ROCKY MOUNTAIN POWER
A DIVISION OF PACIFICORP

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Armand Southall
Regulatory Specialist
Office of Natural Resources Revenue
P.O. Box 25165
MS 61030A
Denver, CO 80225

Subject: Comments to Proposed Rule Consolidated Federal Oil and Gas and Federal and Indian Coal Valuation Reform (ONRR-2012-0004 (RIN 1012-AA13))

Dear Mr. Southall:

On behalf of PacifiCorp and its affiliates, we hereby take this opportunity to provide comments to the referenced proposed rule "Consolidated Federal Oil and Gas and Federal and Indian Coal Valuation Reform."

By way of introduction, PacifiCorp is one of the West's leading electric utilities, serving approximately 1.8 million customers in six states. This utility has a diverse portfolio of generating facilities inclusive of hydroelectric, coal, natural gas, geothermal and wind sources produced through two business divisions of PacifiCorp which includes Rocky Mountain Power and Pacific Power. Collectively, PacifiCorp provides electric service to customers in Utah, Idaho, Wyoming, Oregon, Washington and northern California. Of PacifiCorp's total annual generation output, approximately 62% of this energy is produced from coal-fired generation, 12% from natural gas, 4% from hydro, 5% from wind and other with the balance of 17% coming from energy purchase contracts.

In addition, PacifiCorp through its subsidiaries and affiliates is a producer of federal coal from captive coal mines serving our power plants of which these costs flow through to our customers.

As a regulated utility, we have an obligation to better understand the implications of this proposed rule and the impacts to our customers given the proposed changes involving both arm's length and non-arm's length contracts for the calculation of production royalties. The complexity of these proposed rules as presently written introduces multifaceted ambiguities without simplicity, while creating greater regulatory uncertainty. Additional time is required to more fully evaluate, identify and understand the full range of the consequences of the proposed changes and to provide informed comments and data to the Department of Interior's Office of Natural Resources Revenue (ONRR) to help develop a sensible policy for production royalties from federal lessees, buyers of oil, gas, and coal, taxpayers, and others impacted by such a change. The following comments shed some light on our concerns.

PacifiCorp as a Coal Producer

The proposed regulations under Part 1206.252(b)(1) seeks to value the gross proceeds for coal operations who use their own coal production for electric generation, i.e. a captive mine. The process is attempting to value the gross proceeds for coal, downstream from the mine, for the value of the sale of the electric generation produced by the coal. The proposal allows for coal transportation, coal washing, electric generation, and electric transmission deductions. PacifiCorp states that this proposed regulation is not applicable for the company's current captive mine/power plant operations. This valuation methodology could only be applicable for a true merchant plant operation where there is a definitive, identifiable arms-length sales transaction and a specific sales point for which a transmission deduction could be calculated. The proposal incorporates netback methodology calculations. ONRR should be fully aware from past experience that a valuation requiring netback calculations has historically not met the test of simplification for application for either the lessee or verification of audit for ONRR.

Following the proposed regulation of Part 1206.252(b)(1) with the proposed regulation Part 1206.252(b)(2), ONRR correctly identifies a non-arm's length sales transaction exists when the delivery of electricity occurs directly into the utility transmission grid. However, once electricity enters the grid it physically cannot be tracked to its destinations. Electric tariff rates, as set by the various public service commissions for electric ratepayers, include consideration for generation, transmission, distribution, and customer service expenses. As a regulated utility, we are providing these bundled services in the delivery of electricity to our ratepayers. An attempt to unbundle the components of rates would require numerous assumptions and endless allocations without arriving at a definitive or auditable result.

PacifiCorp has a long history of operating and participating in captive coal mines which provide coal under non-arm's length sales transactions to PacifiCorp owned and jointly owned coal fired generating plants. PacifiCorp has worked extensively with ONRR in developing a valuation methodology to value gross proceeds for these operations. The process has included working through the benchmarks in the current regulations to arrive at settlement agreements for the valuation which has proven workable and defendable.

Although the settlement agreements were not specifically tied to a single benchmark, the benchmarks did provide a framework which allowed for meaningful review by the parties. PacifiCorp maintains that these agreements and valuation methodology are an appropriate representation of gross proceeds accruing to lessee as a regulated utility. By its regulatory charter, PacifiCorp can only earn a return upon the net investment of the asset and the recovery of prudently incurred costs. This principle is represented in the development of the settlement agreements. ONRR has provided no evidence that these settlements are not representative of gross proceeds for PacifiCorp as a regulated utility.
The proposed rules as introduced by ONRR would disregard the past methodologies developed cooperatively by PacifiCorp and ONRR, and would instead invoke ONRR's own unilateral discretion and ambiguity without transparency. For these reasons, PacifiCorp maintains that the benchmarks in the current regulations do provide benefit in valuing non-arm's length sales transactions. We encourage ONRR to consider the past history of valuation in this unique situation and not simply invalidate previous settlement agreements. At a minimum, ONRR should include a grandfather clause for such settlement agreements where circumstances have not materially changed.

If the valuation issues are not specifically addressed by the proposed regulations or ONRR determines that the lessee is not in compliance then Part 1206.254, i.e. the "Default" provision becomes the avenue for valuation and determination. PacifiCorp is concerned that Part 1206.254 gives ONRR an overly broad scope and timeline for the determination of valuation, transportation, and washing regulations. ONRR arrives at the "Default" provision without providing alternatives for lessees to work through valuation issues. The only likely recourse would be for the lessee to enter into lengthy appeals processes once a determination or demand notice has been received from ONRR further delaying meaningful resolutions.

Additionally, PacifiCorp expresses concern that ONRR is seeking to value the commodity of electricity at a royalty rate prescribed in federal coal lease agreements. The company is not aware of statutes that authorize ONRR to interchange these commodities.

PacifiCorp as a Regulated Utility

As a regulated utility, PacifiCorp procures annually over 16 million tons of coal for the production of electric generation in the company's coal-fired thermal generation fleet. These purchases are made through a combination of long term and short term coal contracts with coal suppliers. As a common component in these contracts (coal supply agreements) are provisions for the pass-through of changes in governmental impositions. These provisions allow for changes in costs that the coal supplier would not be able to foresee at the time of the execution of the agreement. We would expect that an increase in the royalty obligation of a coal producer from the proposed regulations would be passed through to PacifiCorp which would result in a direct cost increase to our ratepayers.

PacifiCorp is very vigilant in protecting and managing cost increases for its customers. As such, PacifiCorp would object to a change in regulations, which would result in a direct increase in costs for its ratepayers and greater uncertainty in the valuation process, with the only apparent corresponding benefit being a possible increase in royalty revenue for the federal and state governments. We would view this as only a redistribution of revenue to the government at the direct expense of our electric utility ratepayers.

This is a significant issue facing our operations and customers. Your consideration and immediate attention to this important matter is greatly appreciated.

Respectfully,

Cindy A. Crane

Cindy A. Crane
President & CEO
Rocky Mountain Power