

BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

**IN THE MATTER OF THE APPLICATION)
OF IDAHO POWER COMPANY FOR) CASE NO. IPC-E-05-14
AUTHORITY TO INCREASE ITS RATES)
AND CHARGES FOR ELECTRIC SERVICE)
TO TAKE INTO ACCOUNT INCOME) ORDER NO. 29789
TAXES IN COMPLIANCE WITH ORDER)
NO. 29601)**

On April 13, 2005, Idaho Power Company filed an Application with the Commission requesting approval of changes to base rate schedules in response to a Commission Order issued in Case No. IPC-E-03-13, the Company's last general rate case. Following the Commission's grant of Petitions for Reconsideration in that prior case, the Commission issued Order No. 29601 approving a Stipulation resolving calculation of the Company's income tax expense for ratemaking purposes in that case. In the present Application, Idaho Power asserts that its Application is a compliance filing in accordance with Order No. 29601, requiring only a Commission Order for the proposed rates to become effective June 1, 2005.

BACKGROUND

The Commission issued final Order No. 29505 on May 25, 2004, concluding Idaho Power's rate increase request. Among the many contested issues determined by the Commission in that Order was the calculation of income tax expense that would be allowed. The Commission directed the Company to calculate its income tax expense using a five-year average of historic income tax payments. The Company had proposed to use existing statutory tax rates. Use of the average tax expense reduced Idaho Power's annual revenue requirement by \$11,505,677.

Idaho Power filed a Petition for Reconsideration challenging the Commission's determination to use an average tax rate rather than the statutory tax rates. On reconsideration the Company argued that use of an average tax year could violate normalization requirements of the Internal Revenue Code. The Company offered to present new evidence on the normalization issue. Because of the significance of the income tax adjustment made by the Commission in Order No. 29505, the Commission granted reconsideration on the issue and provided the parties an opportunity to present new evidence. Order No. 29547. Thereafter, the Company and Staff began discussing possible settlement of the tax rate issue, and eventually submitted a Stipulation

to the Commission to resolve the tax expense calculation. The Commission reviewed the Stipulation and approved it in Order No. 29601.

ORDER NO. 29601

The terms of the Stipulation were set forth and reviewed by the Commission in Order No. 29601. For the period June 1, 2004 through May 31, 2005, Idaho Power would compute and record monthly in a regulatory asset account an amount equal to the additional revenue the Company would have received through its energy rates if its revenue requirement had been determined using the statutory income tax rates rather than the five-year historic average rates. In addition, the Stipulation provided that the Company would include \$11,504,677 in its base rates after June 1, 2005. The Company would not, however, seek to recover in its revenue requirement any deficiency assessed by the Internal Revenue Service related to a one-time adjustment associated with capitalized overhead cost tax method change for the years 1987 through 2000.

The Commission noted Idaho Power's argument that use of the proxy tax rate violates principles against retroactive ratemaking and that violation of the IRS's normalization requirements could result in serious consequences to the Company. The Commission expressed concern about the uncertainty created by a resulting IRS challenge and the risks that litigation could pose to ratepayers. The settlement ensured that ratepayers will benefit from accumulated depreciation and pay no tax deficiency assessment for the one-time capitalized overhead tax method change for the years 1987 through 2000. The Commission also noted that avoiding protracted litigation likely resulting from use of the historic tax rate would lower the cost ratepayers will ultimately pay for Idaho Power to borrow money to finance ongoing operations. The Commission also noted that all parties in the rate case either signed the Stipulation or did not actively oppose it.

The Stipulation approved in Order No. 29601 contains three primary components related to the tax rate issue. First, Idaho Power's annual revenue requirement would increase by the amount it had been reduced by use of the average tax rate, but the Company would not immediately include the increase in rates. Instead, for the period June 2004 through May 2005, the Company would record each month in a regulatory asset account the revenue the Company would have received had the statutory tax rates been used. Second, the regulatory asset would then be recovered in rates during June 2005 through May 2006, requiring a one-year temporary

adjustment in rates. Finally, Idaho Power's base rates would be adjusted on June 1, 2005 to recover the \$11,504,677 difference in revenue requirement resulting from application of the statutory tax rates.

DISCUSSION

There was no dispute in Case No. IPC-E-03-13 that Idaho Power's income tax expense is a usual business expense to be included in the Company's revenue requirement. The Company simply would not have an opportunity to earn its authorized return if its unavoidable tax obligations were excluded from rates. The Commission's objective, when evaluating a utility's tax expense in a test year, is to ensure that the tax expense included for recovery is not larger than necessary to pay actual tax amounts. Thus, the Commission initially accepted Staff's recommended five-year average as a reasonable predictor of the Company's tax liability in the future. As the Stipulation and Order No. 29601 demonstrate, however, using the particular historical average for Idaho Power presented significant risk of litigation and adverse consequences. The Commission accordingly approved settlement of the tax issue as a reasonable determinate of the Company's actual tax costs in that case, while providing significant benefit to ratepayers.

Staff reviewed the Company's Application to ensure it complies with Order No. 29106. Exhibit 3 of the Company's Application shows the calculation of the regulatory asset. The \$11,638,229 regulatory asset Idaho Power has accrued at a rate of \$.92209 per MWh includes interest at one percent. Because April and May 2005 are projections, Idaho Power proposes to true up the actual recovery and accrual of the regulatory asset that would be reflected in the Power Cost Adjustment (PCA) next year (June 2006).

To recover the regulatory asset of \$11,638,229, Idaho Power proposed a rate based upon the projected Idaho jurisdictional sales of 12,453,880 MWh. The Company allocated the income tax expenses to customer classes and special contract customers based on revenues associated with each class/customer, resulting in a uniform increase of 2.20% over base rates. This temporary one-year base rate increase will expire on May 31, 2006. To recover the base rate change of \$11,504,667 on a going-forward basis, the Company proposed to apply a uniform increase of 2.25% to each customer class and special contract customer with a uniform percentage increase to the demand and energy billing components.

The Commission finds that Idaho Power's filing complies with the Commission's decision and directive in Order No. 29601. The Commission therefore approves the Application with regard to the amount of the regulatory asset subject to recovery. We will not approve specific rate spread or rate design in this case, however, because the Commission is also considering other cases affecting the Company's base and PCA rates. The filing in this case and in Case Nos. IPC-E-05-10 (Bennett Mountain) and IPC-E-05-15 (the 2005 PCA) shall be consolidated into new rates effective June 1, 2005. After reviewing the record in the other cases, the Commission will approve new rates in Case No. IPC-E-05-15, taking into account the base rate increase authorized in this case.


ORDER

IT IS HEREBY ORDERED that the filing made by Idaho Power Company complies with the Commission's previous Order No. 29601 and is therefore approved. The Commission will approve new rates in Case No. IPC-E-05-15 effective June 1, 2005.

IT IS FURTHER ORDERED that the temporary one-year base rate increase shall expire on May 31, 2006.

THIS IS A FINAL ORDER. Any person interested in this Order may petition for reconsideration within twenty-one (21) days of the service date of this Order. Within seven (7) days after any person has petitioned for reconsideration, any other person may cross-petition for reconsideration. See *Idaho Code* § 61-626.

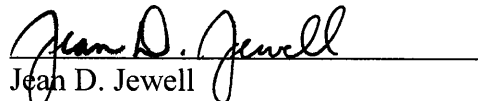
DONE by Order of the Idaho Public Utilities Commission at Boise, Idaho this 25th
day of May 2005.


PAUL KJELLANDER, PRESIDENT


MARSHA H. SMITH, COMMISSIONER


DENNIS S. HANSEN, COMMISSIONER

ATTEST:


Jean D. Jewell
Commission Secretary

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