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Via Electronic Filing

Public Utility Commission of Oregon
Attn: Filing Center
201 High St. SE, Suite 100
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Re: In the Matter of PUBLIC UTILITY COMMISSION OF OREGON Investigation of the Scope of the Commission's Authority to Defer Capital Costs.
Docket No. UM 1909

Dear Filing Center:

Please find enclosed the Joint Closing Brief of the Citizens' Utility Board of Oregon and the Alliance of Western Energy Consumers in the above-referenced docket.

Thank you for your assistance. If you have any questions, please do not hesitate to call.

Sincerely,

/s/ Jesse O. Gorsuch
Jesse O. Gorsuch

BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

UM 1909

In the Matter of the Application of: PUBLIC UTILITY COMMISSION OF OREGON Investigation of the Scope of the Commission's Authority to Defer Capital Costs	JOINT CLOSING BRIEF OF THE OREGON CITIZENS' UTILITY BOARD AND THE ALLIANCE OF WESTERN ENERGY CONSUMERS

I. INTRODUCTION

This docket investigates the scope of the Public Utility Commission of Oregon's ("Commission") authority to defer capital costs for later inclusion in rates. The Oregon Citizens' Utility Board and the Alliance of Western Energy Consumers (collectively "Joint Intervenors") have previously argued that the Commission has no authority to defer return <u>on</u> utilities' investment, and that as a matter of policy, should not allow return <u>of</u> utilities' investment to be deferred. A review of ORS 757.259(2)(e)'s plain text and legislative history shows that the Legislature did not intend to allow deferral of utilities' return on investment and may have intended to expressly foreclose that option. This Closing Brief responds to a range of Joint Utilities' arguments, many of which attempt to create ambiguity in plain statutory language, rely on curated selections of legislative history, and imply that past practice must control future Commission decisions. Joint Intervenors disagree with these arguments.

The Joint Intervenors continue to urge the Commission to find that there is no legally defensible basis for allowing deferrals of the return on capital investment. Further, the Joint Intervenors argue that the Commission should adopt a broad policy against the deferral of return of capital investment, as it is inappropriate and inconsistent with ratemaking principles. Should the Commission allow the deferral of capital investments, these investments should be treated as stochastic risks under the Commission's discretionary authority to approve deferred accounting applications.

II. ARGUMENT

The text and context of ORS 757.259(2)(e), as enacted by House Bill 2145 in 1987 ("HB 2145"), demonstrates that the Legislature did not intend to allow utilities to defer return on investment. Joint Utilities ignore the plain and ordinary meaning of the statute and instead rely primarily on legislative history, with which they argue that the terms "revenues" and "expenses" should be given their lay definitions, not their technical meanings as are commonly used in utility ratemaking. Joint Utilities piece together sections of a lengthy legislative history to make their argument, and Joint Intervenors agree with Staff that the Joint Utilities are attempting to "establish[] ambiguity in the plain and unambiguous text of the statute."[1/] While nothing bars the Joint Utilities from making this argument, their effort to "overcome seemingly plain and unambiguous text with legislative history [is] a difficult task."[2/]

Joint Intervenors reiterate that deferrals are intended to be "used sparingly,"[3/] and in fact constitute illegal retroactive ratemaking unless "expressly authorized" by the legislature.[4/] Moreover, "an administrative body possesses only those powers the legislature grants, and [] it cannot exercise authority that it does not possess."[5/] The Commission's ratemaking authority is broad, but ORS 757.259 specifically circumscribes its discretion in the context of deferrals. By

1/ Staff's Closing Brief at 10:4-5.
2/ State v. Gaines, 346 Or. 160, 172 (2009).
3/ Docket UM 1147, Order No. 05-1070 at 10 (Oct. 5, 2005).
4/ Or. Op. Att. Gen. OP-6076 (Or.AG.), 1987 WL 278316 at *1.
5/ Coquille School Dist. v. Castillo, 212 Or. App. 596, 607 (2007).

mentioning that deferrals are permissible in some cases, but not in others, the statute "implies a legislative intent to exclude related matters not mentioned."[6] Because ORS 757.259(2)(e) states that the Commission may defer "expenses or revenues," it implicitly removes the Commission's authority to defer anything else, like a return on investment.[7] Thus, even if the Commission's general powers included the authority to defer a return on investment, ORS 757.259's specific enumeration of permitted deferrals removed that authority.

These threshold doctrinal principles mean that the Joint Utilities must point to specific language that unambiguously authorizes the Commission to defer return on investment for later collection in rates, i.e., that ORS 757.259(2)(e) has "expressly authorized" such deferrals. The Joint Utilities have failed to meet that burden.

A. The text and context of ORS 757.259(2)(e) does not provide authority to defer a utility's return on investment.

The "text of the statutory provision itself is the starting point for interpretation and is the best evidence of the legislature's intent."[8] At the same time, a court must consider "the context of the statutory provision at issue, which includes other provisions of the same statute and other related statutes."[9] Even when legislative history is helpful, text and context "must be given primary weight in the analysis."[10] Context, such as "other related statutes," will affect how the language of a statute is read, with closely related statutes given more weight.[11]

As discussed below, HB 2145's legislative history, as viewed in its entirety, shows no unambiguous legislative intent to allow deferral of return on investment. Thus, the Commission

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[6] Roseburg Forest Products v. Wilson, 110 Or. App. 72, 76 (1991); Gantenbein v. PERS, 33 Or. App. 309, 319 (1978).

[7] A utility's return on investment is not an "expense or revenue" for purposes of ORS 757.259, and is therefore not eligible for deferred accounting treatment. See Staff's Closing Brief at 2-3.

[8] PGE v. BOLI, 317 Or. 606, 610 (1993).

[9] Id. at 611.

[10] Gaines, 346 Or. at 171.

[11] See, e.g. Gadda v. Gadda, 341 Or. 1, 10 (2006).

should rely on the text and context of ORS 757.259(2)(e), while keeping in mind that the legislative history would support a finding that the statute does not allow deferral of return on investment.

1. Ratemaking statues should be interpreted consistent with ratemaking meanings.

The Joint Utilities' fundamental argument is that the Legislature intended "expenses" in ORS 757.259(2)(e) to be synonymous with "costs," which includes the cost of capital. In combination with the ability to defer "revenues," the deferral statute therefore allows full revenue requirement deferrals, the Joint Utilities allege. In making this argument, the Joint Utilities largely ignore the text and context of this statute in favor of what they claim is a clear legislative intent to conflate "expenses" and "costs."[12/] As discussed below, no such clear legislative intent exists and, thus, text and context must guide the Commission's interpretation of the terms used in the deferral statute.

Oregon courts have consistently interpreted ORS Chapter 757 consistent with its terms' meaning in the ratemaking context. This chapter creates a comprehensive scheme of utility regulation that requires a specialized understanding of the "general legal principles" governing ratemaking.[13/] As the U.S. Supreme Court has stated, "[t]he economic judgments required in rate proceedings are often hopelessly complex and do not admit of a single correct result."[14/] To that end, the Oregon Supreme Court has prefaced discussions of ratemaking disputes by providing an "overview of public utility ratemaking," and has given otherwise undefined terms meanings as "understood within [the] public utility ratemaking" context.[15/] Further, the Oregon Supreme

12/ Joint Utilities' Opening Brief at 9-10, 14-19.
13/ ICNU v. PUC, 196 Or. App. 46, 49 (2004).
14/ Duquesne Light Co. v. Barasch, 488 U.S. 299, 314 (1989).
15/ Gearhart v. PUC, 356 Or. 216, 219-220 (2014), citing Charles F. Phillips, Jr., The Regulation of Public Utilities at 169-70 (2d. ed. 1988).

Court has read into the Commission's ratemaking duties "the following formula: R = E + (V-d)r."[16/] The Joint Utilities protest that this formula was "never cited in the legislative history of ORS 757.259,"[17/] but that is irrelevant and a distraction. The important point is that both the Oregon Supreme Court and U.S. Supreme Court – those with the ultimate power to interpret enacted statutes[18/] – have consistently recognized the technical nature of ratemaking and interpreted terms in ratemaking statutes accordingly, something the Legislature would have been presumed to be aware of when it passed ORS 757.259.

Indeed, the very basis for enactment of ORS 757.259 – that it provided necessary legal authority for the Commission to engage in otherwise impermissible retroactive ratemaking in certain limited circumstances – is itself due to the technical nature of ratemaking, where rates are established prospectively based on a comprehensive examination of all utility revenues and expenses, a valuation of plant used and useful in service, and establishment of a reasonable return that the utility has the opportunity to earn on its rate base.

Joint Utilities acknowledge the possibility that "revenues" and "expenses" are terms of art – but they then argue that they are accounting terms, or perhaps ratemaking terms with a different meaning than is commonly understood.[19/] Joint Utilities' arguments should be rejected.

First, for the same reasons that these terms should not be given their lay meaning, neither should they be given an accounting meaning. But if accounting definitions are given any weight, they should at least be public utility accounting definitions:

> "… above-the-line income statement items include *utility operating revenues and related operating expenses*, depreciation and amortization, and taxes, including income taxes.

[16/] Gearhart, 356 Or. at 220.
[17/] Joint Utilities' Opening Brief at 6.
[18/] Marbury v. Madison, 5 U.S. 137, 177 (1803); Jones v. Gen. Motors Corp., 325 Or. 404, 416 (1997).
[19/] Joint Utilities' Opening Brief at 19-20.

> *All of these items related to utility operations and are used in the ratemaking process in determining revenue requirements*."[20/]

This means that expenses and revenues are components of revenue requirement, with return on investment distinct.

For that matter, even the Joint Utilities' chosen definition of "expenses" proves exactly the same point: "Outflows or other using up of assets or incurrences of liabilities…"[21/] occur when a utility makes its initial investment, with return on investment coming later, and only after that investment is placed in service and found prudent by the Commission. Joint Utilities state that "[b]ecause return *on* investment represents one of those outflows necessary to provide service, it necessarily constitutes an 'expense.'"[22/] But this is not how ratemaking works (or how public utility accounting does). A return on investment is profit to the utility's shareholders, collected from customers, that is not guaranteed, and occurs only after an investment is made (i.e., after the "outflows" occur).

Second, the Joint Utilities argue that "expenses" and "revenues" should not be given the meanings that are typically used in the ratemaking equation (where they are included in "E," where revenues offset expenses).[23/] Instead, Joint Utilities suggest that "expenses" are the "sum total of the revenues required to pay all operating and capital costs."[24/] Essentially, Joint Utilities argue that "expenses" means "revenue requirement," or the "R" in the ratemaking formula. But "revenue requirement" is another ratemaking term of art that should be given its technical meaning, for the same reasons that "expense" should be, as discussed above.[25/] The Joint

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20/ Robert L. Hahne and Gregory E. Aliff, Accounting for Public Utilities § 13.03[2] (2017) (emphasis added).
21/ Joint Utilities' Opening Brief at 19.
22/ Id. at 20 (emphasis in original).
23/ Id.
24/ Id.
25/ See Gearhart, 356 Or. At 220 ("'R' represents the revenue requirement, 'E' represents allowable operating expenses, 'V' represents rate base, 'd' represents accumulated depreciation, and 'r' represents the rate of return.").

Utilities go so far as to argue that HB 2145 authorized deferral of "*revenue requirements* for the utility."[26] HB 2145 did no such thing: its plain text allows deferral of "utility expenses or revenues," which, in the ratemaking context, are components of "revenue requirement," but not the same thing.

2. If "expenses" and "revenues" are lay terms, they still demonstrate that ORS 757.259 does not allow deferral of revenue requirement.

Even assuming, for the sake of argument, that the Joint Utilities are correct and the terms "expenses" and "revenues" were intended to have non-technical meanings, the lay definitions Joint Utilities present do not indicate that revenue requirement capturing a return on investment is appropriate for deferral.

According to the Joint Utilities, "expenses" are commonly understood to mean "something that is expended" or a "financial burden."[27] The Joint Utilities make the leap from those definitions to the conclusion that the "combined *costs*" are reflected in revenue requirement and are therefore part of a utility's financial burden.[28] This oversimplification ignores how utilities – and all businesses – earn money, and how investments are financed.

If Joint Utilities are right that "expenses" should mean "something that is expended in order to secure a benefit or bring about a result," then the term conclusively <u>excludes</u> a return on investment because it requires no expenditure or outlay. Basic business principles dictate that an investment in a new asset – say, a new grocery store, or a new gas plant – will not necessarily turn a profit (the return <u>on</u> investment). Profit depends on managerial skill, demand for a product, managing costs, and market conditions. The amount "expended" to build that grocery store or new gas plant, or the "financial burden" of doing so, happens before it opens or

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[26] Joint Utilities' Opening Brief at 13 (emphasis in original).
[27] <u>Id.</u> at 9.
[28] <u>Id.</u> (emphasis in original).

commences operations, while the profit comes later. Joint Utilities seem to believe that they should be guaranteed the right to earn that profit, which they most definitely are not. While utilities may typically expect recovery of their return of investment (the amount "expended" or "financial burden" associated with new assets), the return on investment (the profit) is not guaranteed.

B. The legislative history of HB 2145 is ambiguous and, consequently, neither modifies the plain language of ORS 757.259 nor identifies an "express intent" to exempt return on capital investment from the prohibition against retroactive ratemaking.

As noted above, rather than rely principally on the text and context of ORS 757.259, the Joint Utilities base their position on HB 2145's legislative history. The heart of their argument is that "revenues" and "expenses" were not given their ratemaking meanings because the legislative history does not consistently refer to these terms in this way.[29/] In support of this argument, Joint Utilities point to the fact that (1) the words "costs" and "expenses" were used interchangeably by Commissioner Charles Davis on one occasion, (2) that a glossary of ratemaking terms provided to legislators did not define "revenues" or "expenses" and (3) that Representative Ron Eachus discussed "revenue requirement" once.[30/]

The most reliable legislative history shows themes "consistently reflected in both houses and throughout the legislative process," making it "more likely to reveal the intentions of the legislature as a whole."[31/] Joint Utilities argue that "it is difficult to imagine a more robust consensus concerning the intent and purpose motivating a piece of legislation," and that the legislative history reveals a similarly clear intent to "authorize comprehensive deferral of a

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29/ Id. at 20 (asserting that "expenses" should reflect "all of the expenses involved in providing utility services"). For reasons discussed below, this definition more properly applies to a utility's "revenue requirement."

30/ Id. at 18.

31/ Denton v. Denton, 145 Or. App. 381, 400 (1996).

utility's revenue requirement."[32/] In fact, HB 2145's legislative history is ambiguous, and is thus insufficient evidence to provide an "express authorization" sufficient to overcome the rule against retroactive ratemaking.[33/]

Joint Utilities' analysis of HB 2145's legislative history is built on two statements and an inference of what the lack of specific definitions in a glossary might mean. But taken in context, Joint Utilities' evidence in fact shows a clear legislative intent only with respect to the deferral of expenses and revenues, and not deferral of the return on investment. Commissioner Davis mixed the terms "expenses" and "costs," but this can hardly be said to conclusively show a consistent legislative intent to allow deferral of return on investment. The Joint Utilities' reliance on the glossary provided to the Legislature is an argument based on the absence of words, not actual definitions. The positions taken by Representative Eachus show a desire to create "balance" between utilities and ratepayers.[34/] And no matter whether the terms "expenses" and "revenues" should be read technically or in their lay sense, there is no conclusive evidence that "expenses" should include return on investment.

First, as Commissioner Davis was attempting to explain a highly technical bill to non-expert legislators, he unsurprisingly did not rely solely on technical language to make his points. And second, the bill was so technical that legislators needed a glossary of technical ratemaking terms to understand it – strong evidence that the non-expert legislators would also have been aware that they were considering a bill drafted by experts wherein technical ratemaking language might reasonably be used. The fact that the specific words "expenses" and "revenues" were not included in the glossary of technical terms, and that testimony mixed technical terms and lay

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32/ Joint Utilities' Opening Brief at 10-11.

33/ See OP 6076 at *1.

34/ Joint Utilities' Opening Brief at 13, citing Hearing on HB 2145 Before the H. Environment and Energy Comm., Tape 97 Side A, at 1:25-1:28 (Apr. 8, 1987) (quoting Rep. Eachus).

terms proves little. Legislators knew they were operating in a highly technical field and modifying a comprehensive ratemaking framework, both facts that weigh in favor of finding that the technical ratemaking meaning of these terms should control.[35/] It would be unusual for the Legislature to intentionally mix technical terms with lay terms in a statute, as the Joint Utilities have suggested it did, especially as the Legislature would have been aware that ratemaking statutes are almost always interpreted consistent with their technical meaning.[36/] Joint Intervenors agree with Staff that "there is no indication that the legislature intended one set of ratemaking definitions to apply in general rates cases or other ratemaking proceedings, and another to apply to deferrals."[37/]

Other references to the legislative history the Joint Utilities' select further undermines their ability to demonstrate a "consistent" legislative intent with respect to the word "expense." Joint Utilities rely in large part on Representative Eachus's single statement during a House Environment and Energy Committee Hearing that HB 2145 provided authority to defer "benefits to the ratepayers as well as *revenue requirements* for the utility.[38/] But as the Joint Utilities note, Representative Eachus's point was that "the key word here is balance."[39/] In fact, the language "utility expenses or revenues" was added to the legislation – by NW Natural, now one of the Joint Utilities – to ensure just such a balance. NW Natural's suggested amendment to HB 2145 was not intended to change the utilities' right to defer "amounts *incurred by* a utility," but solely

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35/ Klamath Irrigation Dist v. United States, 348 Or. 15, 23, 227 P.3d 1145, 1150 (2010) ("the context for interpreting a statute's text includes… the statutory framework within which the law was enacted. (emphasis added)), citing Denton, 326 Or. at 241.

36/ See id., American Can Co. v. Davis, 28 Or. App. 207 (1977), Pac. Tel & Tel. Co. v. Hill, 229 Or. 437, 443-44 (1961), Pac. Power & Light. Co. v. Dept. of Revenue, 10 Or. Tax 417, 421-24 (1987).

37/ Staff's Closing Brief at 7:5-6.

38/ Joint Utilities' Opening Brief at 13 (emphasis in original), citing Hearing on HB 2145 Before the H. Environment and Energy Comm., Tape 97 Side A, at 3:15-3:20 (Apr. 8, 1987) (quoting Rep. Eachus).

39/ Id., citing Hearing on HB 2145 Before the H. Environment and Energy Comm., Tape 97 Side A, at 1:25-1:28, (Apr. 8, 1987) (quoting Rep. Eachus).

to allow deferrals "on the other side."[40] The Joint Utilities ignore this intent and focus solely on the meaning of a technical term – an approach they notably reject when otherwise applied to this legislative history – to argue that the Legislature intended to allow deferral of all components of a utility's revenue requirement. But a solitary statement about revenue requirement, in the context of a discussion about "balance" and allowing deferrals "on the other side," cannot be said to show themes "consistently reflected in both houses and throughout the legislative process," or for that matter, even themes reflected in a single hearing.[41]

This lack of consistent legislative intent is further reinforced by later testimony by Representative Eachus before the Senate Committee on Business, Housing, and Finance, nearly two months after the House Committee's deliberations. By that point, Representative Eachus had dropped the reference to revenue requirement and instead spoke of "costs to the utility" and "benefits to the ratepayer."[42] His explanation of the bill includes no evidence of an intent to allow deferral of return on investment.

It may be that Joint Utilities have the standard right: perhaps a "robust consensus" within the legislative history would be sufficient evidence to show an "express intent"[43] to allow retroactive ratemaking for returns on capital investments.[44] But ambiguity in legislative history means that they have not shown an "express intent," which would require evidence that is "definitively and explicitly stated."[45]

40/ Id., citing Hearing on HB 2145 Before the H. Environment and Energy Comm., Exhibit D at 1 (Mar. 25, 1987) (emphasis added); Tape 96 Side A, at 19:13-19:37 (Apr. 8, 1987) (quoting Rep. Eachus).

41/ See Denton, 145 Or. App. at 400.

42/ Joint Utilities' Opening Brief at 18, citing Hearing on HB 2145 Before the S. Comm. on Bus., Hous. & Fin., Tape 99, Side B, at 16:00-16:05 (May 21, 1987) (testimony of Rep. Eachus).

43/ OP 6076 at *1.

44/ Or it might not, as the Joint Utilities would still have to "overcome seemingly plain and unambiguous text with legislative history." Gaines, 34 Or. at 172.

45/ *Express,* The American Heritage Dictionary of the English Language (5th ed. 2016).

C. A general commission policy against deferral of capital investment protects ratepayers and is sound energy policy.

The Joint Intervenors, aligning with Staff,[46] continue to urge the Commission to adopt a policy against authorizing deferrals for the return of utility capital investments. Deferred accounting is a "discrete and exceptional ratemaking process[,]"[47] and the Commission should be cautious to promote a policy that allows for frequent capital investment deferred accounting in a manner that benefits shareholders to the detriment of customers.[48] Although the Joint Utilities assert that requesting a policy against deferral of capital investment goes beyond the scope of this docket,[49] this argument cuts against the Commission's intent in initiating this proceeding.[50] To make this argument, the Joint Utilities misleadingly and narrowly point to Staff's request to open the docket to investigate whether the Commission has the "legal authority to defer capital costs."[51] However, the Commission requested that the scope of the proceeding include a "discussion of past policy and precedent and [ ] policy considerations" at a subsequent public meeting.[52] The Commission specifically requested this change to allow the scope of this proceeding to extend beyond a mere examination of its legal authority. As such, a discussion of policy rationale relating to the deferral of capital investment is well within the contemplated

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46/ Staff's Closing Brief at 11.

47/ Joint Intervenors' Opening Brief at 5, citing in re Public Utility Commission of Oregon, Docket No. UM 1147, Order No. 05-1070 at 10 (Oct. 5, 2005).

48/ Joint Intervenors' Opening Brief at 7 ("If a utility is permitted to file a deferral every time a capital investment becomes used and useful—but before its next general rate case—regulatory lag is effectively eliminated, while the utility retains the benefit of an authorized ROE intended to compensate for that impact. In that instance, all of the risk associated with regulatory lag is shifted to customers on the back end of the capital investment's depreciation curve, while all of the benefit is shifted to the utility on the front end.").

49/ Joint Utilities' Opening Brief at 24.

50/ Staff's Opening Brief at 1, citing November 21, 2017 public meeting at 51:45 accessed at http://oregonpuc.granicus.com/MediaPlayer.php?view_id=1&clip_id=252&meta_id=12062.

51/ Joint Utilities' Opening Brief at 24, citing Staff's Initial Application at 1.

52/ Staff's Opening Brief at 1, citing November 21, 2017 public meeting at 51:45 accessed at http://oregonpuc.granicus.com/MediaPlayer.php?view_id=1&clip_id=252&meta_id=12062.

scope of this docket.[53/]

As argued in the Joint Intervenors' opening brief, permitting utilities to defer capital investments would fundamentally alter the regulatory lag risk profile in an inequitable manner, causing ratepayers to bear substantially more risk while giving utilities the ability to earn an extra return.[54/] Additionally, allowing deferral of capital investments would enable utilities to earn substantially beyond their authorized rate of return in a manner that cuts against traditional ratemaking practice.[55/] The examples of prior cases cited by the Joint Utilities provide insight into this inequity, and demonstrate why allowing deferral of capital investments is poor policy.[56/]

Further, the Commission currently evaluates deferrals based on two interrelated factors – the type of event giving rise to the deferral and the magnitude of the event's effect.[57/] With regard to the type of event causing the deferral, the Commission draws a distinction between risks that can be predicted to occur as part of the normal course of events ("stochastic risks"), and risks that are not susceptible to prediction and quantification ("scenario risks").[58/] The Commission has concluded that stochastic risks are generally not eligible for deferred accounting, while scenario risks are.[59/] Since the magnitude and timing of a capital investment is completely within the control of the utility, these costs are stochastic risks and should not be eligible for deferred accounting treatment.

53/ See Staff's Closing Brief at 14-15.
54/ Joint Intervenors' Opening Brief at 6-9.
55/ Id. at 10.
56/ Joint Utilities' Opening Brief at 22-23.
57/ Order No. 05-1070 at 3.
58/ Id.
59/ Id.

1. Regulatory lag is a fundamental ratemaking aspect that ensures risk is shared equitably between utilities and customers.

The standard utility ratemaking treatment of bringing capital investments forward for recovery in a general rate case helps ensure that the risk structure is balanced between utilities and shareholders. While the Joint Utilities argue that deferrals help balance the interests of customers and utilities in order to achieve just and reasonable rates,[60] enabling utilities to file a deferral for a capital investment to avoid regulatory lag has the exact opposite effect. If a utility is permitted to file a deferral every time a capital investment becomes used and useful – but before its next general rate case – regulatory lag is effectively eliminated, while the utility retains the benefit of an authorized return on equity ("ROE") intended to compensate for the risk.[61] In this scenario, all of the risk associated with regulatory lag is shifted to customers who bear the back-end regulatory lag risk, while all of the benefit is shifted to the utility on the front end.[62] The Joint Intervenors agree with Staff that allowing deferrals for the return of capital investment would inequitably avoid "[t]he usual principle [] that the Utility enjoys both the risk and reward associated with regulatory lag."[63] This principle encourages efficient utility operation to manage costs between rate cases while customers continue to pay a set rate for utility plant that is continuously depreciating.

In their Opening Brief, the Joint Intervenors provided an illustrative example demonstrating the regulatory lag risk borne by the utility and customers under the traditional rate case recovery paradigm.[64] In that example, customers are accountable for a much larger portion

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60/ Joint Utilities' Opening Brief at 27.

61/ Joint Intervenors' Opening Brief at 7.

62/ Id.

63/ Staff's Closing Brief at 13, citing in re PacifiCorp, Docket Nos. UM 995/UE 121/UC 578, Order No. 01-753 at 4 (Aug. 28, 2001); see also in re PacifiCorp, Docket No. UE 246, Order No. 12-493 at 8 (Dec. 20, 2012) ("[U]tilities typically bear the risk of increased costs between rate cases.").

64/ Joint Intervenors' Opening Brief at 8.

of the regulatory lag risk profile because they are overpaying for continuously depreciating plant until the utility comes in for a rate case – an aspect completely within the utility's control. Eliminating the regulatory lag on the front end of the investment for the utility would further exacerbate this risk shift. In the Joint Utilities' Opening Brief, they ask why "utilities should be required to internalize lost depreciation, especially when the benefits of a capital project may flow directly . . . to customers."[65/] This risk – internalizing lost depreciation – is the exact principle that utilities should bear the risk and reward of regulatory lag.[66/] When utilities internalize lost depreciation by bringing capital investments in a rate case, customers are internalizing far more lost depreciation on the back end of the depreciation curve. This more adequately matches costs and benefits than enabling deferrals for the return of capital investments ever could. To quote Staff, "there is a dual nature to regulatory lag which Joint Utilities fail to acknowledge or address."[67/]

The risk associated with regulatory lag is part of the regulatory compact and traditional regulatory ratemaking. Within this framework, the Commission should not engage in single-issue ratemaking that has all upside to the utilities absent a compelling reason. The regulatory lag associated with the front end of a capital investment's depreciation curve does not rise to that level. The Commission does not go investment-by-investment to determine and set just and reasonable rates, but, rather, sets base rates based on the test year in a general rate case.[68/] The utility's ROE – intended to compensate for the risk it takes on – is also set in a rate case's test year. In addition to its authorized ROE, the utility can earn an additional return by controlling costs in between rate cases. Enabling a utility to earn a ROE for risks that have been shifted to

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65/ Joint Utilities Opening Brief at 29.
66/ See Order Nos. 01-753 and 12-493, supra, note 18.
67/ Staff's Closing Brief at 13.
68/ Id.

customers will enable utilities to systematically over-earn. Utilities should have to live with the rates set until they incur sufficient capital investments or other costs and file for a general rate increase. If utilities are permitted to sidestep the regulatory lag risk that they are traditionally subject to, then their ROEs should be reduced accordingly.

Deferred accounting is supposed to be an exception to traditional ratemaking.[69/] Ratemaking is a holistic practice focused on setting just and reasonable rates, not cost recovery of individual items. Utilities are always adding new investments, while old investments continuously depreciate. Loads are never as predicted. Some expenses increase, while others decrease. The focus of economic regulation is not whether a specific cost was included in rates. The focus is whether rates that were set based on a test year are sufficient to allow the utility an opportunity to earn a reasonable rate of return. If they are not, the solution is a new general rate case to establish new rates based on an updated test year that includes capital investments, depreciation, load, expenses, and revenues.

2. Should utilities be permitted to defer the return of capital investments, they should be treated as stochastic risks.

The Joint Intervenors continue to urge the Commission to adopt a policy to not allow utilities to defer the return of capital investments. However, should the Commission continue to allow utility deferral for the return of capital investments, they should be treated as stochastic, rather than scenario, risks. Within its discretionary authority to approve deferred accounting applications, the Commission has drawn a distinction between the type of event giving rise to the deferral.[70/] Stochastic risks are those that can be predicted to occur as part of the normal course of events, and scenario risks are those that are not susceptible to prediction and quantification.[71/]

69/ See Docket UM 1147, Order No. 05-1070 at 10.
70/ Id. at 3.
71/ Id.

The magnitude of the financial effect on the utility is a significant factor in the Commission's discretion to approve a deferred accounting application.[72/] For a stochastic risk to justify deferred accounting, the financial impact must be substantial.[73/] Scenario risks – extraordinary events that fall outside the predictable and quantifiable – are eligible for deferred accounting.[74/] For these risks to qualify for deferred accounting, the financial impact on the utility need only be material.[75/]

Utilities are in control of the timing of capital investments, and are currently able to recover substantial amounts of capital through deferred accounting.[76/] The Joint Utilities argue that a change in how the Commission approaches deferred accounting for capital investments is not warranted because the Commission recently conducted a comprehensive assessment of its deferral policies.[77/] However, the investigations in UM 1071 and UM 1147 did not fully discuss policy considerations regarding the potential deferral of capital investments, and much of the discussion in UM 1147 surrounded the interest rates applied to deferred accounts before and after amortization. Since utilities are in complete control of the timing and cost of capital investments, they cannot be classified as scenario risks – those that are not predictable or quantifiable. Therefore, should the Commission allow capital investments to be eligible for deferred accounting treatment, it should adopt a policy classifying capital investments as a stochastic risk. As such, capital investments would only be eligible for deferred accounting if the financial impact on the utility is substantial.

72/ In re Portland General Electric Company, Docket No. UM 1071, Order No. 04-108 at 9 (Mar. 2, 2004).
73/ Id.
74/ Id.
75/ Id.
76/ Joint Intervenors' Opening Brief at 6.
77/ Joint Utilities' Opening Brief at 25-26.

D. Past practice does not constitute legal authorization for the Commission to defer return on investment and highlights the fact that such deferrals are bad policy.

As pointed out by the Joint Utilities, the Commission has occasionally allowed deferral of return on investment. The Joint Utilities identify four times over the last 30 years when this has occurred.[78] It appears that the legality of these deferrals was never discussed in any of the decisions the Joint Utilities cite, and that the Commission has never discussed whether return on investment can legally be deferred. The fact that such deferrals have occurred in the past is no evidence that they are lawful or should be allowed in the future; if anything, it proves only the necessity of getting the answer right this time.

In support of their contention that ORS 757.259(2)(e) authorizes revenue requirement deferrals, the Joint Utilities cite several prior decisions to insinuate that the Commission has repeatedly authorized "deferrals for the full revenue requirement effect of capital investments."[79] In fact, the Joint Utilities can cite to only four cases that are either irrelevant or easily dismissed as poor policy. The Joint Utilities also cite to cases that predate the enactment of HB 2145 – they are similarly irrelevant, as they were decided under a prior legal framework that was modified by HB 2145.[80]

First, the Joint Utilities cite an Avista case in which it received annual reauthorization to defer "the revenue requirements and estimated revenue margin losses associated with its [Demand Side Management ("DSM")] investment."[81] This reauthorization is not a good

[78] Id. at 22-23.
[79] Id. at 22.
[80] See id. at 14-16. Those orders were also promulgated without any legal authority. OP 6076 at *6.
[81] Id. at 22, citing in re Avista Corporation, Application for Reauthorization of Certain Deferral Accounts Related to Avista's Demand Side Management Programs, Docket UM 1165, Order No. 16-304 (Aug. 16, 2016).

example of how ORS 747.259(2)(e) should work. In 1993, Oregon allowed utilities to rate base energy efficiency in a similar manner to capital investments that are brought in a rate case. When Avista began deferring energy efficiency expenses in 1993, the Commission was experimenting with allowing utilities to capitalize energy efficiency, so it is possible that the Company was allowed to defer capital investments related to energy efficiency at that time. Avista's annual reauthorizations of its DSM program are routine and generally not opposed by any party – so it is not surprising that old Commission policy has stayed current all these years. However, the policy of the Commission now is that energy efficiency is an expense.[82/] No party to this case is arguing that some deferrals of expenses relating to energy efficiency are improper.

Second, the Joint Utilities cite to a NW Natural case in which the utility received authorization to defer costs associated with the construction of the Coos County Distribution System.[83/] This case and the facts it addressed are unique. The City of Coos Bay wanted gas service to encourage industrial development, and the State of Oregon invested in a gas pipeline to deliver gas to the area.[84/] NW Natural was then expected to invest and build a distribution system. NW Natural proposed that statewide residential and commercial customers subsidize the distribution investment, to which Staff and CUB objected.[85/] Eventually, a negotiated agreement was developed. Within that agreement, there was a realization that customers would be slow in converting to natural gas and hooking up to the distribution system. This created a problem with how capital investments are recovered, because when the project became used and useful, there were no customers to use it. Capital projects are generally front-loaded.[86/] Parties to that docket

82/ See in re PGE, Docket No. UM 964, Order No. 00-232 (May 3, 2000).
83/ Joint Utilities' Opening Brief at 22, citing in re NW Natural, Docket No. UM 1179, Order No. 04-702 (Dec. 3, 2004).
84/ See in re NW Natural, Docket UG 152, Order No. 03-236 (2003).
85/ Id. at 1-2.
86/ Joint Intervenors' Opening Brief at 8.

had come up with a solution to creatively solve the problem of how to collect the front-loaded rate base costs when the anticipated load was back-loaded.[87/] Eventually, a deferral was selected to recover costs, as it would help avoid inequity and cost shifting.[88/] This avoided having non-Coos Bay customers subsidize the distribution system by allowing recovery of costs to be delayed until there were enough customers on the distribution system to fund that recovery. This was done as a one-off settlement, and not as a larger, overarching Commission policy for approving deferrals for capital investments.

Third, the Joint Utilities cite to a PGE case in which it received approval to defer the revenue requirement associated with four capital projects.[89/] This case exemplifies why Staff and the Joint Intervenors believe deferring capital investments is a poor policy choice. In UE 215, PGE proposed to place four capital projects into rate base, but parties objected because the projects would not be used and useful by the time rates were set.[90/] Once again, parties engaged in a one-off settlement to resolve this issue by deferring the revenue requirement for these projects until the next rate case. While some of the Joint Intervenors in this case supported this solution at the time, it is problematic in retrospect. There, PGE contorted the ratemaking process in order to avoid even a single day of regulatory lag. By avoiding regulatory lag in this single-issue ratemaking construct, PGE was able to receive dollar for dollar recovery and additional risk was shifted onto customers. PGE was also able to avoid the risk associated with load forecasting, as discussed in the Joint Intervenors' Opening Brief.[91/] Proper ratemaking treatment should have been to either delay the rate effective date to allow the capital projects to become

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87/ Id. at 3.
88/ See id. at 2, Order No. 04-702 (Dec. 3, 2004).
89/ Joint Utilities' Opening Brief at 23, citing in re Portland General Electric Co., Docket No. UM 1513, Order No. 13-048 (Feb. 12, 2013).
90/ in re Portland General Electric Company, Docket No. UE 215, Order No. 10-478 at 6 (Dec. 17, 2010).
91/ Joint Intervenors' Opening Brief at 12.

used and useful, or to have PGE be subject to regulatory lag and add these capital projects in its next rate case, the timing of which is entirely in its control.

Fourth, the Joint Utilities cite to an Idaho Power case in which it received approval to defer revenue requirement variances associated with the Langley Gulch Power Plant.[92/] This is another excellent example why deferring capital investments is a poor policy choice. Idaho power filed a request to add its Langley Gulch Power Plant to rate base on March 9, 2012, when the plant was expected to go into service on July 1, 2012. Idaho Power's rate request was suspended for 9 months to give time for Staff's and intervenors' review. The deferral was attempting to avoid even a few months of regulatory lag while the rate request was examined and new rates were set.[93/] However, as stated, the timing of a rate case is in the control of the utility, so it could have filed a rate case to align with the plant's online date. At the time, Langley Gulch was a new power plant with decades of useful life ahead of it. The effect of avoiding a few months of regulatory lag on the total ROE of the plant is insignificant. However, customers are still saddled with paying set rates between rate cases while the plant itself is continuously depreciating. This is a prime example of the utilities' complete reluctance to incur any regulatory lag risk to the detriment of customers.

III. CONCLUSION

For the foregoing reasons, the Joint Intervenors respectfully request that the Commission determine that ORS 757.259(2)(e) does not permit the deferral of return on capital investment. If, however, the Commission finds that it does have the legal authority to defer capital investments, the Commission should nevertheless adopt a general policy against such deferrals

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92/ Joint Utilities' Opening Brief at 23, citing in re Idaho Power Company, Docket No. UM 1597, Order No. 12-226 (June 19, 2012).

93/ Order No. 12-226 at 1-2.

because deferrals in general should be used sparingly and capital costs are properly recovered through general rate cases, the timing of which is completely in control of the utilities. Finally, should the Commission determine that capital investments are eligible for deferred accounting treatment, these investments should be treated as stochastic risks under the Commission's discretionary authority to approve deferrals.

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Respectfully submitted,

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