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Department of Commerce
Division of Public Utilities

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ACTION REQUEST RESPONSE

To: Utah Public Service Commission

From: Division of Public Utilities
Chris Parker, Director
Artie Powell, Energy Section Manager
David T. Thomson, Technical Consultant
Jeff Einfeldt, Utility Analyst

Date: February 1, 2019

Re: **Docket No. 18-035-48** – Application of Rocky Mountain Power for an Accounting Order for Settlement Charges Related to its Pension Plans

RECOMMENDATION (NO APPROVAL)

The Division of Public Utilities ("Division") recommends that the Public Service Commission ("Commission") not approve PacifiCorp's dba Rocky Mountain Power's ("RMP" or the "Company") request to: (1) defer the expected impacts associated with the occurrence of a pension event in 2018, and any subsequent similar pension events; and (2) amortize the impact of pension events (i.e., the increase or reduction in regulatory assets or liabilities) to expense over the same period that is used to amortize the underlying regulatory assets or liabilities with the opportunity to recover the amount in future rates as part of net periodic benefit costs.

ISSUE

On December 31, 2018, the Company filed an application for approval of a deferred accounting order. In the application, the Company requests the Commission issue an order authorizing the Company to: (1) defer the expected impacts associated with the occurrence of a pension event in 2018, and any subsequent similar pension events; and (2) amortize the impact of pension events (i.e., the increase or reduction in regulatory assets or liabilities) to expense over the same period that is used to amortize the underlying assets or liabilities with the opportunity to recover the amount in future rates as part of net periodic benefit costs.[1] Together, these would allow the Company to account for the impact of pension events, such as settlements and curtailments, through deferral and amortization in a manner that closely approximates the amortization that would have continued if it were not for the accelerated recognition required by standard accounting principles due to occurrence of a pension event.[2]

On December 31, 2018, the Commission issued an Action Request to the Division requesting the Division review the application and make recommendations. The Commission asked the Division to report back by January 30, 2019. On January 2, 2019, the Commission issued a Notice of Filing and Comment Period. The notice stated that any interested party may submit comments on the application on or before Friday, February 1, 2019, and reply comments on or before Tuesday, February 19, 2019. This memorandum represents the Division's response to the Commission's Action Request and Notice of Filing and Comment Period.

BACKGROUND

The Company's application provides pension background information and an explanation of its accounting for pension costs and the pension settlement situation.[3] This memorandum will not repeat that information.

The Division's basic understanding of the Company's background and explanation is that during 2018, eligible pension participants took permissible lump sum cash distributions that, in aggregate, exceeded a defined threshold (service cost plus interest cost). Per Accounting Standards Codification (ASC) 715-30, the accounting standard that governs defined benefit pension plans, when this happens the Company recognizes in earnings a pro rata portion of the unrecognized actuarial gains or losses recorded in accumulated other comprehensive income rather than continuing to record such costs as a regulatory asset or liability for amortization over a period of years. The application states that the amortization period is 21 years.[4] It also states

[1] Company application, page 1 first paragraph, first sentence.
[2] Company application, page 1, first paragraph, last sentence.
[3] Company application, pages 3-9.
[4] Company application page 6, second paragraph, first sentence.

the total Company amount to be expensed in 2018 is approximately $21 million.[5] On a Utah allocated basis the amount is approximately $9 million.[6]

DISCUSSION

The Division appreciates the Company's efforts to explain the pension background, the pension funded status, pension costs, and pension events accounting and the impact of an event that triggered a requirement to expense. The Division found the explanation informative and helpful.

In the application the Company states, "Historically, the Company has requested approval from the Commission to apply Regulated GAAP upon the occurrence of pension events, which has allowed the company to remove the items from recognition in earnings and instead create either a regulatory asset or liability."[7] This statement has a footnote 2 that references two Dockets - Dockets No. 08-035-93 and Docket No. 14-035-147. Both of these Dockets were settled. Both settlements had general provisions and statements that basically indicated that the stipulations were an integrated whole through negotiation and compromise and that the stipulations were not precedential in future proceedings. Through settlement, the setting up of regulatory assets or liabilities in each Docket was done using negotiation and compromise by participating parties after specific consideration to the facts and situations of each request. Per stipulation, these settlements set no precedent for acceptance or denial of current or future requests for pension cost deferral. Thus the Division has evaluated this request and will evaluate each future requests for deferred accounting on a stand-alone or case by case basis.

The application does not persuade the Division that the proposed deferred accounting treatment is in the public interest. In essence, the application merely states that the deferral should be granted because it will stabilize costs. This is stated in various ways throughout the application. For example, the Company's application indicates, the deferral "will reduce interannual variability in pension cost for the remaining life of the Company's non-contributory defined

[5] Company application, page 2, second paragraph, and second sentence.
[6] This was computed by multiplying the $21 million by the SO allocation percentage of .434678 taken from tab 9 of the Company's June 2018 Results of Operations.
[7] Company application, page 7, last paragraph (ends on page 8).

benefit pension plans";[8] the deferral "would allow for recognition of relatively stable pension costs";[9] and the deferral "is designed to maintain normalized pension costs and credits and avoid exposing customers to potential cost volatility from single year 'pension events.'"[10]

As stated above, the Company's reason for filing the Application is to stabilize pension costs for customers. Customers have had stable pension costs for over four years to date[11] and if a rate case is not filed by the Company until sometime in 2020, the customers would continue with pension cost rate stability for five to six years. With this kind of rate stability, the Company's stated goal of pension stability is already being achieved and there is no need for the deferral. Turning to the impact upon shareholders, the Company incurs myriad fluctuating costs and expenses every year. It has sought to mitigate those effects for its shareholders. With its existing balancing accounts, much volatility for shareholders has already been reduced. While pension expense may have increased, the Company makes no corresponding filings when other items may bring significant benefit to shareholders. Recent instances of the Company earning more than its allowed return were not accompanied by applications to defer those effects for ratepayers' benefit. In short, there is no indication in the Company's application of why this expense should be treated differently than so many others with year-on-year changes.

One cannot determine from the application to what extent there will be future cost volatility or interannual variability. The filing talks about **potential** cost volatility (emphasis added).[12] Also included is, "Change in discount and interest rates **may** (emphasis added) result in more years with total annual settlement amounts that exceed the threshold for recognition of gains and losses."[13] These statements do not support the Company's stated reason for the deferred accounting. Such terms may point to variability but not volatility, particularly when that variability occurs because of previously known and applied accounting principles that merely

[8] Company application, page 2, last paragraph.
[9] Company application, page 9, second sentence before Section IV.
[10] Company application, page 9, last sentence under Section IV.
[11] Normalized pension costs were set by the last rate case under Docket No. 13-035-135 and were effective September 1, 2014.
[12] Company application, page 9, last sentence under Section IV.
[13] Company application, page 8, first paragraph under F section, last sentence.

have a different result for a given year. As explained later in this discussion, the Division does not support ordinary pension cost variability as a reason to approve this request for deferred accounting.

Much of the Company's filing is explanatory. The need for a deferred accounting order for stable pension costs has little to no support. No analysis is given supporting the application's concern with future interannual volatility or even variability in pension costs over the life of the pension using actuarial projections with assumptions. The computation of the approximate $21 million of expense was not presented.[14] After a review of the Company's response to the Office of Consumer Services' (OCS) data request 1.12, the Division believes the Company's use of the words "potential" or "may" for volatility and variability of pension costs is warranted. The projections provided by the Company in OCS data request 1.12 cover years 2019 to 2022, four future periods. The projection results seem to indicate that during this period it is more unlikely than likely that a settlement event will occur.

The Division recommends not approving the request for deferred accounting treatment of $21 million relating to the 2018 pension event.[15] The Division is wary of supporting isolated changes in cost recovery. If only a subset of cost categories are evaluated, other cost centers (which may be declining) are not examined, either individually or in aggregate. In a general rate case, both increasing and decreasing costs are considered, and only when the "net" impact over time points to the need for higher revenues should a rate increase be approved. The Division does not support "piecemeal" ratemaking. It was the Company's decision to set up employee compensation as it did. If the structure results in accelerated expense recognition per the pension rules in later years for people already retired or grandfathered in, that is the risk the Company undertook. The operation of the pension plan and its accounting through the years is well known

[14] The Office of Consumer Services (OCS) in Data Requests 1.1 to 1.26 requested certain detailed data on the pension for past and future years including a request for the current amount computation for the final 2018 settlement expense. The Company provided an amount of $22,066,883 (See Data Request 1.17(a)). Of the data provided, the Division paid most attention to Data Request 1.12. This specifically requested the Company provide projected future estimated settlement thresholds and estimated lump sum distributions for 2019 to 2022.

[15] As requested in the application the Company is not only asking deferred accounting for the 2018 pension event, but also for any subsequent similar pension events.

by the Company, as evidenced by explanations contained in this application. While the specifics of any given period's rates, returns, settlements, and payments are not known, and thus variable to some extent, the general construct of the plan is known to the Company and the variability of pension costs due to settlements and curtailments is ordinary and foreseeable (not unknown). This is another reason why the Division does not support this application.

The application requests this deferred accounting treatment for not only 2018 pension costs but also for all years until the plan expires. The Company's request would allow creation of yet another cost recovery mechanism to recover costs outside of a general rate case. While rate stability is one component of a public interest ratemaking regime, the underlying structure of ratemaking should not yield to it in this case, where the operation of the pension plan the Company established is proceeding as normal. The Division in the past has not supported such mechanisms and does not support the mechanism proposed by the Company through its deferred accounting proposal in this application.[16] Among other reasons, guaranteed cost recovery mechanisms shift normal business risk from the Company to rate-payers who do not have the ability to mitigate such risk. Furthermore, if selectively undertaken, such mechanisms create significant risk that rates will not reflect costs and will cease to be in the public interest. Ordinary pension costs (in this case settlements and curtailments) handled by normal pension provisions should be set for recovery only in the normal course of a general rate case where a proper matching of expenses and revenues can be obtained, and broader decisions about the normal level of pension expenses can be made with proper illumination by adversarial parties availing themselves of discovery and other fact-finding processes.

[16] The Division's reasons for nonsupport of specific cost recovery mechanisms even though given in the context of the Energy Balancing Account (EBA) can be applied generally to this applications mechanism. Thus, see such reasons as outlined in the conclusion section in a memorandum dated September 18, 2018 regarding the Division's comments to the sharing bands in the EBA, Docket No. 18-035-01 (As referenced by Docket No. 09-035-15). See also the Division's filed comments dated May 20, 2016 on its evaluation of the EBA, Docket No. 09-035-15.

CONCLUSION

The Company’s application should be rejected because its argument for smoothing pension cost volatility, the main reason for the request for deferred accounting, is not in the public interest. The application to some extent mentions the possibility, with minimal support, of rate variability. The Division does not support deferred accounting for the variability explained in the application, since it is normal, ordinary, and foreseeable (not unknown). Approval would support “piecemeal” ratemaking and would not consider both increasing and decreasing costs during the deferral periods. In totality, the deferred accounting requested is a cost recovery mechanism. The Division in the past has not supported the implementation of such mechanisms due to risk shifting to rate-payers and for other reasons.

Therefore, the Division recommends no approval for the requested deferred accounting order in the Company’s application in this Docket.

cc: Jana Saba, RMP
Michele Beck, OCS