

ITEM NO. CA5

**PUBLIC UTILITY COMMISSION OF OREGON
STAFF REPORT
PUBLIC MEETING DATE: April 15, 2003**

REGULAR _____ CONSENT X EFFECTIVE DATE April 1, 2003

DATE: April 9, 2003

TO: John Savage through Lee Sparling and Ed Busch

FROM: Ed Krantz

SUBJECT: PACIFICORP: (Docket No. UM 1073) Requests accounting order authorizing recording of a regulatory asset relating to pension liability.

STAFF RECOMMENDATION:

I recommend that the Commission approve PacifiCorp's application authorizing the company to record and maintain a regulatory asset resulting from the requirement to recognize an Additional Minimum Pension Liability under FAS 87. Approval is for accounting purposes only and does not constitute authorization of any future ratemaking treatment of the costs associated with the regulatory asset.

DISCUSSION:

On February 21, 2003, PacifiCorp (Pacific or company) filed an application that was docketed UM 1073. In this filing, the company requests an accounting order authorizing the company to record on an ongoing basis, as a regulatory asset, an amount equal to the pretax charge against equity that would otherwise be necessitated by the recognition of the company's Additional Minimum Liability under Financial Accounting Standards (FAS) 87, relating to pension liability. This application was filed pursuant to ORS 757.120 and 757.125.

The following factors have contributed to PacifiCorp's current underfunded pension status: 1) Declining equity markets over the past three years have led to a decline in the value of the assets held in trust to meet pension obligations; and, 2) the present value of future benefit obligations to employees have increased as interest rates have declined.

In accordance with FAS 87, an Additional Minimum Pension Liability must be recognized if the Accumulated Benefit Obligation (ABO) for an employer's pension plan exceeds the fair value of plan assets by more than the amount currently recorded as the pension fund liability. The ABO is the present value of the plan's accrued benefits, without pay projections, using the discount rate chosen for the fiscal year-end. If the assets are less

than the ABO the company must show a liability on the balance sheet equal to the unfunded ABO. The amount currently recorded as the pension liability (Unfunded Accrued Pension Cost Liability) is the cumulative amount by which each year's net periodic cost, as determined under FAS 87, has exceeded the cumulative amount of contributions to the pension plan. The company anticipates that the ABO, as of March 31, 2003, will exceed the fair value of plan assets by more than \$300 million, whereas the recorded Unfunded Accrued Pension Cost Liability will be approximately \$65 million. The difference is the Additional Minimum Pension Liability (Regulatory Asset).

PacifiCorp expects the amount of net-periodic pension cost, under FAS 87, to increase as a result of lower interest rates which increases the present value of future benefit obligations. When the equity markets and interest rates increase, net-periodic pension cost will begin to decrease.

If the company is not allowed to create and maintain a Regulatory Asset as required by FAS 87, PacifiCorp will be obligated to record, for its fiscal year ending March 31, 2003, a \$200-\$240 million pretax charge to Accumulated Other Comprehensive Income less about \$75-\$95 million in deferred income taxes. Although this charge to equity is expected to be reversed in future periods, the charge will have the immediate effect of reducing PacifiCorp's common equity capitalization. The company claims this could have negative implications on the company's ratings and possibly increase its cost of capital.

Staff does not necessarily agree that the company's cost of capital may increase without approval of the Regulatory Asset; however, Staff agrees that allowing the company to create and maintain the Regulatory Asset is the most reasonable approach in meeting FAS 87 requirements.

PacifiCorp also requests confirmation by the Commission that actuarially determined FAS 87 pension costs are presently recoverable in rates. Staff agrees that actuarially determined FAS pension costs are generally recoverable in rates as has been the case in past rate cases, but any Commission ruling should be made in a general rate proceeding.

Staff and PacifiCorp both acknowledge that there should be no rate change, now or in the future, associated with the requested regulatory asset.

PROPOSED COMMISSION MOTION:

PacifiCorp's application to create and maintain a Regulatory Asset resulting from the requirement to recognize an Additional Minimum Pension Liability under FAS 87 be approved. This approval is for accounting purposes only and does not constitute authorization of any future ratemaking treatment of the costs associated with the regulatory asset.