BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

UE 180/ UE 181/ UE 184

In the Matter of PORTLAND GENERAL ELECTRIC COMPANY Request for a General Rate Revision (UE 180), In the Matter of PORTLAND GENERAL ELECTRIC COMPANY Annual Adjustments to Schedule 125 (2007 RVM Filing) (UE 181), In the Matter of PORTLAND GENERAL ELECTRIC COMPANY Request for a General Rate Revision relating to the Port Westward Plant (UE 184).	OPENING BRIEF OF THE CITY OF PORTLAND, OREGON

INTRODUCTION

In response to Portland General Electric's request for a general rate revision, the City of Portland has asked that the Commission act for the protection and benefit of ratepayers in various aspects of utility tax planning and decision-making. For too long in Oregon utility tax planning and decision-making has focused on optimizing returns to shareholders, to the exclusion of ratepayer interests. In furtherance of these goals, the City has suggested that the Commission undertake a series of determinations.

The City has asked that in setting PGE's rates, the Commission impute the beneficial tax effects of a corporate reorganization. The City has requested that the Commission direct PGE to repay ratepayers for funds paid to Enron without explicit prior authorization by the Commission, as determined after a public proceeding in which the public interest in such transfers was properly weighed. The City asks that the Commission require PGE to provide annual reports of to the Commission of steps taken by the utility to engage in practical and prudent tax planning, and subsequent steps taken to implement such planning. The City seeks the avoidance of having ratepayers double charged for deferred taxes. The City believes that each of these measures are necessary in order to achieve "fair, just and reasonable" rates for PGE ratepayers. ORS 757.210(1).

1. The Commission should impute the tax benefits of reasonable and prudent steps that PGE could have taken in the past to reduce its effective tax rate.

"The public interest requires that utilities maintain their costs at the lowest level consistent with proper service to the consumer." Swiren, "Accelerated Depreciation Tax Benefits in Utility Rate Making", 28 U. Chi. L. Rev. 629, 632 (1961). The City has identified a reasonable and prudent business decision that PGE could have taken that would have provided significant, long-term benefits to PGE's ratepayers through reduction in income tax burdens. COP/100/Jubb/5-10.

"The tax calculations used to establish a utility's test year tax liability for ratemaking purposes [should] reflect [a] ratemaking presumption that the utility prudently takes advantage of available favorable tax options that will reduce its overall tax liability." Re Apple Valley Ranchos Water Co., No. 87-08-024, 85-11-041, 25 CPUC 2d 140, 158 (Cal PUC, August 12, 1987), (citing, City and County of San Francisco v. Public Utilities Commission, 6 Cal. 3d 119, 127, 91 P.U.R.3d 209, 490 P.2d 798, 98 Cal. Rptr. 286 (1971)); adhered to, State Board of Equalization

of Property Owned by Commission Regulated Utilities, No. 92-03-052, 1992 WL 511733 (Cal PUC, March 31, 1992). Setting rates on any other basis would allow the utility to engage in imprudent tax practices at the ratepayers' expense. Apple Valley, supra, 25 CPUC 2d 140, 158. See also, Bell Telephone Co. v. Pennsylvania Public Utility Commission, 47 Pa Cmwlth 614, 619-622, 408 A2d 917 (1979) (holding that the Commission could exclude portion of utility's tax expense where ratepayers were not afforded fair share of tax benefits).

PGE has strenuously objected to the City's proposal, arguing that it would have unreasonably exposed the utility to potential IRS penalties. UE 180/PGE 1700/Piro-Tamlyn/8, 12 and 15. PGE failed to acknowledge that the City's testimony specifically addressed that concern: "PGE/Enron management should have vigorously pursued the LLC conversion transaction by requesting a private letter ruling from the Treasury or completing the transaction on a covered tax opinion without a Treasury ruling." COP 100/Jubb/9. The City's suggestion is no different from what the Commission has itself required in the AR 499 proceeding. In Order No. 06-532, the Commission required that utilities subject to SB 408 file requests for private letter rulings on various utility income taxes, including accelerated depreciation. Id., at pp. 3 - 5.

PGE also argues that it would not have been able to proceed with an LLC conversion as it would not have had a "business purpose", thus violating "step-transaction and economic substance doctrines." PGE/1700/Piro-Tamblyn/8. This represents an erroneous conclusion. The City suggested that the LLC conversion could have proceeded under well-established corporate restructuring and taxation doctrines, providing a step-by-step description of how the conversion might be achieved. COP/100/Jubb/5 - 10. The type of corporate reorganization and asset transfer suggested by the City has been specifically considered and approved by the Internal Revenue Service in its administrative determinations, and in court opinions. See, e.g., Granite Trust Co. v.

United States, 238 F.2d 670 (1st Cir. 1956) (approving a step transaction made for the purposes of avoiding tax consequences on the grounds that minimizing or avoiding taxation is not an illicit motive.); IRS Private Letter Ruling 9822037, 1998 WL 273486 (May 29, 1998); COP/107 (IRS Revenue Ruling 2004-77); (permitting sale of stock to avoid section 332 treatment); Dover Corp. v. Commissioner, 122 T.C. 324, 351, n.19, 2004 U.S. Tax Ct. LEXIS 19, 122 T.C. No. 19 (2004) (2004). See, also, Littriello v. United States, 2005 U.S. Dist. LEXIS 9813, 95 A.F.T.R.2d (RIA) 2581, 2005-1 U.S. Tax Cas. (CCH) P50385 (WD Ky 2005) (affirming validity of IRS's "check-the-box" regulations). The conversion suggested by the City is certainly no less daunting or intricate than other corporate transactions in which PGE has been involved. So it all seems to come down to a matter of motivation and desire, in which the ratepayers' interests have not been as zealously represented.

In the end, the City is not advocating that PGE should have been required to follow a specific process of corporate reorganization. Rather, the City is noting that various, legal means exist by which utility management could have engaged in reasonable tax planning that would have benefited ratepayers. The example offered by the City would have achieved substantial tax benefits, providing the opportunity for significant rate savings. PGE's next objection was that the City's proposal would have been disfavored by the Enron Board. Acting as PGE's sole shareholder, PGE believes that the Board would have been"duty bound to obtain maximum economic recovery for the benefit of the creditors." PGE/1700/Piro - Tamlyn/13. While the Board's response is a matter of pure conjecture, PGE's response serves to otherwise spotlight the regulatory question presented by the City's proposal: who represents the ratepayers' interests? Apparently, the Enron Board was not, and PGE was merely following the directives of its corporate owner. Thus, the Commission must shoulder the responsibility.

Without exception, all public utility regulators are empowered to set just and reasonable rates. In most jurisdictions, the enabling statute explicitly grants the regulator such authority. See, e.g., Pacific Tel. & Tel. Co. v. Public Utility Comm., 62 Cal2d 634, 44 Cal Rptr 1, 401 P2d 353 (1965)[1]. The Oregon Legislature has delegated explicit authority to the Public Utility Commission to regulate public utilities:

> the commission shall represent the customers of any public utility . . . and the public generally in all controversies respecting rates, valuations, service and all matters of which the commission has jurisdiction. In respect thereof the commission shall make use of the jurisdiction and powers of the office to protect such customers . . . to obtain for them adequate service at fair and reasonable rates. The commission shall balance the interests of the utility investor and the consumer in establishing fair and reasonable rates.

ORS 756.040(1).

The Commission's statutory responsibility for protecting ratepayers has been interpreted as delegating "broad rate-making authority". American Can Company v. Lobdell, 55 Or App 451 (1982); Cascade Natural Gas Corporation v. Davis, 28 Or App 621 (1977). In the exercise of this authority, the Commission is required to set utility rates that are fair, just and reasonable. See e.g., Order No. 05-1050, supra, at 4; In the Matter of PacifiCorp, UE 116, Order No. 01-787 at 5.

Other state utility regulatory commissions, operating under similar charges to provide fair and reasonable rates for ratepayers, have adopted rates imputing tax decisions to the utility. In the case of City and County of San Francisco v. Public Utilities Com., 6 Cal3d 119, 490 P2d 798 (1971), the utility had opted to account for asset depreciation on a straight line basis. As a result, the utility incurred higher than necessary income tax expenses. The California Supreme Court

[1] In Pac Tel, the California Supreme Court affirmed the agency's imputing of an income tax rate for the utility where its parent company, which held 90 per cent of the utility's stock, had otherwise elected to file a consolidated federal income tax return to save taxes resulting from intercorporate payment of dividends, by regarding the utility as an unaffiliated corporation.

upheld the finding by the California Public Utilities Commission that management's discretion has harmed the public interest, and thus, that it was fair and reasonable to impute Pacific's income tax expenses for the test year:

> Income tax expense must be considered by the commission in establishing Pacific's cost of service. . . . However, 'the primary purpose of the Public Utilities Act is to insure the public adequate service at reasonable rates without discrimination; and the commission has the power to prevent a utility from passing on to the ratepayers unreasonable costs for materials and services by disallowing expenditures that the commission finds unreasonable. . . The same rule applies where the utility resorts to accounting practices which result in unreasonably inflated tax expense.

City and County of San Francisco, supra, 6 Cal3d at 126 (citations omitted).

The California Supreme Court noted that under the utility's disallowed method of accounting, it would have been "provide[d] a source of interest-free capital.' We do not know how much capital will be provided, but the dissenting commissioners estimate that the ratepayers in the next 10 years will have to provide between $750,000,000 and one billion dollars." Id., at 128. In the instant case, PGE transferred in excess of $700 million in revenues to Enron from 1997 through April 2006, above and beyond reported dividend payments, in the guise of tax payments. COP/100/Jubb/12. The parallels of these two cases almost intersect.

In the case of City of Los Angeles v. Public Utilities Comm., 15 Cal 3d 680, 542 P.2d 1371, 125 Cal Rptr 779 (1975), the City of Los Angeles challenged a decision by the California Public Utility Commission that it lacked regulatory authority to impose rates that would reflect changes in the utility's tax obligations. Citing its prior San Francisco decision, the California Supreme Court held that the Commission had the legal authority, as well as the statutory duty, to

impose rate relief that it was otherwise shying away from. See also, Public Utility Com. v. Houston Lighting & Power Co., 748 SW2d 439, 442, 1987 Tex. LEXIS 408 (Tex. 1987) (utility's rates must reflect the tax liability actually incurred, as rates must reflect tax savings that will reduce utility's federal income tax expenses); Colorado Municipal League v. Public Utility Commission, 172 Colo 188, 203-204, 473 P2d 960 (Colo. 1970) (holding that where utility management abuses discretion to ratepayers' detriment, regulatory commission had a duty to impute tax advantage for ratepayers which utility had otherwise failed to avail for itself); Pittsburgh v. Pennsylvania Public Utility Com., 182 Pa Super 551, 580, 128 A2d 372 (Pa Super Ct 1956) (holding that as utility could only pass on proper expenses and allowances plus a legitimate profit or return to the utility, projected tax expenses were improper and impermissible).

PGE does not argue that the conversion of a regulated utility from a private corporation under ORS Chapter 60 to a limited liability company under ORS Chapter 63 would be anything more than routine matter of corporate law. Under Oregon law, in converting a private corporation to a limited liability company, the business entity continues its existence, title to all real estate and other property is vested in the converted business entity without reversion or impairment, and all obligations of the converting business entity, whether contractual, statutory, or administrative, are automatically obligations of the converted business entity. ORS 63.479(1)(a) – (c).

There are numerous reported cases of regulated utilities forming, merging into or transforming into limited liability corporations. See for example, In re Duke Energy Corp., 2006 WL 1559336 (NC Utility Comm. March 24, 2006) (approving merger agreement in which Duke Energy converted to a limited liability company to be called Duke Power Company, LLC, with subsequent distribution of assets and liabilities); In re Duke Energy Corp., 2006 WL 2422171

(NC Utility Comm. July 11, 2006) (reviewing tax sharing agreement providing for Duke Energy and subsidiaries to file consolidated income tax returns and allocating consolidated income tax liabilities and benefits); Application of Level 3 Communications, LLC Relating to Transfer of Control and Financing Transactions, NO. T-03654A-06-0356, 68997, 2006 WL 3126031 (Ariz Corp. Comm. October 20, 2006); Trans-Elect NTD Path 15, LLC, 111 FERC ¶61,140, 2005 WL 1031405, Docket No. ER05-17-001 (May 4, 2005) (discussing availability of income tax allowances for owner of California electricity transmission facility); Application of Virginia Electric and Power Company, d/b/a Dominion North Carolina Power, for Authority to Transfer Functional Control of Transmission Assets to PJM Interconnection, LLC, Docket No. E-22, 2005 Pa. PUC LEXIS 5 (Penn Public Utility Comm., April 19, 2005); Application for Approval of Transfer of Control of Alaska Pipeline Company, 2004 WL 3317379 (RCA June 4, 2004) (noting that conversion of pipeline company to limited liability company would result in avoidance of federal income taxes); In re Magellan Pipeline Co., LLC, No. 02-0263, 2004 WL 1923054 (Illinois C.C., May 26, 2004) (noting purpose of conversion of pipeline from a corporation to a limited liability company was to qualify spin-off as tax-free for federal income tax purposes); Application for Authority to Transfer Assets of Broadwing Communications Services, Inc., to C III Communications Operations, LLC., 2003 WL 24127221 (Ariz. C.C., July 25, 2003) (noting transaction structured as asset sale, rather than a stock transfer, for federal and state income tax purposes).

PGE asserts that the elimination of its preferred stock was not addressed by the City's testimony. PGE/1700/Piro-Tamlyn/14, line 1. This was not the case. The exhibits submitted by the City noted that the preferred stock is subject to a mandatory 2007 retirement, and that it could be otherwise refinanced along with other long-term debt. COP/100/Jubb/5, lines 13-17;

COP/101/1. The City's exhibits noted that the preferred stock is redeemable through the operation of a sinking fund, and that PGE has the option to redeem additional preferred shares each year and through open market purchases. Id. In the overall context of the proposed conversion, this aspect would have amounted to little more than a "housekeeping detail". COP/101/2. There is no requirement to file rebuttal where the inaccuracy is apparent. To act otherwise would result in an unnecessarily cluttered, repetitive docket.

In calculating PGE's taxable income and income tax rates includable within PGE's rates for electricity, the Commission should deem that an LLC conversion of PGE occurred prior to its stock distribution to Enron creditors. The City was merely suggesting that PGE could follow Treasury Regulations and use them to benefit ratepayers. COP/103/3. The proposed corporate restructuring is one example of many that could have been undertaken by the utility for achieving reasonable and favorable tax benefits for the advantage of ratepayers. To date, the benefits of tax planning have flowed exclusively to PGE's shareholders, as has been so amply demonstrated by Enron.

PGE's response has been outwardly dismissive, indicating variously that the proposal was either too risky, or that it would never have been acceptable to Enron or the IRS. PGE's first point seems to be that the Commission should never direct the utility to take an action that may benefit the ratepayers by reducing rates, and where the utility's shareholders might not obtain as favorable a return. As to the second point, it is the height of irony for anyone to say that Enron should be cautious in taking actions that might be beneficial for ratepayers, given its shear rapaciousness in pumping up corporate returns in earlier times.

The corporate conversion would have been a reasonable and prudent business decision with significant benefits for ratepayers. The effect of this conversion would have been to

significantly reduce PGE's tax burden over a twenty year period, based upon the approximate weighted average useful life of PGE's depreciable assets. COP/100/Jubb/9. PGE and its corporate affiliates benefited significantly over the years from favorable tax policies promoted by the Commission. The time has come for the Commission to reinvigorate its statutory charge to "represent the customers of any public utility . . . [and] obtain for them adequate service at fair and reasonable rates." ORS 756.040(1). There is well-established precedent of imputing tax savings into regulated rates by other public utility commissions, where the utility could have taken reasonable and prudent tax avoidance actions, but chose not to do so to the detriment of the ratepayers. This is a question of what is fair and reasonable for the ratepayers.

2. The unauthorized "tax" payments made by PGE to Enron should be refunded to the ratepayers

The City has asked that the Commission direct PGE to refund to the ratepayers the payments made to Enron without prior, explicit authorization by the Commission. COP/100/Jubb/11-13. PGE asks that the Commission "ignore" the City's request, contending that it "informed the Commission on an annual basis of payments of payments to Enron for taxes in an Affiliated Interest Filing." PGE/1700/Piro-Tamlyn/17. Under ORS 757.495(4), un-reviewed contracts for payments are subject to consideration by the Commission for propriety during subsequent proceedings.

In approving Enron's ownership of PGE under the terms of ORS 757.511, the Commission imposed various regulatory requirements, including but not limited to, creating a "ring fence" between PGE and Enron and its other subsidiaries. Enron Corp., Order No. 97-196, UM 814, 177 P.U.R.4th 587, 1997 WL 406191 (June 4, 1997). For example, under Stipulated Condition No. 9, Enron agreed to provide the Commission with: (a) at least 60 days prior notice

of its intent to transfer more than 5 percent of PGE's retained earnings to Enron over a six-month period; (b) at least 30 days prior notice of its intent to declare a special cash dividend from PGE; and (c) Notice within 30 days of quarterly common stock cash dividend payments from PGE. These conditions were imposed by the Commission to protect the ratepayers from harm. After accepting the Commission's conditions, however, PGE went on to send cash payments in excess of $700 million to Enron under the guise of taxes. COP/100/Jubb/12; COP/110/3[2]; COP/111/3[3]. During the years 1996 through 1999, Enron carried forward net operating losses of $3.1 billion. COP/106/21. On Enron's 2001 Federal income tax return, the company had a net operating loss of $4.6 billion. Id. The "tax" revenues sent by PGE to Enron during the time of Enron's ownership were more than offset by the tax losses generated by Enron. Combined over time, these "tax" payments amounted to more than 150% of the cash dividends reported to the Commission under the conditions of the approved merger. Declaration of David R. Jubb in Support of the City Of Portland's Opposition to Summary Judgment, UM 1262, at 17 (filed September 15, 2006).[4]

Under the Tax Allocation Agreement, PGE agreed that it would compensate Enron's other subsidiaries for the use of their "net operating losses and/or tax credits" ("NOLs").

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[2] Commission staff calculated that the amount of federal, state and local taxes paid by Enron (or Portland General Corporation) from 1997 through the third quarter of PGE's fiscal year 2006 totaled $682,738,599.

[3] "As PGE was included in Enron's consolidated income tax return prior to April 3, 2006, the Company made payments to Enron for PGE's income tax liabilities. The $25 million income taxes payable to Enron at December 31, 2005 represents net current income taxes payable for the fourth quarter of 2005 that was paid to Enron in January 2006. In April 2006, PGE paid Enron $17 million for net current income taxes payable for the first quarter of 2006."

[4] Under OAR 860-014-0050(1)(e), the Commission may take official notice of "documents and records in the files of the Commission". See, In re Pac-West Telecomm, Inc. v. Qwest Corporation, Order No. 05-874, fn. 34, IC 8 & IC 9 (July 26, 2005); Portland General Electric Company Application for Deferral of Hydro Replacement Power Costs, Order No. 04-108, UM 1071, 2004 Ore. PUC LEXIS 87, 231 P.U.R.4th 104 (March 2, 2004) (where Commission took official notice of the UE 92 record).

COP/104/8, Tax Allocation Agreement, § 3.2(a). Under the Tax Allocation Agreement, the NOLs of Enron and its subsidiaries were an asset that PGE was allowed to use. In return, PGE agreed to pay Enron compensation for the use of the NOLs. The Agreement allowed Enron to convert tax losses, otherwise only valuable for offsetting future profits from the subsidiaries that were generating those tax losses, into cash through sales of the losses to PGE. In essence, the Agreement served to allow Enron as PGE's holding company to obtain cash in excess of regularly declared dividends.

Property includes things that are or may be owned or possessed, valuable rights or interests, or things for which there are legal title. *Webster's Third New Int'l Dictionary*, 1818 (unabridged ed 1993). To purchase property means to obtain possession, such as by paying money or its equivalent. Id., 1844 (unabridged ed 1993). Enron's NOLs constitute a form of intangible property, valuable rights that were capable of transfer through an exchange of value. These transactions created present value for Enron by converting the tax losses into cash for the parent corporation. PGE's acquisition of NOLs generated by other Enron subsidiaries were a form of purchasing property by the public utility from affiliated interests.

In Pacific Northwest Bell Telephone Co. v. Katz, 121 Or App 48, 53, 853 P2d 1346, *rev den*, 318 Or 25 (1993), the telephone utility attacked the Commission's determination that telephone directories and business and customer lists were a form of property belonging to the telecommunications utility that were subject to the Commission's jurisdiction and oversight. The utility argued that the lists and directories were not a form of property, and that use of the property was merely exploiting a business opportunity. The court rejected these arguments, finding that the utility's use of the property had resulted in an increase in value, which the utility then sought to redirect to a non-regulated affiliated entity. Under the Tax Allocation Agreement,

PGE and Enron entered into property transactions that allowed Enron to pocket millions of dollars otherwise intended to cover tax payments. Instead, the parent corporation retained the cash, offsetting the revenues against NOLs generated by other corporate subsidiaries. Enron's retention of this cash created substantial value for the parent corporation. In the meantime, as aptly summarized by Minnesota Attorney General Mike Hatch, utility ratepayers must shoulder "the tax twice, once through the utility bill and again through the lost revenue to government that means either higher taxes for them or less government services."[5]

As a regulatory agency, the Commission must remain alert for subterfuge or attempted evasion of the letter or obligation of the law: "Any plan or scheme, whether by purported lease, agency, or other device disguising the true nature of the [arrangement] will be of no avail for that purpose." State ex rel by Heltzel v. O. K. Transfer Co., 215 Or 8, 330 P.2d 510 (1958); Or Atty Gen Op 6462, 1992 Ore. AG LEXIS 33, October 15, 1992 (Concluding that regulated entity could not create affiliate for the purposes of evading regulation by the Public Utility Commission). It is a well established rule of law that no one may do indirectly what may not be done directly. 15 Op Atty Gen Or 344, 1931 Ore. AG LEXIS 276 (July 31, 1931). See, also, 71 Op Atty Gen Wis 147, 1982 Wisc. AG LEXIS 18 (Concluding that the Wisconsin utility commission had authority to determine whether a holding company formed by a public utility corporation if the arrangement was a "device to enable the public utility corporation to evade regulatory jurisdiction.")

In Pacific Northwest Bell Tel. Co. v Katz (1992) 116 Or App 302, 841 P2d 652, reconsideration den 316 Or 528, 854 P2d 940, the Court of Appeals held that the Public Utilities

[5] David Cay Johnston, "Many Utilities Collect for Taxes They Never Pay", New York Times (March 15, 2006) < http://www.nytimes.com/2006/03/15/business/15utility.html?ex=1300078800&en=3efacf3b551be105&ei=5088&partner=rss nyt&emc=rss > (site visited November 16, 2006).

Commission possessed the authority to order the phone company to refund amounts over-collected under an interim rate schedule not in compliance with an authorized revenue level. The court approved the Commission's refund order, even though it was not explicitly authorized by statutory sections requiring refunds under particular circumstances. The court held that because ratemaking was a legislative function which had been broadly delegated to the Commission to perform, the Commission was not limited in its discretion to require the disgorgement of over-collected revenues from ratepayers, nor was the Commission engaged in "retroactive ratemaking" as it was not ordering the company to refund past profits. The court stated that to hold that the commission does not have the power to order such a refund would deprive it of much of its power to protect customers from abusive delay tactics or unexpectedly long delays in implementing an ordered revenue reduction.

The Attorney General's Office has advised the Commission that if it denied an affiliated interest application or approved the application with certain conditions that necessitated a change in accounting treatment, it could order the utility to make adjusting entries on its books. Letter to Rick Elliott, Administrator, Financial Analysis Division, from Larry D. Thomson, Chief Counsel, General Counsel Division, Or. Op. Atty. Gen. OP-5975 (April 30, 1986). The Commission has the right, and the duty, to exercise its authority to set just and reasonable rates for protection of customers, even to the extent of modifying terms of contracts entered into by a regulated utility. American Can Co. v. Davis, 28 Or App 207, 224, 559 P.2d 898, rev denied, 278 Or 393 (1977).

Oregon ratepayers have not been afforded an opportunity to engage in a public debate of whether the Tax Allocation Agreement was in the public interest. Oregon ratepayers were deprived of the opportunity to assert that PGE's actual tax liability was zero during Enron's ownership, as it unquestionably was during the years when consolidated tax filings occurred, to

assert that a new rate case should have been opened, or to assert that Enron was using the Tax Allocation Agreement as a vehicle to avoid limitations upon cash distributions to the holding company.

Cash payments made by PGE to Enron under oral and written Tax Allocation Agreements, and not otherwise explicitly authorized by the Commission from 1997 through 2006, should be refunded to ratepayers through billing credits.

3. PGE should undertake practical and prudent tax planning methods to reduce income tax burdens upon ratepayers.

In its rate filings, PGE has asked the Commission to adopt a combined corporate tax rate of 39%. PGE has identified this number as its current effective, cumulative federal and state corporate tax rate, unchanged from that applied in UE 115. See, UE 180/PGE 200/Tinker-Tooman/13-14.[6] As indicated by ORS 757.210(1)(a):

> The legislative intent behind SB 408 is clear – [the Commission is] to depart from historic practice and consider taxes paid by a utility or its parent when setting rates. When [the Commission] authorize[s] rates for utilities covered by the bill, those rates must reflect the taxes paid to units of government in order to be fair, just and reasonable.

Pacific Power & Light Co. Request for a General Rate Increase, UE 170, Order No. 05-1050 at 18 (September 28, 2005), adhered to on reconsideration, Order No. 06-379 (July 10, 2006).

[6] "A company's effective tax rate is the ratio of its income tax expense (cash and deferred tax) to its pre-tax earnings. It typically differs substantially from the statutory tax rate in the company's reporting jurisdiction." Robert S. McIntyre and Coo Nguyen, Corporate Income Taxes in the Bush Years (Citizens for Tax Justice and the Institute on Taxation and Economic Policy, September 2004) (available on the Internet at http://www.ctj.org/corpfed04an.pdf) According to the study's authors, the effective corporate tax rate for the predominant utilities in the United States was in the range of 14.4% after taking into account various tax breaks and benefits. Id., at p. 31.

Setting aside for now the question of whether the percentage identified by PGE is "fair, just and reasonable",[7] the City believes that it would be appropriate for the Commission to be informed about PGE's efforts to undertake practical and prudent tax planning methods. As noted in the City's testimony, SB 408 has fundamentally changed the former paradigm for utility taxes, where avoided taxes "resulted in additional income to PGE, up to the amount established in its electricity rates approved by the Commission. Now, PGE doesn't gain the use of any taxes that it avoids. The tax savings are merely a pass-through to customers." COP/100/Jubb/4.[8]

PGE responds by arguing that SB 408 did not change "PGE's basic incentive with regard to tax planning." UE 180/PGE 1700/Piro-Tamlyn /4. PGE mischaracterizes the City's concerns. PGE's future incentive will be to aim for the effective tax rate, as authorized by the Commission in this proceeding. To the extent that there are beneficial tax avoidance mechanisms that might be implemented in any given year, PGE will have an economic incentive not to employ them if the effect will be to go below the approved tax rate and have to share those benefits with the ratepayers, "rolling the corresponding deduction into a subsequent year". COP 100/Jubb/4.

[7] Kelly, J, "IOUs tax records refute their claims", 42 Public Power 5 (September 1, 1984) (Describing study of reports filed by investor-owned utilities with FERC, representing over 90 percent of the electric revenues of all private electric utilities, indicated that federal income taxes were only 7.5 percent of 1981 before-tax incomes.)

[8] Not so long ago, PGE was arguing that "it would work against legislative goals of accuracy and fairness to use an effective tax rate based on old test year results. The purpose of [SB 408] is to account for, on an annual basis, actual amounts collected by the utility for taxes." Opening Comments of Portland General Electric Company Regarding Interpretation of SB 408 Section 3(13)(e), page 5 (November 5, 2005). PGE's position is in alignment with decisions made by approximately 25% of the state utility commissions. These commissions have previously considered and ruled that utility rates must reflect actual tax liabilities as operating expenses, including New Jersey, Pennsylvania, New York, Arkansas, Mississippi, Connecticut, Vermont, Rhode Island, West Virginia, Maine, Minnesota, Indiana, Illinois, the District of Columbia, as noted by the Texas Public Utility Commission in a compilation in its decision of In re El Paso Elec. Co., 14 Tex. P.U.C. Bull. 2834, 1989 WL 625088, *183 n. 1 (May 5, 1989).

PGE admits that "SB 408 already requires PGE to file an annual tax report with the Commission on October 15 of each year". UE 180/PGE 1700/Piro-Tamlyn/5. Given this, at a minimum the Commission should commit to actively monitoring PGE's effective tax rates to determine if the percentage identified by PGE in this proceeding is appropriate. This monitoring would be in keeping with the Commission's duties to "keep informed as to the manner and method in which [the management of the public utility] are conducted". ORS 756.070. It is not enough to have over-collected taxes returned year after year to ratepayers. The Commission should proactively protect ratepayers from such "unreasonable exactions" in the first instance. ORS 756.040.

4. PGE's deferred income taxes should be refunded to ratepayers over the reversal period of the specific temporary differences that created the deferred taxes.

The City's testimony noted that PGE carried approximately $280 million in deferred income taxes on its financial statements as of January 1, 2006. COP/100/Jubb/10. In its rebuttal, PGE did not dispute the City's calculation of the amount of deferred taxes. The City's testimony identified how, as deferred taxes become currently payable, they would then be included in taxes paid to governments under the SB 408 true up process. COP/100/Jubb/10-11. PGE disputes this, but relies merely on the broad concept that this is not allowed under "cost of service ratemaking". UE 180/PGE 1700/Piro-Tamlyn /16. The City's point is that as deferred taxes become due, they will then be included in the calculation of the current and owing taxes under SB 408, causing an increase in overall tax obligations for the utility. Income taxes previously included in PGE rates and reflected as deferred taxes on the PGE balance sheet as of January 1, 2006 should be refunded as billing credits to ratepayers in order to avoid double charging ratepayers for

those taxes when the temporary differences that created the deferred tax liabilities reverse and become currently payable income tax liabilities.

CONCLUSION

The City of Portland respectfully requests that the Commission consider its requests and grant the identified relief.

DATED this 17th day of November, 2006

/s/ Benjamin Walters

Benjamin Walters, OSB #85354
Senior Deputy City Attorney
Of Attorneys for City of Portland

CERTIFICATE OF SERVICE

I hereby certify that on November 17, 2006, I mailed an original and five copies of the foregoing OPENING BRIEF OF THE CITY OF PORTLAND, OREGON to:

PUBLIC UTILITY COMMISSION OF OREGON
ATTENTION: FILING CENTER
550 CAPITOL ST., NE., SUITE 215
PO BOX 2148
SALEM, OR 97308-2148

and on November 17, 2006, I hereby certify that the foregoing document was electronically mailed to all persons on the Service List maintained by the Public Utility Commission for the related UE 180, UE 181 and UE 184 proceedings who had an e-mail address posted. I further certify that for those persons on the Service List who were not identified as having an e-mail address, a copy was sent by first class mail, contained in a sealed envelope, with postage paid, and deposited in the post office at Portland, Oregon on said day.

/s/ Benjamin Walters
Benjamin Walters, OSB #85354
Senior Deputy City Attorney
Of Attorneys for City of Portland

CITY OF
PORTLAND, OREGON
OFFICE OF CITY ATTORNEY

Linda Meng, City Attorney
1221 S.W. 4th Avenue, Suite 430
Portland, Oregon 97204
Telephone: (503) 823-4047
Fax No.: (503) 823-3089

November 17, 2006

BY E-MAIL AND FIRST CLASS MAIL

PUBLIC UTILITY COMMISSION
ATTN: FILING CENTER
550 CAPITOL ST, NE #215
PO BOX 2148
SALEM OR 97308-2148

Re: **Docket UE 180/UE 181/UE 184:** In the Matter of PGE's Request for a General Rate Revision

Dear Filing Center:

Enclosed for filing is the original and five copies of the City of Portland's Opening Brief in the above-referenced matter. I served a copy on all parties via e-mail on this date.

Very truly yours,

Benjamin Walters

Benjamin Walters
Senior Deputy City Attorney

BW:lw
Enclosures
c: Service List (by e-mail)

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UE 180 - SERVICE LIST

JIM DEASON **(C)**
ATTORNEY AT LAW
1 SW COLUMBIA ST, SUITE 1600
PORTLAND OR 97258-2014
jimdeason@comcast.net

ROBERT VALDEZ
PO BOX 2148
SALEM OR 97308-2148
bob.valdez@state.or.us

AF LEGAL & CONSULTING SERVICES

ANN L FISHER **(C)**
ATTORNEY AT LAW
PO BOX 25302
PORTLAND OR 97298-0302
energlaw@aol.com

BOEHM KURTZ & LOWRY

KURT J BOEHM **(C)**
ATTORNEY
36 E SEVENTH ST - STE 1510
CINCINNATI OH 45202
kboehm@bkllawfirm.com

MICHAEL L KURTZ **(C)**
36 E 7TH ST STE 1510
CINCINNATI OH 45202-4454
mkurtz@bkllawfirm.com

BONNEVILLE POWER ADMINISTRATION

GEOFFREY M KRONICK LC7 **(C)**
PO BOX 3621
PORTLAND OR 97208-3621
gmkronick@bpa.gov

CRAIG SMITH
PO BOX 3621--L7
PORTLAND OR 97208-3621
cmsmith@bpa.gov

BRUBAKER & ASSOCIATES INC

JAMES T SELECKY **(C)**
1215 FERN RIDGE PKWY - STE 208
ST. LOUIS MO 63141
jtselecky@consultbai.com

CABLE HUSTON BENEDICT HAAGENSEN & LLOYD LLP

TAMARA FAUCETTE
1001 SW 5TH AVE STE 2000
PORTLAND OR 97204
tfaucette@chbh.com

CHAD M STOKES
1001 SW 5TH - STE 2000
PORTLAND OR 97204
cstokes@chbh.com

CITIZENS' UTILITY BOARD OF OREGON

LOWREY R BROWN **(C)**
UTILITY ANALYST
610 SW BROADWAY - STE 308
PORTLAND OR 97205
lowrey@oregoncub.org

JASON EISDORFER **(C)**
ENERGY PROGRAM DIRECTOR
610 SW BROADWAY STE 308
PORTLAND OR 97205
jason@oregoncub.org

COMMUNITY ACTION DIRECTORS OF OREGON

JIM ABRAHAMSON **(C)**
COORDINATOR
PO BOX 7964
SALEM OR 97301
jim@cado-oregon.org

CONSTELLATION NEWENERGY INC

WILLIAM H CHEN
REGULATORY CONTACT
2175 N CALIFORNIA BLVD STE 300
WALNUT CREEK CA 94596
bill.chen@constellation.com

DANIEL W MEEK ATTORNEY AT LAW

DANIEL W MEEK **(C)**
ATTORNEY AT LAW
10949 SW 4TH AVE
PORTLAND OR 97219
dan@meek.net

DAVISON VAN CLEVE PC

S BRADLEY VAN CLEVE **(C)**
333 SW TAYLOR - STE 400
PORTLAND OR 97204
mail@dvclaw.com

DEPARTMENT OF JUSTICE

STEPHANIE S ANDRUS **(C)**
ASSISTANT ATTORNEY GENERAL
REGULATED UTILITY & BUSINESS SECTION
1162 COURT ST NE
SALEM OR 97301-4096
stephanie.andrus@state.or.us

EPCOR MERCHANT & CAPITAL (US) INC

LORNE WHITTLES
MGR - PNW MARKETING
1161 W RIVER ST STE 250
BOISE ID 83702
lwhittles@epcor.ca

GRESHAM CITY ATTORNEY'S OFFICE

DAVID R RIS
SR. ASST. CITY ATTORNEY
CITY OF GRESHAM
1333 NW EASTMAN PARKWAY
GRESHAM OR 97030
david.ris@ci.gresham.or.us

GRESHAM CITY OF

JOHN HARRIS **(C)**
TRANSPORTATION OPERATIONS SUPERINTENDENT
1333 NW EASTMAN PKWY
GRESHAM OR 97030
john.harris@ci.gresham.or.us

KAFOURY & MCDOUGAL

LINDA K WILLIAMS **(C)**
ATTORNEY AT LAW
10266 SW LANCASTER RD
PORTLAND OR 97219-6305
linda@lindawilliams.net

LEAGUE OF OREGON CITIES

ANDREA FOGUE **(C)**
SENIOR STAFF ASSOCIATE
PO BOX 928
1201 COURT ST NE STE 200
SALEM OR 97308
afogue@orcities.org

MCDOWELL & ASSOCIATES PC

KATHERINE A MCDOWELL
ATTORNEY
520 SW SIXTH AVE - SUITE 830
PORTLAND OR 97204
katherine@mcd-law.com

NORTHWEST ECONOMIC RESEARCH INC

LON L PETERS **(C)**
607 SE MANCHESTER PLACE
PORTLAND OR 97202
lpeters@pacifier.com

NORTHWEST NATURAL

ELISA M LARSON **(C)**
ASSOCIATE COUNSEL
220 NW 2ND AVE
PORTLAND OR 97209
elisa.larson@nwnatural.com

NORTHWEST NATURAL GAS COMPANY

ALEX MILLER **(C)**
DIRECTOR - REGULATORY AFFAIRS
220 NW SECOND AVE
PORTLAND OR 97209-3991
alex.miller@nwnatural.com

PACIFICORP

LAURA BEANE
MANAGER - REGULATORY
825 MULTNOMAH STE 2000
PORTLAND OR 97232
laura.beane@pacificorp.com

PORTLAND CITY OF - OFFICE OF TRANSPORTATION

RICHARD GRAY **(C)**
STRATEGIC PROJECTS MGR/SMIF ADMINISTRATOR
1120 SW 5TH AVE RM 800
PORTLAND OR 97204
richard.gray@pdxtrans.org

PORTLAND CITY OF ENERGY OFFICE

DAVID TOOZE
SENIOR ENERGY SPECIALIST

721 NW 9TH AVE -- SUITE 350
PORTLAND OR 97209-3447
dtooze@ci.portland.or.us

PORTLAND GENERAL ELECTRIC

PGE- OPUC FILINGS
RATES & REGULATORY AFFAIRS

RATES & REGULATORY AFFAIRS
121 SW SALMON ST 1WTC0702
PORTLAND OR 97204
pge.opuc.filings@pgn.com

DOUGLAS C TINGEY **(C)**
ASST GENERAL COUNSEL

121 SW SALMON 1WTC13
PORTLAND OR 97204
doug.tingey@pgn.com

PRESTON GATES ELLIS LLP

HARVARD P SPIGAL
ATTORNEY AT LAW

222 SW COLUMBIA ST STE 1400
PORTLAND OR 97201-6632
hspigal@prestongates.com

SEMPRA GLOBAL

THEODORE E ROBERTS

101 ASH ST HQ 13D
SAN DIEGO CA 92101-3017
troberts@sempra.com

LINDA WRAZEN

101 ASH ST HQ8C
SAN DIEGO CA 92101-3017
lwrazen@sempraglobal.com

SMIGEL ANDERSON & SACKS

SCOTT H DEBROFF

RIVER CHASE OFFICE CENTER
4431 NORTH FRONT ST
HARRISBURG PA 17110
sdebroff@sasllp.com