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BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF THE APPLICATION OF IDAHO POWER COMPANY FOR AUTHORITY TO IMPLEMENT POWER COST ADJUSTMENT (PCA) RATES FOR ELECTRIC SERVICE FROM MAY 16, 2004 THROUGH MAY 31, 2005.	**CASE NO. IPC-E-04-9** **COMMENTS OF THE COMMISSION STAFF ON PROPOSED SETTLEMENT**

COMES NOW the Staff of the Idaho Public Utilities Commission, by and through its Attorney of record, Donald L. Howell, II, Deputy Attorney General, and files these comments in response to the Notice of Proposed Settlement, Notice of Modified Procedure and Notice of Comment and Protest Deadline issued in Order No. 29568 on August 18, 2004.

BACKGROUND

In Order No. 29506 issued on May 25, 2004, the Commission authorized Idaho Power Company to implement Power Cost Adjustment ("PCA") rates that included recovery of power supply expenses Idaho Power incurred when Valmy generation was unavailable during June 26 through September 9, 2003. The Valmy plant was shut down due to an erroneous energization of the Plant Unit No. 2 generator following scheduled maintenance. In that Order, the Commission directed Staff and Idaho Power to advise the Commission whether it should adjust the PCA in

2005 to credit customers for the recovery of the cost of the replacement power. On August 16, 2004, Idaho Power and Commission Staff (the "Parties") filed a Joint Motion for Acceptance of Settlement to resolve not only the Valmy 2 replacement power expense issue, but the expense adjustment rate for growth ("EARG") component of the Company's PCA calculation as well.[1] This comprehensive settlement also addresses regulatory accounting issues related to the Company's 2001 non-recurring income tax deduction created by its accounting method change for capitalized overhead costs.

The settlement formalized through the Parties' Stipulation is an integrated document that resolves the following outstanding issues, more specifically described below.

1) Valmy Unit No. 2 replacement power expenses. In Order No. 29506 issued in this case on May 25, 2004, the Commission authorized the Company to implement PCA rates that included the power supply expenses Idaho Power incurred to replace Valmy generation that was unavailable from June 26, 2003 through September 9, 2003. The Commission directed the Staff and Idaho Power to examine the cost of obtaining replacement power resulting from the outage and to advise the Commission whether an adjustment to next years' PCA would be appropriate, since the outage resulted from an inadvertent energization of the Valmy Plant Unit No. 2 generator.

2) Modification of the expense adjustment rate for growth (EARG) component of the Company's PCA calculation addressed by both Staff and the Company in Idaho Power's general rate case, Case No IPC-E-03-13. In Order No. 29505 issued in the case, at the request of both the Staff and Idaho Power, the Commission directed the parties to initiate a separate proceeding to address this component of the PCA calculations.

3) Regulatory accounting issues related to the Company's 2001 non-recurring income tax deduction created by its method change for capitalized overhead costs. Although not necessarily associated with any specific case, the issue of out-of-test year regulatory treatment of the non-recurring tax deduction has been the subject of continued discussion between Staff and Idaho Power.

[1] In Order No. 29505 issued in Case No. IPC-E-03-13, the Commission directed Idaho Power and Staff to initiate a separate proceeding to address the EARG component of the PCA calculation.

STAFF ANALYSIS

The Stipulation requires that Idaho Power provide a $19.3 million revenue credit to Idaho Power customers through the Company's PCA. This revenue credit will consist of a separate line item of $804,166 each month for 24 months for the period of June 2004 through May 2006 in the PCA true-up calculation. The credit will be in addition to any other credit provided through the PCA and will include interest from June 1, 2004 at the PCA carrying charge rate, which is currently (1) percent.

Resolution of these contested issues is a reasonable compromise of the parties' divergent claims and results in a comprehensive settlement amount of $19.3 million without specifically attributing a dollar amount to any single issue. Staff believes that resolution of these issues in one comprehensive settlement, as set forth in the stipulation and as more fully described below, is in the public interest and should be approved by the Commission.

Valmy Unit No. 2

In Order No. 29506, issued in Case No. IPC-E-04-9, the Commission stated with respect to the Valmy Unit No. 2 outage:

> ...we shall direct the Staff and the Company to informally examine this issue in greater detail. We encourage the parties to reach a settlement that is fair to both the Company and its ratepayers. If necessary, any adjustment in power cost recovery will be carried over to next years' PCA case.

After informal examination of the issue in greater detail and additional discussions with the Company, Staff believes resolution of the Valmy issue as part of this comprehensive settlement complies with the Commission order and is in the public interest. While the cause of the Valmy outage is not in dispute, several issues complicate any possible recovery from the responsible party, and mitigate the responsibility of Idaho Power. Those issues include the magnitude of the replacement power costs, the inability of Idaho Power to control the events, the uncertainty and difficulty of cost recovery from the operating utility (Sierra Pacific) and the nature of the PCA, which passes through the benefits of superior plant performance as well as the costs of poor plant performance. These considerations influenced Staff's decision to settle this issue as part of the Stipulation, which establishes a significant credit for customers through the PCA.

EARG

Modification of the EARG was originally addressed by the Company in prefiled direct testimony submitted as part of the Company's general rate case, Case No. IPC-E-03-13. The EARG's purpose is to subtract from actual power supply costs in a given year those power supply costs associated with customer growth beyond normalized levels established in the last general rate case. Company witness Said proposed that the PCA EARG be reduced from its current level of $16.84 per Megawatt hour (Mwh) to $7.30/Mwh to more appropriately reflect base PCA expenses embedded in customer rates. Staff witness Hessing countered in his rate case prefiled direct testimony that the EARG should be increased to $29.71/Mwh to reflect the average annual marginal cost of energy. No other party to the case addressed this issue.

Both parties agreed that given the large discrepancy between the two positions, modification of the EARG would be best addressed outside the general rate case. The Commission agreed stating in Order No. 29505:

> ...The Commission at hearing granted Staff's motion for a separate proceeding to address Expense Adjustment Rate for Growth component of the PCA formula.

The Commission also indicated that the proceeding could be handled in a workshop setting without formal hearing. Although structured workshops were not actually held on the EARG issue, a notice of settlement discussions was transmitted and discussions were held with interested parties.

The EARG level of $16.84 agreed to by Staff and Idaho Power as part of this stipulation continues the EARG adjustment originally approved by the Commission when the Idaho Power PCA was first established. In fact, absent approval of the stipulation and pending further proceedings on this issue, it is likely that the existing EARG would remain in place anyway. Consequently, Staff believes that including the EARG in the comprehensive settlement at the $16.84/Mwh level is consistent with Commission Orders, is roughly half way between the proposals of the parties and assisted in compromise between the parties on the other issues resolved in the Stipulation. Moreover, the settlement on EARG modification is essentially for an interim period until the next general rate case that is anticipated to be filed within two years. Both Staff and the Company believe that EARG modification can be more properly identified and included upfront as an issue in that case. Staff believes that including resolution of the EARG modification issue in the Stipulation is appropriate and that maintaining the existing EARG level until the next Idaho Power general rate case is reasonable.

Regulatory Tax Accounting

The issue associated with the 2001 non-recurring income tax deduction, created by the accounting method change for capitalized overheads, addresses the manner in which the Company for regulatory purposes, accounted for the 2002 out-of-test year income tax refund. The Company maintained that many expenses, including income taxes, fluctuate from year-to-year outside of rate case test years and thus are not necessarily recaptured for regulatory purposes. Staff maintained, in fairness to ratepayers, the one-time reduction in income taxes that occurred in 2001, that will reverse in the future, was an extraordinary event subject to special consideration.

The dispute between the parties includes multiple regulatory accounting concerns associated with the dollar amount and regulatory accounting treatment. By including this issue as part of a comprehensive settlement, the parties can resolve these contentious issues without fully determining the magnitude of any expense reduction or the merits of an out-of-test year regulatory adjustment. Staff believes that both parties reasonably compromised on the 2001 non-recurring income tax deduction issue, created by the accounting method change for capitalized overheads, and it is reasonably reflected in the comprehensive settlement.

CONCLUSION

The issues described above and included as part of the comprehensive settlement are highly technical and complicated, involving difficult accounting, tax reporting and third-party subrogation issues. In addition, Staff and Idaho Power have taken widely different positions on how these issues should be individually resolved. The potential for costly, time consuming formal proceedings, and the risk to each party of unfavorable resolution on each issue, is high for both parties. In Staff's view, the settlement and proposed stipulation serves the best interest of Idaho Power ratepayers.

The proposal represents thoughtful compromise of cost responsibility for the Valmy Unit No. 2 outage, maintains the EARG at current levels until the next rate case and secures ratepayer benefits associated with reduced Company expenses in 2001. The overall resulting customer credit of $19.3 million passed through the PCA aids in rate stability over the next two years and removes the uncertainty created by continued and lengthy litigation. Staff fully supports the comprehensive settlement and recommends that the Commission approve the Stipulation as filed.

Respectfully submitted this 1st day of September 2004.

for

Donald L. Howell, II
Deputy Attorney General

Technical Staff: Randy Lobb

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY THAT I HAVE THIS 1st DAY OF SEPTEMBER 2004, SERVED THE FOREGOING **COMMENTS OF THE COMMISSION STAFF ON PROPOSED SETTLEMENT,** IN CASE NO. IPC-E-04-09, BY MAILING A COPY THEREOF, POSTAGE PREPAID, TO THE FOLLOWING:

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