

Service Date: June 18, 1998

DEPARTMENT OF PUBLIC SERVICE REGULATION
BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MONTANA

* * * * *

IN THE MATTER of the Application of)	UTILITY DIVISION
PACIFICORP for Approval of its Electric)	
Utility Restructuring Transition Plan Filed)	DOCKET NO. D97.7.91
Pursuant to Senate Bill 390)	ORDER NO. 5987e

ORDER IMPLEMENTING LARGE CUSTOMER CHOICE ON JULY 1, 1998

APPEARANCES

FOR THE APPLICANT:

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Suite 2300, Portland, Oregon 97204-1268.

FOR THE INTERVENORS:

Robert A. Nelson, Montana Consumer Counsel, 616 Helena Avenue, P.O. Box 201703,
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Donald W. Quander, Holland & Hart LLP, 401 North 31st Street, Suite 1500, Billings,
Montana 59103-0639, representing Plum Creek Timber Company.

James M. Madden, Special Assistant Attorney General, Dept. of Environmental Quality,
Metcalf Building, P.O. Box 200901, Helena, Montana 59620-0901.

BEFORE:

DAVE FISHER, Chairman
NANCY McCaffree, Vice Chair
BOB ANDERSON, Commissioner
DANNY OBERG, Commissioner
BOB ROWE, Commissioner

COMMISSION STAFF:

Denise Peterson, Staff Attorney; Eric Eck, Chief, Revenue Requirements Bureau;
Will Rosquist, Staff Economist; and G. Joel Tierney, Utilities Engineer;
1701 Prospect Avenue, P.O. Box 202601, Helena, Montana 59620-2601.

Background

1. On June 24, 1997, pursuant to Senate Bill 390, now codified at §§ 69-8-101 through -503, Montana Code Annotated (MCA), the Montana Public Service Commission (Commission) issued Procedural Order No. 5987 in Docket No. D97.7.91. The Commission directed PacifiCorp to file its transition plan, as required by the Act, by July 1, 1997. The Commission set forth a procedural schedule with a hearing date of March 24, 1998 and a Final Order to be issued June 1, 1998, in order to implement customer choice by July 1, 1998.

2. On July 1, 1997, PacifiCorp filed its Electric Restructuring Transition Plan with the Commission. PacifiCorp filed a Motion for Protective Order on August 7, 1997, and the Commission issued its Protective Order (No. 5987a) on August 14, 1997.

3. The Commission issued a Notice of Transition Plan Filing and Intervention Deadline on July 10, 1997. Numerous parties intervened in the Docket and are cited as Intervenor in the Service List attached and incorporated into this Order. Individual participation will be noted where applicable in this Order.

4. The Commission issued its Preliminary Determination and Order on Transition Plan on September 22, 1997 (Order No. 5987b). The Commission directed PacifiCorp to file a revised plan remedying specific deficiencies. The Commission determined that PacifiCorp's transition plan was incomplete and inadequate with respect to (1) demonstration of transition costs; (2) functional separation of rate base and expense items related to electricity supply, retail transmission and distribution and regulated and unregulated retail energy services; and (3) proposed pilot programs. PacifiCorp filed its Revised Plan on October 13, 1997.

5. On February 17, 1998, PacifiCorp filed Objections to Data Responses, Motion to Compel, and Motion to Amend Procedural Schedule, stating that there were problems with responses to PacifiCorp data requests from the witness for Montana Consumer Counsel (MCC), consultant Richard S. Albert, Lotus Consulting Group (LCG), particularly those of on market clearing prices of generation in a competitive market. PacifiCorp requested an Order compelling Mr. Albert to respond and moved to amend the Procedural Schedule to allow PacifiCorp two weeks after receipt of responses to file Rebuttal Testimony, moving all subsequent procedural deadlines.

6. On February 24, 1998, PacifiCorp filed Rebuttal Testimony.

7. PacifiCorp amended its Objections to Data Responses, Motion to Compel and Motion to Amend Procedural Schedule and Submission of Alternative Motion to Strike on March 2, 1998. PacifiCorp stated that it was able to obtain sufficient data to file Rebuttal Testimony on aspects of LCG's model. However, PacifiCorp maintained it had not had an opportunity to acquire sufficient information to "fully" understand how the LCG "Network Power Model" functions because LCG did not appropriately respond to PacifiCorp data requests.

8. MCC responded to PacifiCorp's Motions on March 4, 1998, maintaining that PacifiCorp's rebuttal testimony indicated that PacifiCorp's witnesses had obtained "a significant amount of information." Asserting its continuing cooperation on discovery matters, MCC said that it believed that its supplemental responses had provided the information. MCC maintained that the Motion to Strike was premature.

9. On March 5, 1998, at a duly noticed work session the Commission denied PacifiCorp's motion to strike. On the motion to compel answers to discovery, the Commission directed Staff to continue to work with the parties on discovery concerns.

10. MCC filed a motion on March 9, 1998, to amend the procedural schedule to allow intervenors the opportunity to submit additional intervenor testimony, noting that (1) PacifiCorp's 22-page initial filing on July 1, 1997 was deemed deficient by the Commission; (2) PacifiCorp's Revised Transition Plan filing on October 15, 1997, was still scant; (3) MCC's intervenor testimony was filed January 16, 1998, with independent market price study and forecast for estimating stranded costs; and (4) PacifiCorp's Rebuttal Testimony was filed February 24, 1998, significantly more substantial than the revised, with new issues.

11. MCC maintained that PacifiCorp's Rebuttal Testimony was actually response testimony to which MCC's witnesses should have an opportunity to reply. To develop a full record on issues of first impression and allow parties to address expanded issues and to rebut what is essentially response testimony, MCC requested the opportunity to file "surrebuttal" testimony. MCC proposed that the Commission postpone the hearing scheduled March 24, 1998, and convene a scheduling conference to set a May hearing date, with the possibility of an interim open access tariff by July 1, 1998.

12. PacifiCorp replied that MCC's motion was not specific enough to support the relief requested, including what issues are "new" and what issues merit revising the procedural schedule. PacifiCorp maintained that its February 24 testimony was properly rebuttal to Intervenor's prefiled testimony and that PacifiCorp offered nothing "new" in criticizing the model of MCC's witness. PacifiCorp stated that it had provided full opportunity for discovery on its rebuttal, including an on-site visit March 12. PacifiCorp expressed the concern that large customers must have access on July 1, 1998, and desired a final order before that date.

13. The Department of Environmental Quality and the Northwest Power Planning Council (DEQ/NPPC) opposed the motion to reschedule the hearing, believing that the delay could impair the ability to meet the statutory deadline for large customer choice by July 1, 1998, and all other customers by July 1, 2002 under the Act. According to DEQ, PacifiCorp was responsible for any delay caused by rescheduling, because its plan failed to provide sufficient information to comply with the Act. DEQ indicated that the remedy would be to go to hearing

on March 24, 1998 and let PacifiCorp suffer the consequences in a possible modification of its transition plan to comply with the Act.

14. Plum Creek Timber Company (Plum Creek) responded, agreeing with MCC, that PacifiCorp's "rebuttal" testimony expanded, rather than narrowed, the scope of issues. PacifiCorp introduced new information, claims and elements which it should have included in its principal case, including: (1) proposed inclusion of "Montana Border Customers" and strip mines in stranded costs; (2) a new market price credit proposal; (3) a series of new tariff schedules; (4) and an "extraordinary 14-page proposed 'Rule 18,' purporting to establish extensive requirements for Customer Choice Direct Access."

15. Plum Creek joined in MCC's request that intervenors be allowed to provide "surrebuttal" testimony. While striking PacifiCorp's new material would be an appropriate option, Plum Creek maintained this remedy would limit rather than enhance the record; the ensuing legal dispute would further delay proceedings. Plum Creek maintained that intervenors are entitled to respond to PacifiCorp and that the Commission is entitled to a comprehensive record. Cross-examination alone would not suffice, where there is new information and claims. While this surrebuttal could be provided live at the hearing on March 24, additional discovery and pre-filed surrebuttal testimony would produce a more comprehensive record.

16. Plum Creek recognized the "dilemma" in that an unbundled tariff for large customers is required by July 1, 1998, and a utility cannot recover a competitive transition charge until the Commission makes a determination based on an affirmative showing of stranded costs. If the Commission extended the hearing schedule, Plum Creek proposed adoption of a limited interim tariff exclusive of transition charges, subject to a simple accounting order pending the final determination of stranded costs.

17. At its work session on March 11, 1998, the Commission granted MCC's motion, vacating the hearing date scheduled to begin on March 24, 1998, in Kalispell, Montana and allowing intervenors the opportunity to file surrebuttal testimony to the Rebuttal Testimony filed by PacifiCorp on February 24, 1998. The Commission directed Commission Staff to set a scheduling conference with the parties which would establish a procedural order with the following requirements: (1) an opportunity for intervenors to file testimony in rebuttal to the testimony filed by PacifiCorp on February 24, 1998, and any necessary corresponding discovery; (2) a deadline for parties to provide an interim tariff for PacifiCorp's July 1, 1998, statutory requirement to provide choice to qualifying large customers and a proposed accounting order, for the Commission's approval; (3) an alternative date for a one-day hearing in May 1998 in Helena, Montana for the sole issue of choice for the five qualifying large customers entitled to choice on July 1, 1998, if parties have not presented and received Commission approval of an interim tariff and accounting order; (4) a hearing date on all issues, including but not limited to transition

costs, customer choice and pilot programs, preferably in July or August; and (5) a final order on all issues in September, 1998. The Commission suspended the Procedural Schedule in Order No. 5987, to be rescheduled in a procedural conference.

18. Commission Staff, PacifiCorp, MCC, Plum Creek and DEQ convened a telephonic procedural conference on March 26, 1998, and developed a procedural schedule. A hearing was set for May 19 and 20, 1998, in Helena, Montana on the issues related to customers entitled to choice on July 1, 1998. A full hearing on all issues was scheduled to begin on July 20, 1998, in Kalispell, Montana. At this procedural conference, PacifiCorp outlined its soon-to-be filed motions for reconsideration of the Commission's action or alternatively, for permission to submit the last round of testimony. Intervenors agreed to submit responses to the motions by 5:00 p.m., Monday, March 30, 1998.

19. PacifiCorp filed a Motion for Reconsideration on March 26, 1998. PacifiCorp first requested that the Commission reconsider its action on March 11, 1998, in which the Commission granted MCC's motion to vacate the hearing date of March 24, 1998, and allow Intervenors the opportunity to file testimony in rebuttal to testimony filed by PacifiCorp on February 24, 1998.

20. PacifiCorp asked for clarification on the scope of intervenor surrebuttal testimony, whether limited to "new" issues raised or all issues raised in PacifiCorp's testimony. Allowing Intervenors to respond on all issues would restart the process and broaden the scope of discovery, PacifiCorp maintained. PacifiCorp also questioned the scope of the surrebuttal testimony afforded MCC to respond to PacifiCorp testimony, maintaining that it should be limited to the Lotus Consulting Group (LCG) model, i.e., witnesses Moriss and Costa (and "new" issues). Finally, PacifiCorp asked the Commission to set forth the basis of its findings on its action, as part of its Motion for Reconsideration.

21. Assuming that the Commission might reject the Motion for Reconsideration, PacifiCorp amended its motion on March 27, 1998, to request an alternative order "that allows the party with the burden of proof in this contested case" (PacifiCorp) to file the last round of testimony.

22. In response to PacifiCorp's Motions, MCC recommended denying the motion to reconsider the action of March 11. MCC did not oppose the separate Amended Motion, which would allow PacifiCorp to file the last round of testimony. Plum Creek responded that rather than requesting clarification, PacifiCorp in reality wanted to limit parties and staff to a narrow discovery. PacifiCorp had greatly expanded its filing in response to Intervenors and should not complain about their having an opportunity to respond. PacifiCorp had cited no authority that it was denied due process by not being allowed to file "sur-surrebuttal" (Alternative Motion). Plum Creek believed that PacifiCorp's three rounds of testimony, plus supplemental testimony on

MCC's model, was an adequate opportunity to have its say. Plum Creek requested that the Commission deny PacifiCorp's motions, affirm its March 11 action, and adopt the new procedural schedule.

23. At its work session on March 31, 1998, the Commission denied the Motion for Reconsideration of its actions on March 11, 1998, and granted the motion for permission to file the last round of testimony in response to Intervenors Rebuttal. To accommodate the filing of this last round and additional discovery, the Commission granted PacifiCorp's request to postpone the hearing tentatively scheduled for July 20, 1998, on all issues other than those to be considered in the May 19-20, 1998, hearing on large customers entitled to choice by July 1, 1998. The Commission directed its staff to work with parties to develop the final procedural schedule with a hearing date of August 25, 1998, in Kalispell, Montana on all issues.

24. In Order No. 5987d, the Commission determined that delaying the hearing to July or August to allow the intervenors to conclude discovery and prefile surrebuttal would facilitate a full and complete record. Because the large customers in PacifiCorp's service territory are entitled to choice on July 1, 1998, the Commission directed Staff to set a hearing in May, 1998, to lead to an interim tariff for those customers, and an accounting mechanism, pending the final hearing.

25. The Commission conducted the public hearing on the issue of large customer choice on May 19, 1998, at the Commission offices, Bollinger Hearing Room, 1701 Prospect Avenue, Helena, Montana. Active participants were PacifiCorp, with witnesses Bruce Hellebuyck, David L. Taylor and Connie Colter; and Plum Creek Timber Company, with witness Dr. Alan Rosenberg. Counsel for PacifiCorp informed the Commission that there are now seven large customers entitled to choice on July 1, 1998, with the addition of two Wyoming/Montana border customers.

26. At the request and consent of the parties at the hearing on May 19, 1998, Commission Staff moved all the prefiled testimony and data responses into the record for this proceeding and the subsequent hearing on all the issues to be conducted in August, 1998. The scope of cross-examination and use of the testimony, prefiled exhibits and discovery was limited to the issue of large customer choice and pertinent issues. DEQ's witness John Goroski was unable to testify. PacifiCorp waived cross-examination of Mr. Goroski and agreed to submission of his testimony for purposes of this proceeding. Conversely, DEQ waived cross-examination of PacifiCorp's witnesses in this proceeding. The Commission denied PacifiCorp's motion to present rebuttal testimony of Mr. Taylor to the testimony of Dr. Rosenberg filed May 12, 1998.

Findings and Discussion

27. To prepare for large customer choice in PacifiCorp's Montana service territory on July 1, 1998, the Commission must do two things: (1) address the need for an accounting order

that will track any costs which PacifiCorp may later be able to collect as stranded costs; and (2) decide on an unbundled rate structure to be incorporated in new tariffs.

Tracking Interim Transition Costs

28. Certain customers of PacifiCorp will have choice on July 1, 1998, pursuant to Senate Bill 390. Because the Commission will not have determined transition costs or benefits by that time, the Commission finds that PacifiCorp may track the amount of transition costs or benefits which would have been paid or received by customers who exercise choice after June 30, 1998. The Commission determines that the interim period constitutes the period commencing July 1, 1998, and terminating with the Commission's Final Order determining non-mitigable, net transition costs or benefits in this Docket.

29. The first element necessary to track is the amount of energy used by customers who exercise choice during the interim transition period. PacifiCorp proposed that the customer's monthly kilowatt-hour usage times the current rates be credited to the Transition Cost Revenue Account. This amount equals the generation component of revenues that the customer would have paid PacifiCorp if it had continued to purchase power from PacifiCorp. The Commission authorizes PacifiCorp to create two Memorandum Accounts, the Transition Cost Revenue Account and the Transition Cost Accounts Receivable Account.

30. The next amount to track is the amount of revenue received by PacifiCorp for the sale of the power released by the customers who have choice. The kilowatt-hours used by the customers exercising choice will be multiplied by average sales price received for the power in that month. PacifiCorp proposed using the Dow Jones Mid-Columbia Price Index as shown in the Company's proposed Schedule 700. The Commission authorizes PacifiCorp to make a debit entry for this power, but does not approve the use of the Dow Jones Mid-Columbia Price Index. PacifiCorp has the burden of proof to show that the sale of power each month has achieved the highest possible price to fully mitigate stranded costs. Sales to new customers on PacifiCorp's system, or new incremental sales to existing customers are examples of sales that would produce revenues greater than the Dow Jones Mid-Columbia Price Index.

31. The Commission authorizes PacifiCorp to make an entry to the Transition Cost Revenue Account to reflect the carrying charges on the monthly average balance in the Transition Cost Revenue Account. Plum Creek Timber recommended setting the interest rate at 6 percent per annum. PacifiCorp recommended an interest rate of 9.13 percent per annum. The Commission finds that an interest rate of 6 percent per annum is appropriate for the interim transition period, as a better proxy for the rate at which transition bonds may be issued.

32. Approval of the tracking of interim transition costs or benefits is for accounting purposes only. This Order is not to be construed as, nor is it in any way, a directive as to the proper accounting treatment for stranded costs or benefits, or an approval of either the actual

numbers involved, the accounting method used, or the assumptions underlying those numbers. Most importantly, this Order does not imply or direct in any fashion that stranded costs or benefits deferred pursuant to this Order will be at any time reflected in rates.

Decision on Tracking Mechanism

33. The Commission authorizes a mechanism for tracking transition costs/benefits for those customers electing choice after June 30, 1998, as outlined in ¶¶ 28-32, *infra.*, for accounting purposes only.

Scope of Unbundling

34. As a threshold issue, the Commission must decide whether to unbundle the currently tariffed rates for the seven customers with choice on July 1, or unbundle the tariffs for all customer classes. The Notice of Public Hearing did not state that the Commission would consider unbundling rates for smaller customer classes. MCC (representing small customers) did not submit supplemental testimony prior to the hearing and was not active at the hearing. Plum Creek Timber's Dr. Rosenberg advocated unbundling all customer class rates on July 1, 1998 (May 1998 Supplemental Testimony, p. 4, January 1998 Prefiled Direct Testimony, p. 37).

35. PacifiCorp's position on unbundling was not explicit. At the hearing, Mr. Hellebuyck testified that PacifiCorp had already filed all proposed tariffs separating charges into generation, transmission and distribution functions. Tr. p. 57. However, Mr. Hellebuyck also testified that by July 1, 1998, PacifiCorp will provide unbundled bills to the seven customers who have choice, but it had not planned to unbundle other customers' bills July 1, 1998, as part of the education process. Tr. p. 52. PacifiCorp's witness Taylor testified that if the interim order in this proceeding sets forth functionalized prices for all classes, PacifiCorp could put those tariffs in the tariff book. Tr. p. 100. PacifiCorp's position appears to be that the Commission could implement unbundled tariffs for all customer classes on July 1, 1998, but that such information should not be provided to consumers through the education process until after a final order is issued.

36. A policy question is whether any unbundling method the Commission determines appropriate for large customers should also be applied to other customer classes. The record thus far does not envision applying different methods to various customer classes; PacifiCorp and Plum Creek each apply their preferred methods to all customer classes. Consumer Counsel has not presented any testimony on how to properly unbundle residential class revenues, but may do so in intervenor testimony scheduled for June 19, 1998.

37. If the Commission unbundles rates now for large customers only, the next question is whether the Commission intends to examine that method further in the next hearing. A Commission decision after the proceeding in August, 1998, to use a different method to unbundle the rates of other customers could lead to a corresponding question about whether the

method to unbundle large customer rates was appropriate in the first place. However, large customers would face further uncertainty if, in addition to the unknown Competitive Transition Charges (CTCs), their unbundled rates on July 1, 1998, could change following the Commission's August hearing.

Decision on Unbundled Tariffs

38. At this time, the Commission will require unbundled tariffs only for the seven large customers with choice. Unbundled bill information is important in educating small customers about supply choice, but residential and small commercial customers do not require this information on July 1, 1998. If bills for small customers were not unbundled until December, 1998, there would still be six months during which customers would get unbundled bills before going to choice, under PacifiCorp's proposal. Waiting to unbundle tariffs for other customers also gives MCC an opportunity to submit testimony on a proper method.

39. The Commission determines that, upon approving an unbundled rate design for the large customers, there should be no shifting of revenue requirements among the functions as a result of the August hearing, other than any CTC-related revenues.

Unbundling Options

40. The record to date consists of four viable options for unbundling rates out of the six presented. Each option differs in how the total revenue requirement of a customer class is divided among the three functions: Production, Transmission and Distribution. The following discussion pertains to unbundling of the large customer tariffs only.

41. The primary source of contention between PacifiCorp and Plum Creek with respect to unbundling has to do with what was referred to at the hearing as the "subsidy" or the "residual." "Subsidy" is incorrectly used in this context as it is an economic concept, while the issue at hand relates to embedded costs. Tr. p. 105. The residual is the difference between the revenues produced by currently-tariffed rates and the revenues allocated to a particular customer class under the allocated cost-of-service study filed by PacifiCorp. For some customer classes, the revenues produced by current rates exceed what is allocated to them by the cost study, while for other customer classes current rates produce less revenue. The current rates for the Large General Service customer class produce more revenue than what is allocated to that class by PacifiCorp's allocated cost-of-service study.

42. The process of unbundling necessarily requires assigning the residual to one or more of the individual functions; on the appropriate assignment PacifiCorp and Plum Creek differ. PacifiCorp places all of the residual in the distribution function, while Plum Creek prefers putting it all in the production function. PacifiCorp's unbundling method relies on its allocated cost study results to establish the unbundled revenues for the production and transmission

functions. The distribution function is then set residually to maintain the current revenue level for each customer class.

43. Plum Creek offers several methods for unbundling class revenues. The method it prefers (Method A) establishes the transmission function revenues based on Federal Energy Regulatory Commission (FERC) approved revenues and sets distribution function revenues using the results of PacifiCorp's allocated cost study. The production function revenues are then established on a residual basis. Plum Creek's Method B also sets transmission based on FERC revenues, but sets both production and distribution revenues based on the allocated cost study. The total revenues produced are compared to current rate revenues; the difference is eliminated by making a proportional change to both production and distribution revenues. With Method B the residual is shared between production and distribution.

44. Plum Creek also offers Method D. Method D sets transmission revenues based on FERC revenues and sets both production and distribution revenues at the marginal cost revenues estimated by PacifiCorp. The total revenues produced are compared to current rate revenues, and the difference is eliminated by making a proportional change to both production and distribution revenues, as with Method B. A variation on Method D (Method DR) makes an equiproportional adjustment to the distribution revenues, reconciling the sum of the distribution revenues of all classes to the functionalized current revenues.

45. The following table shows, for the large customer class, the effective per unit rate for the production and distribution functions that result from each of the four rate design options just described (Pacific, Plum Creek A, Plum Creek B and Plum Creek DR), along with PacifiCorp's estimated per unit long-run marginal costs (mc). PacifiCorp's rate design proposal produces a higher distribution rate, while the three Plum Creek rate design options produce a higher production rate. Some adjustment to production or distribution, or both, is necessary, since current rates recover more than allocated embedded costs for this customer class (marginal costs and allocated embedded costs are also not equal -- PacifiCorp's total estimated marginal costs for this class are about 85 percent of allocated embedded costs).

Effective Per Unit Rates by Cost Function (mills per kwh)		
Rate Design Option	Production	Distribution
Marginal Cost	21.8	3.9
PacifiCorp	20.8	9.4
Plum Creek Method A	27.8	2.8
Plum Creek Method B	26.9	3.7
Plum Creek Method DR	26.3	4.3

46. Plum Creek opposes PacifiCorp's method of unbundling, maintaining that it produces an artificially low supply price which will preclude other suppliers from entering the market. In supplemental testimony Dr. Rosenberg states that "...if PacifiCorp's residual method is adopted, competition will be illusory for PacifiCorp's customers." May Supplemental Testimony, p. 15. PacifiCorp counters that Plum Creek's unbundling proposal produces an excessive supply price for large customers, while at the same time producing an unrealistically low supply price for residential customers. PacifiCorp asserts that the excessive supply price for large customers will enable those customers to escape the effects of past rate decisions and will unfairly harm shareholders. Mr. Taylor testified that Plum Creek's method shifts responsibility for the residual to the PacifiCorp's stockholders and produces a revenue loss for the utility that is unrelated to the difference between the embedded cost of its generation resources and market prices. Feb. Rebuttal Testimony, p. 8.

47. There are merits to both PacifiCorp's and Plum Creek's unbundling approaches, but neither is entirely acceptable. Plum Creek's desire to establish distribution revenues based on embedded costs has some appeal, because that component will continue to be regulated. However, there is no difference between Plum Creek's and PacifiCorp's method in terms of *how much* total distribution revenue is collected, just *who pays* it. On the other hand, since the production component is subject to choice, it is important to set unbundled production rates that encourage economically efficient initial supply choices. PacifiCorp's approach appears to come closer to (but falls short of) sending customers correct economic price signals, based on evidence in the case.

48. PacifiCorp's proposed production price (effectively 20.8 mills/kwh) is lower than four possible alternative benchmarks for an unbundled production price: (1) PacifiCorp's

estimated long-run marginal production cost (21.8 mills/kwh);¹ (2) the average generation component of PacifiCorp's current prices (22.79 mills/kwh);² (3) MCC's estimated average seller's market clearing price in the Northwest (a possible opportunity cost, 24.8-26.7 mills/kwh);³ and (4) Dr. Rosenberg's estimate of "realistic" long-run marginal costs (26-35 mills/kwh).⁴ To the extent the Commission ultimately determines that PacifiCorp has stranded costs, the CTC would be removed from the production component, making PacifiCorp's contestable production price even lower.

49. The outcome identified by Plum Creek, i.e., that new entrants may not be able to compete against PacifiCorp's production price, appears possible. Failure of a market to develop through superior quality at the same price or through lower priced services, however, is not necessarily a negative outcome, so long as the unbundled production rate conveys economically correct price signals.

50. PacifiCorp's approach is not satisfactory, because the unbundled production rate is less than PacifiCorp's estimated long-run marginal cost. (Dr. Rosenberg testified that, for the purposes of this case, he accepts the results of the Company's cost studies as reasonable. Tr. p. 135). Long-run marginal cost provides a more appropriate price signal than allocated embedded costs with respect to the societal cost of providing the supply service customers are currently receiving. (That is, production costs associated with providing the same service quality, reliability and firmness over the same term, with similar price stability and other characteristics of service provided under regulation). Therefore, long-run marginal cost is a more appropriate cost and price against which new entrants should compete and to which customers considering market based supply should compare alternative supply offers. MCC's seller's market clearing price might also be an appropriate price to the extent it reflects PacifiCorp's

¹ February 1998 Rebuttal Testimony of David Taylor, Exhibit DLT-4, p. 11.

² Revised Transition Plan, Appendix G1, p. 1.

³ January 1998 Direct Testimony of Richard Albert, Exhibit-LC02, p. 2-6.

⁴ May 1998 Supplemental Testimony of Alan Rosenberg, p. 17, Tr. p. 132.

opportunity costs. However, the study that produced these prices caused considerable dispute so it may not be appropriate to use them at this time.

51. Plum Creek's Method A prices unbundled distribution below the Company's estimated long-run marginal cost, but equal to what the allocated cost study produces. Method A's residual unbundled production price (27.8 mills/kwh) is higher than the first three possible production benchmarks discussed above, but within the range of "realistic" marginal costs identified by Dr. Rosenberg. (Although Dr. Rosenberg accepts the results of PacifiCorp's marginal cost study, he testified at the hearing that the results are about one-third lower than PacifiCorp's previous study and he believes marginal production costs in the 26-35 mill range are more realistic). The risk, identified by PacifiCorp, that Method A could result in reduced earnings that shareholders would bear during the transition period, appears possible. Whether or not PacifiCorp would actually experience a net revenue reduction would depend on its success in marketing freed-up power to other customers and in other markets.

Decision on Rate Design

52. Neither PacifiCorp's proposal nor Plum Creek's Method A in present form is satisfactory. The other options in the record are Plum Creek's Methods B and D. Both of these methods involve sharing the residual between production and distribution. Plum Creek believes Method B is preferable to Method D. Method B's production rate is about 27 mills/kwh while Method D's is about 26.3 mills/kwh.

53. The Commission determines that it is appropriate to modify PacifiCorp's proposal to establish a production rate at least as high as its estimated long-run marginal production costs. The difficulty with such an approach is knowing what the appropriate marginal cost number is. Although Dr. Rosenberg testified that he accepts PacifiCorp's results, he leaves the impression that those results might be too low. Determining the most appropriate number in the range between 21.8 and 35 mills would be subjective, based on the current record.

54. Production revenues produced by PacifiCorp's estimated long-run marginal costs and Dr. Rosenberg's acceptance of those costs are established in the record. PacifiCorp shall set unbundled production revenues for eligible large customers electing choice at the levels produced by its long-run marginal cost study. Feb. Rebuttal Testimony of David Taylor, Exhibit DLT-4, p. 11 of 22.

55. Transmission revenues shall be established based on FERC approved transmission revenues and allocated to the large customer class according to FERC allocation methods, as recommended by Dr. Rosenberg. Jan. Testimony, p. 38. The unbundled transmission price should be consistent with the FERC transmission price, to the extent possible. This prevents customers from having to make supply decisions based on how both the transmission and supply portions of their bills may be affected by their decision to move to market based supply.

Consistency in transmission may also promote more efficient supply decisions since consumers will judge supply offers on their relative merits and not because of differences in how FERC and the Montana PSC treat regulated transmission services. Recovery of other revenues necessary to achieve the revenue level produced by current rates shall be through distribution revenues.

Conclusions of Law

1. The Commission exercises authority over public utilities and the electric utility industry restructuring pursuant to its authority under Title 69, particularly Chapters 3 and 8, MCA. PacifiCorp is a public utility subject to the Commission's jurisdiction and authority.

Order

WHEREFORE, the Commission orders the following, in order to implement large customer choice on and after July 1, 1998:

1. PacifiCorp shall track transition costs/benefits of those customers entitled to and electing choice on July 1, 1998, pursuant to the accounting mechanism outlined in this Order, for accounting purposes only. The Commission will make the determination on these costs/benefits in the order issued based on the final proceeding to be held on August 28, 1998.

2. PacifiCorp shall incorporate the rate design established in this order, setting unbundled production revenues for eligible large customers electing choice at the levels produced by its long-run marginal cost study.

3. PacifiCorp shall unbundle its tariffs into Production, Distribution and Generation functions, as provided in this Order, for its customers entitled to choice on July 1, 1998.

Done and dated this 16th day of June, 1998 by a vote of 5-0.

BY ORDER OF THE MONTANA PUBLIC SERVICE COMMISSION

DAVE FISHER, Chairman

NANCY MCCAFFREE, Vice Chair

BOB ANDERSON, Commissioner

DANNY OBERG, Commissioner

BOB ROWE, Commissioner

ATTEST:

Kathlene M. Anderson
Commission Secretary

(SEAL)

NOTE: Any interested party may request the Commission to reconsider this decision. A motion to reconsider must be filed within ten (10) days. See ARM 38.2.4806.