

1 **BEFORE THE PUBLIC UTILITY COMMISSION**
2 **OF OREGON**

3 UM 1909

4 In the Matter of

5 PUBLIC UTILITY COMMISSION OF
6 OREGON

STAFF'S CLOSING BRIEF

7 Investigation of the Scope of the
8 Commission's Authority to Defer Capital
Costs

9 **I. INTRODUCTION**

10 This docket seeks to answer two questions. First, whether the Commission has the legal
11 authority pursuant to ORS 757.259(2)(e) to defer the revenue requirement effects of a utility's
12 capital investment, which includes a utility's return *on* investment. Second, if the answer is yes
13 for some or all of components of the utility's revenue requirement related to a capital project,
14 whether the Commission should authorize such deferrals as a matter of policy. All parties agree
15 that in order to address the first question as to what may or may not legally be included in a
16 deferral pursuant to ORS 757.259(2)(e), the Commission must undertake a statutory construction
17 analysis, and that the statute must contain operative language to support any potential legislative
18 intent.

19 Joint Utilities' arguments purport to provide a streamlined way forward for the deferral of
20 capital costs, including return *on* utility investment, but their arguments are unsupported by the
21 plain language of the statute. Moreover, the Joint Utilities' proposed definitions of "revenues"
22 and "expenses" lead to absurd and unsupportable results, and ignore conflicting legislative
23 history.

24 The plain text and context of the statute make clear that neither "revenues" nor
25 "expenses" in subsection (2)(e) provide the Commission with the legal authority to defer a
26 utility's return *on* investment, a conclusion which is also supported by sound policy. Therefore,

1 Staff continues to recommend that the Commission find it does not have the legal authority to
2 defer the return *on* a utility’s capital investment. Staff also continues to recommend that the
3 Commission adopt a general policy against deferral of return *of* utility investment. Doing so
4 preserves longstanding ratemaking incentives and policies.

5 **II. ARGUMENT**

6 **(A) The plain language of ORS 757.259 does not provide the Commission with authority**
7 **to authorize deferrals for the return *on* a utility’s capital investment.**

8 The purpose of a statutory construction analysis is set forth in ORS 174.010, which
9 provides “[i]n the construction of a statute, the office of the judge is simply to ascertain what is,
10 in terms or in substance, contained therein, not to insert what has been omitted, or to omit what
11 has been inserted; and where there are several provisions or particulars such construction is, if
12 possible, to be adopted as will give effect to all.” To do this, courts review the text, context and
13 legislative history of the statute in question.¹

14 The most logical and supportable construction of “revenues” and “expenses” is to define
15 them as they are used for ratemaking purposes, as Staff and Joint Intervenors have advocated.
16 This is the most aligned with how ratemaking statutes have been construed by courts, the general
17 discussion in the legislature, and it preserves traditional ratemaking principles.

18 1. For purposes of ORS 757.259(2)(e), “expenses” do not include a utility’s return *on*
19 *capital investment*.

20 In relevant part, ORS 757.259(2)(e) provides the Commission with the authority to
21 authorize the deferral of “identifiable utility *expenses* or *revenues*, the recovery or refund of
22 which the commission finds should be deferred in order to minimize the frequency of rate
23 changes or the fluctuation of rate levels or to match appropriately the costs borne by and the
24 benefits received by ratepayers.”²

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26 ¹ *State v. Gaines*, 346 Or 160 (2009).

² Emphasis added.

1 Joint Utilities argue that “a plain reading of the statute supports deferral of the revenue
2 requirement effect of capital investment, as a reflection of the financial costs inherent in
3 providing utility service.”³ In reaching this conclusion, Joint Utilities argue that the dictionary
4 definition of “expenses” should be applied,⁴ and argue that a utility’s return *on* investment meets
5 that definition. As expanded upon below, Joint Utilities’ position is inconsistent with court
6 precedent construing ratemaking terms as terms of art, fails to give effect to all provisions of the
7 deferral statute, and is inconsistent with legislative history. As Staff argued in its opening brief,
8 “expenses” and “revenues” are terms of art in utility ratemaking, and should be interpreted
9 accordingly.⁵

10 *i. “Revenues” and “expenses” are terms of art and should be interpreted accordingly.*

11 As briefed by the parties in this proceeding, “revenues” and “expenses” are inexact terms
12 which must be construed in accordance with the policy that the word or phrase is trying to
13 convey.⁶ As Staff and Joint Intervenors have briefed, “revenues” and “expenses” are
14 appropriately construed within the ratemaking context—as those terms are used by the
15 Commission in setting rates.

16 Courts have acknowledged that terms within ratemaking statutes are appropriately
17 considered “terms of art.” In *Citizens’ Utility Board v. Public Utility Com’n of Oregon*, the
18 Oregon Court of Appeals acknowledged that “rate base” was a term of art in utility ratemaking
19 and construed the statutes in question consistently with ratemaking principles.⁷ In *Beaver Creek*
20 *Co-Op. Tel. v. Public Utility Com’n*, the Oregon Court of Appeals addressed the use of terms of
21 art in the utility context, noting that well-established definitions in the public utility context are

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23 ³ Joint Utilities’ Opening Brief at 9.

24 ⁴ Joint Utilities’ Opening Brief at 9.

25 ⁵ Staff’s Opening Brief at 3-4.

26 ⁶ Staff’s Opening Brief at 3; Joint Utilities’ Opening Brief at 5-6; Joint Intervenors’ Opening Brief at 3.

⁷ *Citizens’ Utility Bd. of Oregon v. Public Utility Com’n of Oregon*, 154 Or App 702, 709-711 (1998).

1 appropriately construed as terms of art.⁸ Finally, in *Oregon Trail Elec. Consumers Co-op, Inc. v.*
2 *Co-Gen Co.*, the Oregon Court of Appeals noted that “contractual language in such specialized
3 or highly technical areas often reflects terms of art and usages that have particular meaning to
4 those in the field,” in addressing a PURPA issue.⁹ Joint Utilities’ reliance on the Court of
5 Appeals’ use of the term “costs” interchangeably with “expenses” in reference to the deferral
6 statute is misplaced. The Court was not interpreting the meaning of “expenses” in either case,
7 nor did it offer any indication about the appropriate definitions, or whether a utility’s rate of
8 return was considered an “expense” for purposes of ORS 757.259(2)(e).¹⁰

9 It is also clear that Oregon courts interpret ratemaking statutes within the existing
10 ratemaking context.¹¹ For example, in *Industrial Customers of Northwest Utilities v. Public*
11 *Utility Com’n of Oregon*,¹² the Court of Appeals begins its analysis by stating “[t]o place the
12 facts of this case in context, a brief discussion of the general legal principles in place is helpful”
13 and then goes on to describe the ratemaking context in which rates are set.¹³ In *Gearhart v.*
14 *Public Utility Com’n of Oregon*, the Oregon Court of Appeals stated “[w]e begin with a brief
15 overview of utility ratemaking, which is at the heart of this dispute. The following basic
16 principles concerning the PUC and ratemaking provide needed context for an understanding of
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⁸ *Beaver Creek Co-Op. Tel. v. Public Utility Com’n*, 182 Or App 559, 572 (2002).

20 ⁹ *Oregon Trail Elec. Consumers Co-op v. Co-Gen Co.*, 168 Or App 466, 477-478 (2000).

21 ¹⁰ Joint Utilities’ Opening Brief at 23, citing *Indus. Customers of Northwest Utilities v. Public*
22 *Utility Com’n of Oregon*, 196 Or App 46 (2004) and *Utility Reform Project v. Public Utility*
Com’n of Oregon, 261 Or App 388 (2014).

23 ¹¹ See *State v. Ofodrinwa*, 353 Or 507, 512 (2013) (“The context for interpreting a statute’s text
includes...the statutory framework within which the law was enacted.”).

24 ¹² *Industrial Customers of Northwest Utilities*, 196 Or App at 49.

25 ¹³ See also *Gearhart v. Public Utility Com’n of Oregon*, 255 Or App 58, 60 (2013) (“We begin
26 with a brief overview of utility ratemaking, which is at the heart of this dispute. The following
basic principles concerning the PUC and ratemaking provide needed context for an
understanding of this history of this dispute, and as we later discuss, they, in part, ground our
holding in this case.”).

1 this history of this dispute, and as we later discuss, they, in part, ground our holding in this
2 case.”¹⁴

3 Moreover, it is also incontrovertible that the legislature itself intended the terms and
4 grants of authority within the deferral statute to be construed consistently with how the terms are
5 used and understood in ratemaking. First, the glossary of terms included in the legislative
6 history were provided in direct response to requests from the House Environment & Energy
7 Committee to have definitions of significant terms used in the context of this legislation—in an
8 effort to understand how they would be construed by the Commission once the statute was
9 enacted.¹⁵

10 Second, the definitions provided were *ratemaking* definitions, not accounting definitions
11 and not from a standard dictionary. Some terms were defined in a memorandum from the
12 Commission, with the subject “Glossary of Terms – HB 2145.”¹⁶ Attached to this memorandum
13 are photocopied pages from the Public Utilities Manual published by Deloitte Haskins & Sells.¹⁷
14 “Accounting – Ratemaking,” is defined as “[f]or a regulated company, accounting practices and
15 entries are largely controlled by the ratemaking treatment. Ratemaking decisions can create
16 assets and liabilities by postponement of recognition of transactions which would enter into the
17 determination of income for a non-regulated firm in one period or at an earlier time.”¹⁸ There is
18 simply no indication in the legislative history that statutory terms were intended to be construed
19 in any manner other than consistent with how they are used to set rates.

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23 ¹⁴ *Gearhart*, 255 Or App at 60 (2013).

24 ¹⁵ March 25, 1987 Public Hearing on HB 2145 before House Environment and Energy
25 Committee, Audio Tape 73, Side A; HB 2145 House Environment and Energy Committee -
26 Exhibit F.

27 ¹⁶ HB 2145 House Environment and Energy Committee - Exhibit F.

28 ¹⁷ *Id.*

¹⁸ *Id.*

1 ii. A utility's "rate of return" is not an expense for ratemaking purposes.

2 Joint Utilities' position is that "'revenues' and 'expenses' represent two sides of a
3 comprehensive financial assessment, with expenses constituting outflows and revenues
4 constituting inflows."¹⁹ Joint Utilities' argument rests on the concept that "[c]apital costs are
5 part of the expense of providing utility service—expenses for which revenues are required,"²⁰
6 and that the dictionary definition of "expenses" should be applied when construing the statute in
7 order to achieve this concept.²¹ Their preferred definition of "expense" is one in which the terms
8 is construed as a synonym of "costs."²² As expressed in an equation: Revenues = Expenses.
9 Revenues would represent the amounts necessary to be collected in rates from customers as well
10 as "other revenues," and Expenses would include all operations and maintenance costs, taxes,
11 depreciation, as well as the utility's cost of capital.²³ Joint Utilities go on to argue that even
12 "[a]ccounting and regulatory definitions of 'expenses' encompass all costs necessary to supply
13 utility service—including the cost of obtaining capital."²⁴ Joint Utilities construction of the
14 terms "revenues" and "expenses" pursuant to ORS 757.259 is, however, unpersuasive and
15 unsupportable for several reasons.

16 First, Joint Utilities' argument is divorced from the way that rates are set. Equations
17 aside, as succinctly stated by the Oregon Court of Appeals:

18 Generally speaking, the utility's revenue requirement is determined prospectively,
19 by examining a future test period to determine: (1) the utility's allowable
20 operating expenses, including taxes, maintenance, and depreciation; to which is
21 added (2) the utility's investment in property used to provide utility services less
22 depreciation, representing the utility's "rate base" upon which a return may be
23 earned; and (3) a rate of return that should be applied to the rate base to establish
24 the return to which the utility's investors are reasonably entitled. A.J. Gustin

23 ¹⁹ Joint Utilities' Opening Brief at 20.

24 ²⁰ *Id.* at 6.

25 ²¹ *Id.* at 9.

26 ²² *Id.*

²³ *Id.* at 20.

²⁴ *Id.* at 17.

Priest, *1 Principles of Public Utility Regulation: Theory and Application*
1 *Principles of Public Utility Regulation*, 45 (1969).²⁵

2 The effect of Joint Utilities' over-simplification is not without consequence—in arguing that
3 “expenses” include all “outflows” from the utility, Joint Utilities seek to re-define how
4 “revenues” and “expenses” are construed for ratemaking purposes within the deferral context.
5 There is no indication that the legislature intended one set of ratemaking definitions to apply in
6 general rate cases or other ratemaking proceedings, and another to apply to deferrals.

7 Regarding “expenses,” Joint Utilities' argument ignores the difference between the
8 standard applicable to a utility's return *on* investment compared to the recovery of “expenses,”
9 such as wages, fuel, maintenance and taxes. In ratemaking, a utility's revenue requirement
10 represents “the amount of money the utility must collect to cover its reasonable operating
11 expenses incurred in providing service, as well as a reasonable return *on* investments made to
12 provide that service.”²⁶ A utility's rate of return “reflects the risks of recovery that the utility
13 confronts trying to collect its revenue requirement.”²⁷ Though not on a dollar-for-dollar basis, a
14 utility is entitled to recovery of its prudently incurred costs, whereas a utility is afforded an
15 *opportunity* to recover its rate of return.²⁸ Regarding the utility's rate of return, as succinctly
16 stated by the Oregon Court of Appeals:

17 The rate of return is inherently a judgment call. The factors that go into
18 consideration of the rate of return include capital costs and the requirement
19 that the return to investors be commensurate with returns on other investments
subject to similar risk and sufficient to ensure the financial viability of the
business...a utility cannot be guaranteed a particular return on investment.²⁹

20 This difference between a utility's expenses and cost of capital is also borne out in other
21 ratemaking statutes. Pursuant to ORS 757.355 and ORS 757.140, when a utility retires plant
22 prior to its full recovery in rates, a utility retains its ability to recover its return *of* undepreciated

23 ²⁵ *Gearhart*, 255 Or App at 62 (2013).

24 ²⁶ *Id.* at 61 (citing to ORS 756.040(1)).

25 ²⁷ *In re Public Utility Com'n of Oregon*, OPUC Docket No. 1147, Order No. 06-507 at 5 (Sept.
6, 2006).

26 ²⁸ *Gearhart v. Public Utility Com'n of Oregon*, 356 Or 216, 220-221 (2014).

²⁹ *Gearhart*, 255 Or App at 62 (internal citations omitted).

1 investment assuming statutory requirements are met, but is no longer permitted to earn a return
2 on its investment.³⁰ Additionally, deferral of a utility's cost of capital effectively provides the
3 utility with a guarantee of cost recovery—something not afforded under traditional ratemaking.
4 There is no indication in the legislative history—either by legislators or by proponents of the
5 bill—to upend traditional ratemaking principles through the passage of the deferral statute.

6 Regarding “revenues,” Joint Utilities’ definition would allow for customer revenues (i.e.
7 rates paid by customers) to be deferred, which is unsupported by the legislative history,³¹ is
8 legally questionable,³² and is unsupported by sound policy.³³ While customer revenues represent
9 an inflow to the utility, these are not the same as revenues that are used in setting rates. Going
10 back to the general ratemaking equation, $R = E + (V-D)r$,³⁴ revenues from non-customers are
11 included because they offset the utility’s revenue requirement (R)—these “benefits” to customers
12 are the type of revenues that were discussed in the legislature.³⁵ Once the revenue requirement is

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14 ³⁰ See also *Citizens’ Utility Bd. of Oregon*, 154 Or App at 714 (1998).

15 ³¹ March 11, 1987 Public Hearing on HB 2145 before House Environment and Energy
16 Committee, Audio Tape 56, Side B. As discussed below, changes in cost of capital and changes
17 in load were not intended to be covered by the statute. Also, as Joint Utilities point out, the
18 intent of the statute was to provide authorization to the Commission for its current practice of
19 deferrals—and not to go beyond what the Commission was already doing. Joint Utilities’
20 Opening Brief at 11-12 (citing *Hearing on HB 2145 Before the H. Environment and Energy
Committee*, Tape 57, Side A at 15:55-16:12 (Mar. 11, 1987)).

21 ³² Or. Op. Atty. Gen. OP-6076 (Or.A.G.), 1987 WL 278316 at 5 (“[R]atepayers’ constitutional
22 rights may be violated if ratepayers are required to pay in the future a surcharge for services they
23 used under lawful rates. Such a surcharge may deprive ratepayers of property without due
24 process or violate the contracts clause of the United States or Oregon Constitution.”) (internal
25 citations omitted).

26 ³³ As succinctly stated in Attorney General Opinion 6076, “Revenue adjustments are the precise
evil against which the rule against retroactive ratemaking protects. Under that rule, if actual
revenues fall short of predictions, the utility must bear that loss. If actual revenues exceed
predictions, the utility is permitted to retain that excess profit. Thus, the utility is encouraged to
operate efficiently.” Or. Op. Atty. Gen. OP-6076 (Or.A.G.), 1987 WL 278316 at 14-15.

³⁴ *Gearhart*, 356 Or at 220.

³⁵ Staff’s Opening Brief at 6; Joint Utilities’ Opening Brief at footnote 49; see also HB 2145
Senate Business, Housing and Finance Committee - Exhibit D (referring to Attachment 2, which
is illustrative of the types of circumstances under which deferred accounts had been created. The
“Summary List as of December 31, 1986,” has a list of accounts, by category, of deferral
accounts, including offsets to the utility’s revenue requirement by certain property sales deferrals
and utility commitments for rate reductions.).

1 determined, rates are then designed in order to allow the utility to collect that revenue
2 requirement from customers.

3 *iii. Joint Utilities' proposed definition of "expenses" is inconsistent with legislative*
4 *history indicating that a utility's return on investment was not intended to be subject*
5 *to deferral.*

6 In arguing that a utility's rate of return is appropriately deferred pursuant to ORS
7 757.259(2)(e), the Joint Utilities fail to acknowledge and address legislative history regarding
8 deferral of a utility's cost of capital. At the March 11, 1987 House Environment & Energy
9 Committee public hearing for HB 2145, Commissioner Davis discussed the purpose and
10 intended function of the legislation. In discussing what utility expenses or revenues would be
11 subject to deferral under the currently numbered subsection (2)(e), Commissioner Davis
12 explained that the intent of now current subsection (2)(e) was to "cover[] the many occasions
13 when legitimate ratemaking expense item is changing and the PUC believes rate changes should
14 take place at some subsequent time."³⁶ Representative Eachus asked whether the legislation was
15 intended to cover reductions in load or reductions in the costs of capital.³⁷ Commissioner Davis
16 responded that the Commission had never deferred anything of that nature simply because it is
17 part of a general rate case.³⁸ Representative Eachus then asked for an explanation of the
18 difference between a deferral for a reduction in the utility's cost of capital and something like
19 Colstrip 4.³⁹ In response, Commissioner Davis explained that it was a question of magnitude and
20 the number of rate changes seen by consumers, and that capital changes and load changes are
21 rather "amorphous" items.⁴⁰ This is a clear indication that a utility's rate of return was not
22 intended to be construed as an "expense" or "revenue" subject to deferral—despite discussion
23 that deferrals were intended to cover plants such as Colstrip 4.

23 ³⁶ March 11, 1987 Public Hearing on HB 2145 before House Environment and Energy
24 Committee, Audio Tape 57, Side A at 17:33.

25 ³⁷ *Id.* at 25:26.

26 ³⁸ *Id.* at 25:46.

27 ³⁹ *Id.* at 26:00.

28 ⁴⁰ *Id.* at 26:15.

1 2. Operative language is required in order to give life to legislative intent.

2 The operative language of the statute does not provide the Commission with discretion to
3 defer a utility's return *on* investment. Joint Utilities spend ample pages discussing the legislative
4 history, seemingly arguing that the legislative history establishes ambiguity in the plain and
5 unambiguous text of the statute. However, the text and context "must be given primary weight
6 in the analysis."⁴¹ As the Court explained in *Gaines*, "[t]he formal requirements of lawmaking
7 produce the best source from which to discern the legislature's intent, for it is not the intent of
8 the individual legislators that governs, but the intent of the legislature as formally enacted into
9 law."⁴²

10 Review of legislative history in a statutory construction analysis may aid a court to the
11 extent that the statute contains language that, when reasonably construed, is capable of
12 effectuating what the legislative history reveals was intended.⁴³ In this case, legislative history
13 was inconsistent—when deferral of a utility's rate of return was discussed on a stand-alone basis,
14 the answer was no;⁴⁴ this is in conflict with statement indicating an intent to defer the revenue
15 requirement effects of capital projects, which includes the utility's rate of return.⁴⁵

16 Joint Utilities may argue that the Commission should nevertheless authorize the deferral
17 of a utility's return *on* investment in only the limited circumstance of capital investments, but
18 this distinction does not bear out in the plain language of the statute as it contains no such
19 exception. There is no operative language that would allow "expenses" to be defined as
20 inclusive of a utility's rate of return when capital costs are at issue, but not included on a
21 standalone basis. The same argument is true for "revenues"—there is no basis in the plain
22 language of the statute to support the conclusion that customer revenues, generally, were not

23 ⁴¹ *Hoekstre v. DLCD*, 249 Or App 626, 634, *rev den*, 352 Or 377 (2012).

24 ⁴² *Gaines*, 346 Or at 171.

25 ⁴³ *Id.* at 172-173.

26 ⁴⁴ March 11, 1987 Public Hearing on HB 2145 before House Environment and Energy
Committee, Audio Tape 57, Side A at 25:26.

⁴⁵ Joint Utilities' Opening Brief at 14-16.

1 intended to be deferred, but that deferral of other types of revenues would be permissible. To
2 read these distinctions into the plain language of the statute would be to “insert what has been
3 omitted,” which is impermissible.⁴⁶

4 **(B) The Commission should adopt a policy against authorizing deferrals for return of**
5 **utility capital investments.**

6 Staff continues to find that in addition to the legal reasons discussed in its opening brief
7 and in this closing brief, policy considerations weigh against deferral of the revenue requirement
8 effects of a capital investment. As argued in Staff’s opening brief, deferral of the utility’s
9 revenue requirement effects would allow the utility to earn a higher return *on* capital projects
10 than would be permitted under standard ratemaking.⁴⁷ Additionally, deferrals represent
11 extraordinary ratemaking treatment whose use should be limited and there are other ratemaking
12 alternatives to deferrals that are better suited for capital costs.⁴⁸ Joint Intervenors also articulated
13 compelling policy reasons that weigh against the use of deferrals for capital investments.⁴⁹
14 Importantly, no party has disputed that deferrals constitute extraordinary ratemaking treatment,
15 are a matter of Commission discretion, or that under traditional ratemaking, utilities generally
16 recover capital costs associated with new projects through general rate case proceedings.⁵⁰

17 In arguing for the use of deferrals for capital investments, Joint Utilities make a number
18 of assertions that bear further discussion. First, Joint Utilities argue that it is reasonable to earn
19 its authorized rate of return *on* deferred amounts that include the utility’s calculated rate of return

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21 ⁴⁶ ORS 174.010.

22 ⁴⁷ Staff’s Opening Brief at 9.

23 ⁴⁸ *Id.* at 9-13.

24 ⁴⁹ Joint Intervenors’ Opening Brief at 5-12.

25 ⁵⁰ Staff understands that capital costs for some Renewable Portfolio Standard compliant
26 resources may be recovered outside of general rate case proceedings. A decision from the
Commission in this proceeding may have the effect of changing the methodologies currently
used by PGE and PacifiCorp for cost recovery pursuant to ORS 469A.120, but would not alter
the utility’s ability to recover “all prudently incurred costs” associated with RPS compliance.
Fixed-rate automatic adjustment clauses provide the Commission with a flexible tool for rate
recovery of renewable capital costs outside of general rate cases.

1 for a particular capital project.⁵¹ Second, Joint Utilities’ arguments call into question the
2 function and policy of regulatory lag, seemingly arguing that it should be a policy objective of
3 this Commission to eliminate it.

- 4 1. A utility’s rate of return fairly compensates the utility for the recovery of capital costs
5 over time.

6 Staff and Joint Intervenors agree that utilities should not be permitted to have a more
7 favorable financial outcome through a deferral for capital investment—which constitutes an
8 extraordinary exception to standard ratemaking that the Commission has stated should be “used
9 sparingly”—than the utility would otherwise achieve through inclusion of the capital investment
10 via a general rate case, which is standard ratemaking treatment.⁵² Joint Utilities unpersuasively
11 attempt to sidestep this fundamental premise by arguing that the interest on a deferral account is
12 akin to the time value of money, whereas a utility’s return *on* capital investment is to compensate
13 for costs of obtaining capital. As discussed above, a utility’s return *on* investment is not an
14 expense for which it is guaranteed rate recovery. By including return *on* investment in a capital
15 deferral, at a rate authorized by the Commission in the utility’s last general rate case, the effect is
16 to guarantee recovery of the utility’s authorized rate of return at a time value of money
17 equivalent to its rate of return. In short, deferral of a utility’s return *on* investment at the utility’s
18 rate of return guarantees recovery of the utility’s rate of return *twice*, whereas under standard
19 ratemaking as discussed above, a utility is only entitled to the *opportunity* to earn its rate of
20 return once. Joint Utilities’ arguments also ignore that the utility’s rate of return is already
21 intended to compensate the utility for the lag in recovery between dollars expended for a capital
22 project up front, and the time over which that amount is recovered from customers.⁵³

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25 ⁵¹ Joint Utilities’ Opening Brief at 28.

26 ⁵² Staff’s Opening Brief at 8-9; Joint Intervenors’ Opening Brief at 8-9.

⁵³ Joint Intervenors’ Opening Brief at 7.

1 2. Regulatory lag is a standard aspect of utility ratemaking.

2 Joint Utilities argue that the Commission should not adopt a general policy against the
3 use of deferrals for the return of capital investment, in part because of regulatory lag.⁵⁴ Joint
4 Utilities' arguments are unpersuasive and easily dismissed when considered in the context of
5 ratemaking as a whole.

6 From the outset, it is important to remember that deferrals are, by definition, single-issue
7 ratemaking. In allowing the deferral of a utility expense or revenue, the Commission is allowing
8 for the possibility that a single issue will be allowed into rates, without the examination of all
9 other expenses or revenues that may have changed since rates were approved in the utility's
10 general rate case.⁵⁵ In a general rate case, rates are set based on a snapshot in time—the test
11 year. This means that depreciation expense is set based on that year, and does not account for
12 plant that will be added after the rate-effective date, nor does it account for plant that will be
13 further (or perhaps fully) depreciated between the rate-effective date and the utility's next
14 general rate case. In short, there is a dual nature to regulatory lag which Joint Utilities fail to
15 acknowledge or address. As stated by the Commission, “[t]he usual principle is that the Utility
16 enjoys both the risk and reward associated with regulatory lag.”⁵⁶ Deferrals for new capital
17 investment allow the utility to side-step regulatory lag for new plant, without recognition in rates
18 of the fact that other utility plant has further depreciated since the Company's last general rate
19 case.⁵⁷

20 _____
21 ⁵⁴ Joint Utilities' Opening Brief at 29.

22 ⁵⁵ The requirement that the Commission review a utility's earnings prior to amortization of
23 deferred amounts brings balance to this concern. See *Utility Reform Project v. Oregon Public*
24 *Utility Com'n*, 277 Or App 325, 342-344 (2016) (“In part, the purpose of an earnings test is to
25 allow the PUC to inquire whether ‘the extraordinary measure of amortization of the deferred
26 amount is justified, *i.e.*, despite the deferred costs or revenue, did the utility earn a reasonable
return on its equity during the period of the deferral and did ratepayers pay an appropriate rate
for services received?’” citing to *Utility Reform Project v. PUC*, 261 Or App 388, 401, 323 P.3d
430, *rev. den.*, 356 Or 517, 340 P.3d 48 (2014)).

⁵⁶ *In re PacifiCorp*, OPUC Docket Nos. UM 995/UE 121/UC 578, Order No. 01-753 at 4 (Aug.
28, 2001).

⁵⁷ Joint Intervenors' Opening Brief at 7-8.

1 Additionally, as Joint Intervenors argue, utility investments are recovered on a declining
2 curve—as more plant is depreciated, the return *on* the undepreciated investment shrinks.⁵⁸ This
3 change is not captured between rate cases.⁵⁹ One effect is that this regulatory lag allows the
4 utility to use additional non-cash depreciation to make new investments without necessarily
5 needing new rates. By allowing deferral of new capital, but failing to account for other changes
6 in depreciation, there is an upside to the utility without a corresponding benefit to customers.⁶⁰

7 Joint Utilities further argue that Staff “fails to explain why a partial loss is preferable to
8 ratemaking treatment that better matches costs and benefits.”⁶¹ Joint Utilities’ conclusion
9 regarding Staff’s position is a non sequitur. Staff’s argument is not that regulatory lag is
10 *preferable* to matching the costs and benefits of capital investments in rates. Rather, regulatory
11 lag is a standard tenet of ratemaking, which generally seeks to match costs and benefits in rates.
12 Singling out one aspect of rates for new capital investment, which is the effect of a deferral,
13 ignores the dual nature of regulatory lag.

14 3. Adoption of a policy against the deferral of return of utility investment is not beyond
15 the scope of this proceeding.

16 Joint Utilities argue that adopting a policy against deferral of capital investments is
17 beyond the scope of this docket.⁶² Joint Utilities are incorrect for several reasons. First, Joint
18 Utilities interpret the Commission’s direction in this proceeding too narrowly. Chair Hardie
19 discussed her interest in the proceeding, including the distinction between expenses and capital
20 costs, as well as regulatory lag.⁶³ Chair Hardie also discussed whether there was a need to
21 change the Staff motion, which contains language related to the Commission’s legal authority, in

22 _____
⁵⁸ Joint Intervenors’ Opening Brief at 8.

23 ⁵⁹ *Id.*

24 ⁶⁰ *Id.* at 9.

25 ⁶¹ Joint Utilities’ Opening Brief at 29.

26 ⁶² *Id.* at 24-25.

⁶³ November 21, 2017 Oregon Public Utility Commission Public Meeting at 54:26, accessed at http://oregonpuc.granicus.com/MediaPlayer.php?view_id=1&clip_id=252.

1 order to ensure that the parties did not overly restrict the discussion to a purely legal issue of
2 what the Commission “can and can’t do” as opposed to what it should or should not do.⁶⁴
3 Commissioner Decker noted that briefing generally contains policy considerations that the
4 Commission may want to take into account, and that inclusion of that discussion here would not
5 overly broaden the issues.⁶⁵

6 Second, the Commission’s legal authority and policy considerations are inextricably
7 linked in addressing the appropriate treatment for deferrals for capital costs, which Staff noted at
8 the public meeting opening this investigation. It is an incomplete discussion to omit policy
9 discussions from the Commission’s legal authority related to a discretionary statute.

10 Third, a generic docket is the appropriate place for the Commission to adopt a policy for
11 deferring return of utility investment. This generic proceeding stemmed from PGE’s UM 1791
12 proceeding, wherein PGE argued that the legal issue should be addressed in a generic proceeding
13 because it was generally applicable to all utilities. The same argument holds true for a generally
14 applicable policy. Staff has, and made, a generic policy recommendation to the Commission
15 regarding the deferral of capital costs. It is inefficient and unnecessary to address this issue in a
16 separate, generic proceeding.

17 Finally, it is important to note that no party has been deprived the ability to respond to
18 Staff’s policy recommendation, which all parties except the Joint Utilities support. Because
19 Staff went first in briefing, the Joint Utilities were able to fully respond to Staff’s
20 recommendation, and will have a closing brief to further expound upon their position.

21 4. The Commission should determine the application of a generic policy to pending
22 dockets within those dockets.

23 Joint Utilities jump to the incorrect conclusion that Staff’s recommendation is to “reject
24 all revenue requirement deferrals with capital costs, including pending deferrals.”⁶⁶ Staff’s brief

25 ⁶⁴ *Id.* at 54:49.

26 ⁶⁵ *Id.* at 56:35.

⁶⁶ Joint Utilities’ Opening Brief at 3.

1 did not recommend that the Commission make a determination about the application of any
2 policy choice to currently pending or amortizing deferrals. Because the Commission lacks the
3 legal authority to authorize the deferral of a utility's return *on* investment, the Commission has
4 no discretion to authorize the amortization of deferrals containing a utility's return *on*
5 investment. However, application of a policy to currently pending proceedings is an issue better
6 addressed within the specific, pending dockets.


7 **III. CONCLUSION**

8 For the reasons discussed above, Staff respectfully requests that the Commission find:

- 9 • It lacks the legal authority to defer return *on* capital investment.
- 10 • Policy considerations support the conclusion that deferral of return *of* capital
11 investment is inappropriate and inconsistent with ratemaking principles.
- 12 • It should establish a policy against deferring the return *of* capital investment.

13
14 DATED this 16th day of April, 2017.

15 Respectfully submitted,
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