.

2. Further delay in consideration of the Application could potentially result in a surcharge that exceeds the two percent of the revenue requirement threshold required by the KHSA

As noted above, the KHSA requires that PacifiCorp request the Commission to establish a surcharge to generate funds for California's customers' 8 percent share of the Customer Contribution to dam removal costs (calculated to be \$13.76 million) that can never exceed two percent of the revenue requirements set by the Commission for PacifiCorp as of January 1, 2010. The surcharge is designed with a January 1, 2011 effective date to accommodate that limit. If consideration of PacifiCorp's Application is delayed, PacifiCorp's surcharge effective date would inevitably slip, jeopardizing the Company's ability to collect California's share of the customer surcharge under the two percent of revenue requirement threshold.

3. The KHSA provides for use of the surcharges to benefit customers in the event that dam removal does not proceed

It also is important to note that funds collected from the surcharges will ultimately be used to benefit customers, even in the event the dam removal process does not go forward due to failure of the Bond Measure or some other reason. As described in PacifiCorp's Application, funds collected from the proposed surcharges would be remitted by PacifiCorp into two trust accounts to be created by the Commission. Section 4.4 of the KHSA outlines specific contingency plans in the event that (1) excess funds remain in the trust accounts after dam removal, or (2) one or more dams are not removed. In all events, the Commission retains the authority to ensure that the funds are used for the benefit of customers, including possible refund. As such, there is no risk that funds collected under the proposed surcharges would not benefit customers.

B. Accelerated Depreciation and Relicensing and Settlement Process Costs

DRA also argues that consideration of PacifiCorp's request for approval for accelerated depreciation of its remaining investment in the dams and its relicensing and settlement costs is premature.⁸ Again, DRA's basic rationale is that there is no need for the Commission to expend time and resources considering PacifiCorp's request until after the Bond Measure is decided or other dam removal funding mechanisms are secured.⁹ DRA further argues that it would be overly complicated for the Commission to reverse the effects of accelerated depreciation in the event that dam removal does not move forward. Finally, DRA adds that "... PacifiCorp and its shareholders would not be disadvantaged or otherwise harmed by a delay because its settlement and relicensing costs are secure and accruing interest as booked to Allowance for Funds used During Construction ["AFUDC"] and shareholders will continue to recover normal depreciation."¹⁰ DRA is incorrect in these assertions.

1. The Commission would not be required to order refunds to customers in the event the dam removal process does not move forward

With respect to DRA's argument regarding the burdensome nature of reversing the accelerated depreciation in the event that the KHSAs does not ultimately go forward, PacifiCorp points to the common and routine practice of adjusting depreciation schedules in Commission ratemaking proceedings. Depreciation rates are reviewed and adjusted as part of the normal course of business. For example, updated depreciation rates are currently under review as part of PacifiCorp's pending general rate case, A.09-11-015. Moreover, contrary to DRA's suggestion, the Commission would not be required to refund the accelerated portion of the depreciation to customers in the event the dam removal process stalled. Rather, the Commission could adjust the depreciation schedules on a prospective basis and apply the new schedules to the remaining

⁸ Protest at pp. 8-9; Motion at pp. 9-10.

⁹ Protest at pp. 8-9; Motion at pp. 9-10.

¹⁰ Protest at p. 9; Motion at p. 9.

net investment in the Klamath projects. This is neither burdensome nor unfair to customers, who will pay rates based on the correct depreciation schedules over the long term, irrespective of whether the KHSA is implemented or not.

2. The Company cannot indefinitely book AFUDC on costs related to the relicensing and settlement process costs

As to DRA's second line of reasoning regarding AFUDC, PacifiCorp wishes to clarify that pursuant to Federal Energy Regulatory Commission ("FERC") rules of accounting, relicensing and settlement costs may not indefinitely accrue AFUDC. Instead, FERC allows recovery of AFUDC while a utility is seeking relicensing.¹¹ It is the Company's opinion that as of December 31, 2010, AFUDC would be shut off unless the Company petitioned the Commission to treat the relicensing and settlement costs as a regulatory asset. This potential requirement, combined with the possibility that the relicensing and settlement process costs could receive different treatment in Oregon and California introduces a significant complication for the Company. PacifiCorp believes that the appropriate course is for the Commission to initiate the ratemaking adjustments contemplated by the KHSA, thus avoiding the potential for PacifiCorp to be denied a fair return on its costs if AFUDC treatment were disallowed in some fashion. The risk of such an action far outweighs DRA's argument that it should be spared from the inconvenience of participating in the case until the Bond Measure has been passed.

3. Any delay in implementation of the surcharge or accelerated depreciation will increase impacts on customers

The proposed surcharge is currently designed to spread \$13.76 million equally over a 9-year period beginning on January 1, 2011. As noted above, any further delay in beginning surcharge collection will decrease the amount of interest earned in the surcharge accounts and could result in a need to increase the amount of the surcharge to be collected from customers up

¹¹ Code of Federal Regulations, Electric Plant Construction, Number 3 Item 17.

to the cap of \$16 million—up to \$2.32 million more than what is currently proposed in the Application.

As explained in PacifiCorp's Application, the Company has a general rate case pending in A.09-11-015. The Company's rate case includes an adjustment that reflects the shorter depreciation lives, as well as the addition to rate base of the relicensing and settlement process costs. This adjustment increases California's revenue requirement by approximately \$330,000. The effective date of the rate change in the general rate case is also January 1, 2011. Given the three-year rate case cycle in California, if the Commission does not implement the accelerated depreciation requested effective January 1, 2011, it will not have the opportunity to implement this adjustment until January 1, 2014. As a result, the hydroelectric assets would need to be depreciated over a 6-year, rather than a 9-year, period. The longer schedule proposed by PacifiCorp helps mitigate the impact on customers while a three-year delay would increase the impact to customers from approximately \$330,000 to \$630,000. Again, PacifiCorp suggests that the risk of such an increased impact on customers far outweighs the concerns of DRA regarding participation in the proceeding when the ultimate results remain subject to further contingencies.

C. Transfer of dams and related property

Finally, DRA argues consideration by the Commission of PacifiCorp's request to transfer the dams and related property pursuant to Section 851 of the Public Utilities Code is premature until after the Bond Measure is decided or other dam removal funding mechanisms are secured.¹² As stated by DRA, "[t]here will be ample time to consider issues related to the requested transfer of assets pursuant to Section 851 once the source of funding for dam remove [sic] is certain."¹³

¹² Protest at p.10; Motion at p.10.

¹³ Protest at p.10; Motion at p.10.

For the reasons discussed above, the Company's requests under this Application are not premature and are timely to ensure orderly implementation of the KHSA.

It is appropriate for the Commission to consider all elements of the implementation of the KHSA in the same application rather than in several applications spread over time. PacifiCorp opposes DRA's suggestion for the reason that it would effectively create an additional, unilateral precondition on KHSA implementation, namely the requirement to return to the Commission and seek Section 851 approval to transfer the hydroelectric assets to the Dam Removal Entity, after the Commission has already authorized the surcharge and depreciation ratemaking adjustments. PacifiCorp believes that such an additional step is unnecessary, as no transfer authority will be effective unless all the KHSA preconditions are met, and it will create additional uncertainty in other parties' minds as to whether the Commission will fully support implementation of the KHSA.

D. Issues related to PacifiCorp's Application

DRA also provides a preliminary list of issues related to the Application. PacifiCorp agrees that DRA's list includes issues that should be considered as part of this proceeding and is committed to working with DRA to develop a mutually agreeable case schedule that will allow for development and discovery with respect to these issues.

III. CONCLUSION

PacifiCorp's Application is not premature and the potential for delay and frustration of the KHSAs far outweigh any potential benefits to be achieved by postponing consideration until after a decision on the Bond Measure. For this, and the reasons stated herein, PacifiCorp respectfully requests the Commission deny DRA's request to deny PacifiCorp's Application as set forth in the Protest.

Respectfully submitted this May 6, 2010, at San Francisco, California.

By Jordan A. White/MT
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Certificate of Service

I hereby certify that, pursuant to the Commission's Rules of Practice and Procedure, I have this 2nd day of June, 2010, at Portland, OR, provided via electronic mail a true and correct copy of PacifiCorp's (U 901-E) Reply to Protest of Division of Ratepayer Advocates to the following parties:

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