State of Utah
Department of Commerce
Division of Public Utilities

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MEMORANDUM

To: Utah Public Service Commission

From: Utah Division of Public Utilities

Chris Parker, Director

Artie Powell, Energy Section Manager

Charles Peterson, Technical Consultant

Jeff Einfeldt, Utility Analyst

Lane Mecham, Utility Analyst

Date: September 18, 2018

Re: **DPU Comments Relating to the Sharing Band in the Energy Balancing Account.**
Docket No. 18-035-01 (As referenced by 09-035-15)

RECOMMENDATION

The Division of Public Utilities (Division) continues to believe that the elimination of the sharing band in the PacifiCorp Energy Balancing Account (EBA) is not in the public interest. The Division recommends that the sharing band as originally set up by the Public Service Commission (Commission) in its order creating the EBA in Docket No. 09-035-15 should be reinstated at the earliest possible moment.

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ISSUE/REQUEST

The Public Service Commission (Commission) has invited comments from interested parties by September 18, 2018,[1] regarding the Commission's report to the state legislature's Public Utilities and Technology Interim Committee. The Division's comments relate to the EBA in general and the 70/30 sharing band in particular.

DISCUSSION AND COMMENTS

In May of 2016, S.B. 115, the Sustainable Transportation and Energy Plan Act (Act) became effective. The bill "allows an electrical corporation to recover 100% of the electrical corporation's prudently incurred costs in an energy balancing account." The electrical corporation that the bill currently applies to is PacifiCorp (Utility). Prior to the Act, any difference between PacifiCorp's base net power costs (NPC) and actual NPCs were passed through the EBA, subject to a 70/30 "sharing band". The PacifiCorp EBA was established by the Commission in Docket No. 09-35-15. The sharing band eliminated recovery or payment of 30% of the variation between Base NPC's and Actual NPC's. The original 70/30 sharing band provided incentives for PacifiCorp to manage its costs and share business risk with ratepayers and reduce the fluctuations in customers' bills from year to year. The elimination of the sharing band is a significant shift of risk to ratepayers.

In Docket 09-035-15, the Division, the Office, and some intervenors argued the sharing band was in the public interest. The parties argued that a sharing mechanism would be necessary to retain economic incentives to "promote optimal planning, expansion and efficient operation that would otherwise be lost if all excess net power cost were passed on to customers."[2] The Commission concluded that the sharing band was necessary to keep both the Utility and ratepayers at risk:

[1] Public Service Commission, Docket No. 18-035-01, "Scheduling Order, Notice of Hearings, and Tariff Status", page 3.
[2] Docket No. 09-035-15, In the Matter of the Application of Rocky Mountain Power for Approval of its Proposed Energy Cost Adjustment Mechanism, March 2, 2011, Report and Order, p. 39

> We recognize, however, relying solely on prudence reviews will shift too much of the risk for suboptimal planning and operation currently borne by the company, who is in the best position to manage this risk, to customers, who are not. Therefore, the balancing account we adopt requires both Company [PacifiCorp], customers and shareholders to remain at risk for a portion of the actual net power cost which deviates from approved forecasts. This decision recognizes the value of Company management having meaningful financial incentives to minimize net power cost in the short-run and long-run, regardless of the extent of net power cost volatility. We find a sharing mechanism is the best method, at this point, to ensure customer and shareholder interests are aligned and the public interest is maintained.[3]

The only party opposed to the sharing mechanism in the docket was the Utility, which argued that there were ample opportunities for review of the prudency and that the sharing mechanism was unnecessary.

SUBSEQUENT FINDINGS

In May of 2016, the Division filed comments with the Commission on its evaluation of the PacifiCorp EBA, part of which included the evaluation of the sharing mechanism (Division Report).[4] The DPU asked other interested parties for comments to be addressed in the Division Report. The Division also solicited comments from its outside consultants Daymark Energy, which were also included in the Division Report. As set forth in the Division Report, the Utah Association of Energy Users (UAE), the Division, and Daymark all concluded that the sharing band was in the public interest and that the changes made in SB 115 to allow 100% recovery of costs further shifted risks onto ratepayers and minimized the incentives for good decision making[5]. The Division further argued that the volatility of customers' bills had increased

[3] Docket No. 09-035-15, In the Matter of the Application of Rocky Mountain Power for Approval of its Proposed Energy Cost Adjustment Mechanism, March 2, 2011, Report and Order, p. 69
4 Docket No. 09-035-15, In the Matter of the Application of Rocky Mountain Power for Approval of its Proposed Energy Cost Adjustment Mechanism, May 20, 2016, Redacted Comments from the Division of Public Utilities
5 Docket No. 09-035-15, In the Matter of the Application of Rocky Mountain Power for Approval of its Proposed Energy Cost Adjustment Mechanism, May 20, 2016, Redacted Comments from the Division of Public Utilities, pp. 60, 65.

significantly since the creation of the EBA, which is magnified by the removal of the 70/30 sharing band, since it funnels more costs through the surcharge/credit on customers' bills.[6]

The Division Report also highlighted the fact that even though a shift in risk onto ratepayers had occurred, the return on equity had not been adjusted to compensate for the reduction in risk the Company previously assumed. Generally, financial and economic theory suggests that investors are rewarded with higher returns when more risk is assumed by the investors, and lower returns when fewer or no risks are assumed. Though the company now faces less risk it has maintained its allowed return.

CONCLUSION

The Division believes the EBA is beneficial to the Utility with little to no net benefit to ratepayers. The elimination of the sharing band further benefits the company and magnifies the problem of shifting risks onto ratepayers. It also does not compensate ratepayers for this additional risk by adjusting the return on equity for the Utility. By effectively guaranteeing the Utility 100% recovery of its net power costs, the EBA as now implemented misaligns the Utility's incentives in forecasting, managing net power costs, accounting for net power costs, and overall operational efficiency. The Division recommends that the EBA be eliminated, but should it survive, a sharing band should be reinstated to maintain a reasonable level of incentives to the Utility to manage the risks it faces, and not simply pass those risks to ratepayers.

CC Service List

6 Docket No. 09-035-15, In the Matter of the Application of Rocky Mountain Power for Approval of its Proposed Energy Cost Adjustment Mechanism, May 20, 2016, Redacted Comments from the Division of Public Utilities, p. 29.