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J. Jeffrey Dudley
Associate General Counsel

March 23, 2006

Via Electronic Filing and U.S. Mail

Oregon Public Utility Commission
Attention: Filing Center
PO Box 2148
Salem OR 97308-2148

Re: OPUC Dockets DR 10, UE 88, UM 989, UF 4218, and UM 1206

Attention Filing Center:

Enclosed for filing in the above-captioned dockets is Portland General Electric's Response to *Ex Parte* Communications. This document is being filed by electronic mail with the Filing Center.

An extra copy of this cover letter is enclosed. Please date stamp the extra copy and return it to me in the envelope provided.

Thank you in advance for your assistance.

Sincerely,

/s/ J. JEFFREY DUDLEY

JJD:am

cc: Combined Service Lists: DR 10, UE 88, UM 989, UF 4218, UM 1206

Enclosure

BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

DR 10/UE 88/UM 989
UF 4218/UM 1206

In the Matters of PORTLAND GENERAL ELECTRIC COMPANY Application for an Investigation into least Cost Plan Plant Retirement (DR 10) Revised Tariffs Schedules for Electric Service in Oregon (UE 88) Application for an Accounting Order and for Order Approving Tariff Sheets Implementing Rate Reduction (UM 989) Application for an Order Authorizing the Issuance of 62,500,000 Shares of New Common Stock Pursuant to ORS 757.410 et seq. (UF 4218) and STEPHEN FORBES COOPER, LLC as Disbursing Agent, on behalf of the RESERVE FOR DISPUTED CLAIMS Application for an Order Allowing the Reserve for Disputed Claims to Acquire the Power to Exercise Substantial Influence over the Affairs and Policies of Portland General Electric Company Pursuant to ORS 757.511. (UM 1206)	)	**PORTLAND GENERAL ELECTRIC COMPANY'S RESPONSE TO *EX PARTE* COMMUNICATIONS**

Pursuant to the Notice of Public Meeting issued on March 8, 2006, in the above-captioned dockets, Portland General Electric Company ("PGE" or the "Company") hereby responds to the *ex parte* communications made at the March 13, 2006, meeting of the Public Utility Commission of Oregon ("OPUC"). Neither the *ex parte* communications nor this

Response is part of the record in the above dockets, as the OPUC has closed the record in each docket.[1]

I. Utility Reform Project – DR 10/UE 88/UM 989

The Utility Reform Project, in written comments dated March 13, 2006 ("URP Comments"), claimed that the PUC Staff Review[2] is contrary to several Oregon court decisions. URP Comments p. 2 PGE responds that URP's claim is incorrect and has been fully briefed by URP and PGE in the current remand dockets (DR 10/UE 88/UM 989).[3]

II. Commissioner Randy Leonard – UF 4218/UM 1206

Portland City Commissioner Randy Leonard, in his March 13, 2006, Memorandum to the OPUC ("Leonard Memo") on page 4, requests that the Commission delay "the implementation of the stock redistribution plan." This request is based on the "other unresolved issues" and the claimed benefits of an "LLC conversion." Leonard Memo p. 4. Most of Commissioner Leonard's "unresolved issues" are resolved in the PUC Staff Review. PGE addresses the balance of the "unresolved issues" and explains the fatal defects in the "LLC conversion" in its March 13, 2006 memo to the OPUC (Attachment A).

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1 In Dockets DR 10, UE 88, and UM 989, the record was closed on August 30, 2005. Hearing Transcript. Volume 2, Page 343. In Dockets UF 4218 and UM 1206, the record was closed pursuant to a Ruling dated October 13, 2005.

2 "Staff Review of PGE Issues Raised by the City of Portland," Staff Report from Ed Busch through Lee Sparling, March 2, 2006.

3 In OPUC Dockets DR 10, UE 88, and UM 989, *see* Utility Reform Project et al. and the Class Action Plantiff's Opening Brief, November 9, 2005; PGE's Opening Post-Hearing Brief (Phase I), November 9, 2005; Staff's Opening Post-Hearing Brief (Phase I), November 9, 2005; PGE's Post-Hearing Reply Brief (Phase I), November 30, 2005; Utility Reform Project et al. and the Class Action Plantiff's Reply Brief, November 30, 2005; Staff's Post-Hearing Reply Brief (Phase I), November 30, 2005; PGE's Post-Hearing Response Brief (Phase I), December 14, 2005.

DATED this 23rd day of March, 2006.

Respectfully submitted,

/s/ J. JEFFREY DUDLEY
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CERTIFICATE OF SERVICE

I hereby certify that I have this day caused the foregoing RESPONSE OF PORTLAND GENERAL ELECTRIC COMPANY TO *EX* PARTE COMMUNICATIONS to be served by electronic mail, and for the parties who have not waived paper service, by First Class US Mail, postage prepaid and properly addressed, upon each party on the attached combined service lists of OPUC Dockets DR 10, UE 88, UM 989, UF 4218, and UM 1206.

Dated at Portland, Oregon, this 23rd day of March, 2006.

/s/ J. JEFFREY DUDLEY____________________
J. Jeffrey Dudley

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MEMORANDUM

TO: **Oregon Public Utility Commission**

FROM: **Portland General Electric Company**

DATE: March 13, 2006

RE: **City of Portland Key Areas of Interest**

At the Commission's meeting on March 2, 2006 Portland City Commissioner Randy Leonard presented a memo stating seven "key areas of interest" to the City of Portland. The memo also for the first time presented the City of Portland's "proposed alternative" to PGE's stock distribution. This memo is intended to respond briefly to the issues raised in Commissioner Leonard's memo.

1. **Compliance with State Income Tax Law.** PGE is in compliance with Oregon State Income Tax laws. The City cites several Oregon statutes relating to the Oregon State Income Taxes. These statutes are administered and enforced by the Department of Revenue. ORS 314.805. As a result all the issues raised in Commissioner Leonard's key issue number one should be addressed to the Department of Revenue and not to the Oregon Public Utility Commission.

2. **Federal Energy Regulatory Commission Tax Policy.** Commissioner Leonard's statement is incorrect about Federal Energy Regulatory Commission policy on income tax allowances. Current FERC policy on including taxes in rates provides that income taxes included in rates for a utility like PGE would be on a stand-alone basis. *See* Policy Statement on Income Tax Allowances, 111 FERC 61139 (May 4, 2005); *City of Charlottesville v. FERC,* 774 F.2d 1205, 1208-1211 (D.C. Cir.1985) (describing evolution and rationale behind FERC's stand-alone tax policy).

3. **Multnomah County Business Income Tax.** The matters raised in Commissioner Leonard's third key issue are adequately addressed by the Staff Report presented to the Commission on March 2, 2006. The class action brought on this issue is in the process of being settled and all collections of Multnomah County Business Income Taxes from January 1, 1999 through December 31, 2005 will be refunded to PGE customers with interest.

4. **Responsibility of PGE to Multnomah County.** Multnomah County is the taxing authority for the Multnomah County Business Income Tax, not the City of Portland. Multnomah County last fall confirmed that it had no interest and did not intend to assert any claim for the amounts PGE collected for the Multnomah County Business Income Tax that were not paid to the County. The class action that raised this issue is in the process of being settled and all collections of Multnomah County Business Income Taxes from 1999 through 2005 will be refunded to PGE customers with interest.

5. **No Double Charge for Multnomah County Business Income Tax.** Rates set by this Commission do not double charge customers for the Multnomah County Business Income Tax. Rates set by the Commission in PGE's last general rate case, UE 115, do not include any component for Multnomah County Business Income Tax. The only collections for Multnomah County income taxes have been through charges separately placed on customer bills. The fact that effective tax rates vary from the rate used for setting rates in a rate case illustrates the variable nature of income taxes. PGE's effective tax rate frequently changes to reflect differences between book and tax accounting for certain items of income and expense. The changes in PGE's effective tax rate are unrelated to the collection on Multnomah County Business Income Tax.

6. **PGE Did Not Harm the Wholesale Trading Market in 2000.** The claims about PGE trading have been resolved by the Commission Staff Report. In addition:

   - PGE's need for a rate increase in October 2001 was established through a full general rate case process conducted from the end of 2000 through 2001. PGE had the burden of proof to demonstrate an increase was necessary. The City of Portland was an intervener with full party rights in that process. The Commission's final Order identified a revenue deficiency for the test year 2002 (see Order No. 01-777 appendix G, page 2, column 3). The Commission found that that without a rate increase PGE would be operating at a loss, that is, with negative net operating revenues.

   - Neither profitable nor unprofitable past years are proper considerations for setting future utility rates. This is the rule against retroactive ratemaking. Instead the Commission makes judgments on the cost of service to customers in a prospective period (the "test year") and independently determines whether future rate increases are needed to cover the cost of service. The Commission exercised its judgment in 2001 in Order No. 01-777. The City of Portland was a party to that Commission proceeding.

- PGE had no "increases in profit" in 2001; it earned less than its authorized level. In 2002, the first year after the rate change authorized in UE 115, PGE also earned below its authorized level.

- PGE does not make any profit on purchased power. PGE's rate increase in 2001 was driven in large part by the need to buy more expensive power to serve our customers. The way the Commission currently sets rates, purchased power does not create any margin for PGE.

- In the 2001 time period other utilities needed to raise rates to customers. Seattle City Light raised its residential rate by 54.3%. Seattle City Light raised its large industrial rate by 63.0%. The City of Tacoma raised its overall rates by 50% and by as much as 70% for industrial customers.

7. **PGE Does Not Pay Deferred Taxes to Enron.** PGE payments to Enron for income taxes are computed and paid the same way as tax obligations due to taxing authorities. PGE, like all taxpayers, does not pay deferred taxes to taxing authorities – it pays only current taxes. Likewise, PGE does not pay deferred taxes to Enron; it only pays its current income tax obligations.

Regarding the "proposed alternative" of converting PGE to an LLC (disregarded entity) suggested for the first time in Commissioner Leonard's March 2 memo, PGE attaches a Memorandum from Skadden, Arps, Slate, Meagher & Flom LLP analyzing this LLC proposal ("Skadden Memo"). The Skadden Memo concludes that the claimed tax benefits from the City of Portland's proposed alternative can not be achieved.

SKADDEN, ARPS, SLATE, MEAGHER & FLOM LLP

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March 13, 2006

TO: Portland General Electric Company

FROM: James V. Alpi
Alexander L.T. Reid

RE: Certain U.S. Federal Income Tax Consequences of Converting Portland General Electric Company to a Limited Liability Company

You have asked us to review a proposal whereby Portland General Electric Company ("PGE") would file articles of conversion with the state of Oregon to convert into a limited liability company ("LLC") prior to the distribution to the creditors of Enron Corp. ("Enron") of the common stock of PGE. Rather than distributing the stock of PGE to Enron's creditors as contemplated under the Court Order of the US Bankruptcy Court for the Southern District of New York and the Fifth Amended Joint Plan of Affiliated Debtors Pursuant to Chapter 11 of the United States Bankruptcy Code dated January 9, 2004 (the "Plan"), we understand that, under the proposal, Enron would instead distribute interests in the LLC holding PGE's assets to Enron's creditors.

Our understanding is that the sole purpose for the proposed change to the existing Plan is to reduce PGE's U.S. federal income taxes for future years by effecting an increase or "step up" of tax basis in PGE's assets for PGE after the transfer to the Enron creditors. The step up in basis, in theory, would entitle PGE to the benefit of increased depreciation deductions which would otherwise not be available.

We believe this scheme would not result in the intended tax benefits for PGE for at least the following reasons. First, the proposal suggests that the conversion to an LLC would cause PGE to be treated as a "disregarded entity" for tax purposes, which would constitute a deemed liquidation of PGE. This assertion is incorrect since a disregarded entity may only have one owner, whereas PGE is owned by Enron as well as PGE's preferred stockholders. Furthermore, because the PGE stock to be issued to the Enron creditors will be listed on the New York Stock Exchange at the time of transfer to Enron's creditors, PGE would be treated as a publicly traded partnership under Section 7704 of the Internal Revenue Code. Consequently, PGE would automatically be treated as a corporation for U.S. federal income tax purposes at the time of the transfer of the PGE stock to the Enron creditors.[1] Accordingly, for U.S. federal income tax purposes, the transfer of the LLC interests to Enron's creditors should be treated as the transfer of stock of a corporation and not as a transfer of assets creating increased tax benefits for PGE.

Second, in addition to the application of section 7704, we believe that under long-standing judicial doctrines, the scheme should be characterized as a sale of stock instead of assets, and, therefore, it would be ill-advised to attempt to implement such a scheme.

The Supreme Court denied a taxpayer's attempt to change the form of a transaction in a very similar tax-saving scheme in a well-known decision dating back to 1945. In Commissioner v. Court Holding Co., 324 U.S. 331, 334 (1945), a taxpayer who had an arrangement with a buyer to sell the property of a subsidiary corporation attempted to alter the income tax consequences of the sale by restructuring the transaction as a corporate liquidation followed by a sale. The Supreme Court held that a corporate liquidation will not be respected, as such, if the negotiations of a transaction have culminated in an understanding that is inconsistent with the form of the final transaction. As Justice Black succinctly stated,

> To permit the true nature of a transaction to be disguised by mere formalisms, which exist solely to alter tax liabilities, would seriously impair the effective administration of the tax policies of Congress.

Accordingly, if Enron were to attempt to alter the tax consequences of the existing Plan by undertaking such a scheme, we believe PGE would not achieve the intended tax benefits under well-established principles of U.S. federal income tax law.

In addition, we note that when tax avoidance is a principal purpose of a transaction, it is generally subject to greater scrutiny by the Internal Revenue Service ("IRS") (and other taxing authorities). Thus, if PGE were to engage in the foregoing scheme, not only could the IRS seek to disallow the increased tax basis and depreciation to PGE, but it could also seek to assert penalties against PGE. In such case, PGE ratepayers could both fail to realize the benefit under the proposal and end up paying higher rates.

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[1] Under Section 7704, if interests in a partnership or limited liability company are traded or available for trading on an established exchange, the entity will be treated as a corporation for U.S. federal income tax purposes. While Section 7704(c) provides certain exceptions for entity's with qualifying income (e.g., oil and gas exploration, production and transportation), PGE would not be eligible for the exceptions provided in Section 7704(c) since PGE's activities of production and sale of electricity are not qualifying income for purposes of the exception.