BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

DR 10, UE 88, UM 989

In the Matters of

The Application of Portland General Electric Company for an Investigation into Least Cost Plan Plant Retirement, (DR 10)

Revised Tariffs Schedules for Electric Service in Oregon Filed by Portland General Electric Company, (UE 88)

Portland General Electric Company's Application for an Accounting Order and for Order Approving Tariff Sheets Implementing Rate Reduction. (UM 989)

PORTLAND GENERAL ELECTRIC COMPANY'S OPENING BRIEF

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I. INTRODUCTION

Portland General Electric Company ("PGE") submits this Opening Brief to describe the issues that the Commission must decide in Phase I of this proceeding and to summarize PGE's proposals. We explain the legal foundation for the factual and policy decisions raised in our Opening Testimony.

II. SCOPE OF PHASE I

A. THIS FIRST PHASE IS AN EXAMINATION OF WHAT RATES THE COMMISSION WOULD HAVE APPROVED IN UE 88 HAD IT INTERPRETED ORS 757.355 TO PROHIBIT A RETURN ON PGE'S INVESTMENT IN TROJAN

Phase I of this proceeding is delineated in the Commission's October 18, 2004 Order ("Commission's Order on Scope").[1] The Commission's task is:

> [T]o undertake a retrospective examination of what rates would have been approved in UE 88 if the Commission had interpreted the authority delegated to it by the legislature in ORS 757.355 to not allow a return on investment in retired plant, as the Court of Appeals did in Citizens' Utility Board. Id. at 5.

The Commission will consider "those aspects of the ratemaking process in UE 88 that are affected by the Court of Appeals' statutory interpretation of ORS 757.355," with the goal of determining "what rates would have originally been set under this statutory interpretation." Id. at 6-7 (internal quotes omitted). The Commission's review will include, but is not limited to, three specific determinations in UE 88:

> 1) the appropriate recovery period for the Trojan investment balance; 2) the cost of capital effects of the utility's change of circumstances; and 3) the application of the net benefits formula given that PGE is precluded from recovering the cost of capital represented by the Trojan investment. Id. at 7.

[1] Order No. 04-597. Administrative Law Judge ("ALJ") Kirkpatrick divided this proceeding into three phases in a ruling on May 5, 2004. She subsequently defined the scope of the first phase (Phase I) in a Ruling dated August 31, 2004 ("ALJ's Ruling on Scope"). The Commission affirmed the ALJ's Ruling on Scope in its entirety.

This first phase will not address whether past or current rates should be adjusted, or whether refunds should be granted. Nor will the first phase address whether the Commission has the legal authority to order refunds. Commission's Order on Scope at 7-8. Such issues will be dealt with in a later phase, if necessary, after the Commission first determines what rates it would have approved in UE 88 had it interpreted ORS 757.355 to prohibit a return on PGE's investment in Trojan. ALJ's Ruling on Scope at 19. At the outset, "it is impossible to know whether any retroactive adjustment of rates will be necessary. Analysis could show end rates would remain the same as, be greater than or lesser than rates approved in UM 989 (and other relevant rate orders)." Id. Thus, the Commission has decided to defer to a later phase of this proceeding any reconciliation of the rates determined in Phase I with the rates that the Commission previously approved.

B. THE COMMISSION MUST DETERMINE PGE'S TOTAL REVENUE REQUIREMENT

The Circuit Court's remand orders require the Commission to engage in ratemaking in this proceeding. ALJ's Ruling on Scope at 17. In reconsidering its prior rate orders, the Commission must establish "just and reasonable" rates pursuant to ORS 757.020 and within the limitations of ORS 757.355 and ORS 757.140(2). Id. The first step of any ratemaking process by the Commission is determining the utility's total revenue requirement. Id. No single item in the revenue formula may be considered or modified in isolation because "a change in one item of the revenue formula may be offset by a corresponding change in another component of the formula." Id.; see also Commission's Order on Scope at 6. The Commission must take into account all relevant aspects of the utility's circumstances to determine a revenue requirement that fairly balances the interests of utility shareholders and customers and provides the basis for fair, just and reasonable rates.

C. THIS PROCEEDING PRESENTS UNIQUE ISSUES THAT REQUIRE A CAREFULLY TAILORED APPROACH

The Commission confronted unique and complex issues when it first dealt with the retirement of Trojan in DR 10 and UE 88. It must now confront those same issues within the framework of a complex procedural history that presents unique challenges of its own. In crafting a fair and reasonable result, the Commission must acknowledge traditional ratemaking principles while tailoring its ratemaking methods to the unique procedural circumstances of this proceeding.

1. THE COMMISSION MUST DEVELOP RATES THAT IMPLEMENT THE RATEMAKING POLICIES THE COMMISSION IDENTIFIED AT THE OUTSET OF DR 10 AND UE 88 WHILE OBSERVING THE COURT OF APPEALS' INTERPRETATION OF GOVERNING LAW

In the original proceedings in DR 10 and UE 88, the Commission had to develop a fair means of dealing with a generating plant retired for economic reasons that represented 15 percent of PGE's rate base. Given that retirement of Trojan was in the public interest, the Commission needed to set rates that allowed PGE to recover its prudent costs and that did not penalize PGE for its decision to retire Trojan before the end of its expected useful life. To accomplish these goals, the Commission approved recovery of PGE's investment in Trojan, plus a return on the undepreciated balance. This "return on" component allowed PGE to recover its costs of equity and debt capital associated with recovery of its investment over time. An important benefit of this approach was that rates remained stable and did not include recovery of PGE's entire remaining investment in Trojan immediately when UE 88 rates became effective. See *In Re PGE*, DR 10/UM 535, Order No. 93-1117 (Aug. 9, 1993); *In re PGE*, UE 88, Order No. 95-322 (Mar. 29, 1995).

The Circuit Court has declared that the Commission must return to the drawing board because the structure it developed in DR 10 and UE 88 to deal with PGE's

retirement of Trojan to achieve the least cost for customers was in error.[2] The Court of Appeals did not determine that the rates set by Order No. 95-322 were unjust or unreasonable. It held only that the Commission could not include a return on the Trojan investment. The challenge for the Commission will be to develop new rates that implement the Commission's ratemaking policies in a manner that does not violate the Court of Appeals' interpretation of governing statutes.

2. THIS IS THE FIRST TIME THE COMMISSION HAS BEEN REQUIRED TO RECONSIDER RATEMAKING DECISIONS MADE MANY YEARS IN THE PAST

The procedural history of DR 10 and UE 88, culminating in the remand orders of the Circuit Court, has led to this highly unusual situation in which the Commission must reconsider policy decisions that it approved nearly 12 years ago and rates that it approved nearly 10 years ago. In this unique proceeding, the Commission must step back in time and determine what rates it should have imposed in 1995, taking into account all relevant factual, legal and policy considerations, including the interpretation of the relevant statutes in the Court of Appeals' 1998 opinion and including new evidence and argument added to the reopened record. If the Commission determines in this phase that it would have set lower rates 10 years ago had it been informed of the Court of Appeals' interpretation of the relevant statutes, the Commission will then have to determine whether it should order any refunds to be made. The Commission has never engaged in such a process because it always has adhered to the view that it has no authority to order refunds of amounts collected pursuant to the filed rates. See Order No. 02-227 at 8-12.

[2] The remand from the Court of Appeals is different. It simply requires "further proceedings." It does not require any refunds or rate reductions. Rather, the Court of Appeals requires that any prospective rates must be free from the error the Court identified.

D. THE COMMISSION HAS THE DISCRETION TO ESTABLISH RATES BY A VARIETY OF METHODS WITHIN ITS CONSTITUTIONAL AND LEGISLATIVE AUTHORITY

Ratemaking is a legislative function delegated to the Commission, and the Commission has broad authority to employ various means in setting rates, as the Commission finds the circumstances require. *American Can Co. v. Lobdell*, 55 Or App 451, 463 (1983). As long as the Commission acts within its constitutional and statutory authority, it is "not obligated to employ any single formula or combination of formulas to determine what are in each case 'just and reasonable rates.'" *Pacific Northwest Bell Telephone Co. v. Sabin*, 21 Or App 200, 224 (1975). *See also* ALJ's Ruling on Scope at 14-15.

III. THE COMMISSION'S PRIMARY DUTY IS TO ESTABLISH FAIR AND REASONABLE RATES

In exercising its broad ratemaking authority, the Commission is guided by ORS 756.040(1), which directs the Commission to protect customers and the public from "unjust and unreasonable exactions and practices" and to establish "fair and reasonable rates." That statute defines "fair and reasonable rates" as follows:

> Rates are fair and reasonable for the purposes of this subsection if the rates provide adequate revenue both for operating expenses of the public utility . . . and for capital costs of the utility, with a return to the equity holder that is:
>
> (a) Commensurate with the return on investments in other enterprises having corresponding risks; and
>
> (b) Sufficient to ensure confidence in the financial integrity of the utility, allowing the utility to maintain its credit and attract capital.[3]

[3] We cite the current language of ORS 756.040(1). The statute was amended in 2001 to incorporate the controlling standard articulated in *Federal Power Comm'n. v. Hope Natural Gas*, 320 US 591 (1944). HB 3502, Oregon Laws 2001 Ch. 569. The amendment did not change either the law or the Commission's practice. *See* Paul Graham letter to Michael Grant, January 19, 2005.

The Commission is also guided by ORS 757.020, which provides that rates must be "reasonable and just."

IV. WHAT WE ARE RECOMMENDING AND WHY

PGE recommends that the Commission find that PGE should:

1. Recover the entire un-depreciated investment in Trojan, based on the positive net benefit resulting from comparing the cost of closure to the cost of continued operation and including the effects of the Court of Appeals' interpretation in the cost of closure and steam generator replacement in the cost of continued operation;

2. Leave $80 million of the Trojan assets in the plant-in-service accounts;

3. Offset the $111 million Boardman gain against the un-depreciated Trojan assets that were not still plant-in-service and amortize the remainder over one year;

4. Be allowed a required return on equity of 11.85 percent;

5. Defer a portion of its 1995 and 1996 (four months, to match the period of Trojan recovery) net variable power costs, for recovery over the subsequent ten years; and

6. Recover the AMAX termination payment, pre-UE-88 deferred power costs and SAVE incentive over the same ten years.

Alternatively, should the Commission determine that a 17-year amortization period for Trojan is more appropriate, PGE recommends that the Commission find that PGE should:

1. Recover the entire un-depreciated investment in Trojan, based on the positive net benefit resulting from comparing the cost of closure to the cost of continued operation and including the effects of the Court of Appeals' interpretation in the cost of closure and steam generator replacement in the cost of continued operation;

2. Receive 20 percent of the positive net benefit created through its economic retirement of Trojan, spread evenly over 17 years;

3. Leave $80 million of the Trojan assets in the plant-in-service accounts;

4. Offset the $111 million Boardman gain against the un-depreciated Trojan assets that were not still plant-in-service;

5. Be allowed a required return on equity of 13.1 percent; and

6. Recover the AMAX termination payment, pre-UE-88 deferred power costs and SAVE incentive over three years beginning with UE 88 rates.

Under either of these recommended alternatives, application of these factual and policy decisions will result in fair and reasonable rates that meet the Commission's regulatory policy goals. It will promote actions that PGE took to achieve the least cost to customers. It will serve to allocate costs to customers fairly over time. Finally, it will maintain PGE's ability to access capital so that service remains safe and adequate. We address each of these steps below.

V. LEGAL AUTHORITY

At this time, PGE has identified nine policy and factual decisions that the Commission may choose to address. These decisions arise from the specific rate determinations affected by the Court of Appeals' interpretation and the ratemaking techniques appropriate to consider as a result. This section outlines each issue and examines the Commission's authority to consider it in these proceedings.

A. A REDUCED AMORTIZATION PERIOD WOULD RESULT IN FAIR AND REASONABLE RATES

In the original UE 88 proceedings, the Commission did not want to put PGE in a worse financial position than it would have been in if it had continued to operate Trojan.

It was reasonable at that time to retain Trojan's original amortization period, which expired in 2011, because the Commission believed that it could set rates including a return on PGE's investment. Now that the Commission is unable to set rates on this basis, the Commission should revisit the question of the proper amortization period for Trojan. If PGE

must recover its investment over 17 years without earning a return, it will be in a significantly worse financial position than if it had kept Trojan in operation. Lesh Section IV A; PGE Panel Section II.

The Commission has already acknowledged that a change in the ground rules for UE 88 would require reconsideration of all affected ratemaking decisions in the docket, including the appropriate amortization period. In UM 989, it stated that it "could determine that if Trojan should not have been included in rate base, PGE should have recovered the entire Trojan balance immediately instead of over 17 years . . . ." UM 989, Order No. 02-227 at 10-11.

As the Commission also explained in UM 989, it has the authority to prescribe accounting treatment for public utilities pursuant to ORS 757.105 to ORS 757.140. This authority includes the power to prescribe amortization periods for utility assets. Id. at 12-13. ORS 757.140 does not require the Commission to delay recovery of an investment over a number of years, particularly when the useful life of the asset has ended. And as the Commission underscored in UM 989, nothing in *CUB* precludes it from shortening Trojan's recovery life because the Court of Appeals expressly declined to address this issue. UM 989, Order No. 02-227 at 13; *CUB*, 154 Or App at 712 n.5.

B. THE COMMISSION SHOULD CONSIDER THE EFFECTS OF THE COURT OF APPEALS' INTERPRETATION ON PGE'S AUTHORIZED RETURN ON EQUITY AND CAPITAL STRUCTURE

A central aspect of the Commission's ratemaking in UE 88 was a determination of PGE's authorized cost of capital. The Commission should now consider how the Court of Appeals' disallowance of return on investment affects both PGE's return on equity and cost of debt. Lesh Section IV B; Makholm.

There are two statutory bases for revisiting this issue. First, ORS 756.040(1)(a) provides that a utility's return on investment (both debt and equity) must

be commensurate with the return on investments in other enterprises having corresponding risks. With respect to equity, the Commission should consider whether exclusion of any return on the Trojan balance changes PGE's risk profile and, therefore, the enterprises with which PGE's allowed return on investment should be comparable. With respect to debt, the Commission should consider how the Court of Appeals' interpretation has affected the regulatory environment in which PGE operates which, in turn, may affect its credit ratings and debt costs.

Second, ORS 756.040(1)(b) provides that fair and reasonable utility rates must allow a return on investment that is "[s]ufficient to ensure confidence in the financial integrity of the utility, allowing the utility to maintain its credit and attract capital." With the elimination of the Trojan balance from rate base, the Commission should consider whether it must increase the approved rate of return on investment in UE 88 or revise PGE's capital structure for setting rates in order to comply with ORS 756.040(1)(b).

Further, the history of ORS 757.355 suggests that cost of capital impacts were anticipated when the initiative passed. The Voter's Pamphlet advised that passage of Ballot Measure No. 9 would require the Commission to authorize "much" higher rates of return for utilities.[4]

C. THE COMMISSION SHOULD REVISIT THE NET BENEFITS FORMULA IN LIGHT OF THE COURTS' DECISIONS

In UE 88, the Commission used a net benefits test to determine the point at which PGE customers were indifferent between continued operation of Trojan and shutdown

[4] "If these current charges (85 cents per month for PGE customers using 1,200 kilowatt hours) were outlawed by this bill, consumers would pay higher, not lower electric bills. As an alternative, says the Public Utility Commissioner, he would be required to allow the utilities a 'much higher rate of return.'" Voters Pamphlet statement in Opposition to Measure No. 9. Order No. 93-1117, Appendix A at 21.

coupled with the replacement of its output. Under this formula, a net benefit to customers exists if:

$$(X + Y) > (X + Z)$$

where: X = Unamortized investment in Trojan
Y = Expected allowable long-term costs of continued Trojan operation
Z = Replacement resource costs

UE 88, Order No. 95-322 at 33.

The Commission's analysis of the Trojan investment ("X") assumed that customers would be responsible for paying the return on PGE's undepreciated Trojan investment over the 17-year amortization period, whether the plant continued in operation or was closed. The Court of Appeals' interpretation has altered this analysis. Given that customers enjoy a significant cost savings in the closure scenario from the preclusion of return on investment, the Commission should revisit the entire net benefits issue. Lesh Section IV C.

The Commission has both the power and the duty to reconsider or reapply the net benefits formula. ORS 756.568 authorizes the Commission to consider additional evidence, with no restrictions on its scope and nature, in the course of rescinding, suspending or amending an order. Moreover, the Circuit Court's remand of UM 989 requires the Commission to revisit all aspects of the UE 88 ratemaking process that are affected by the Court of Appeals' interpretation of ORS 757.355, as well as take new evidence if necessary. *See* Commission's Order on Scope at 6-7 and ALJ's Ruling on Scope at 16-17. As ALJ Kirkpatrick noted, the application of the net benefits formula is a core issue implicated by the question "What rates would have been approved in UE 88 if ORS 757.355 had been interpreted to prohibit a return on Trojan?" Id. The Commission should, therefore, revisit the entire net benefits issue in these proceedings.

D. SHARE THE SAVINGS/INCENTIVES

The Commission generally relies on a utility's costs as the basis for setting rates. However, the Commission has authority to adopt alternative ratemaking conventions that advance the goal of adequate service at fair and reasonable rates. Lesh Section IV C. In the early 1990s, for example, the Commission departed from the convention of basing rates on cost in order to motivate utilities to acquire energy efficient resources. In Order No. 91-98, the Commission adopted the SAVE program for PGE. The incentive component of SAVE allowed PGE to earn revenues in addition to the allowed rate of return on capital investment over a period of 15 years. It also allowed PGE to share the savings from the non-use of electricity based on the value of verified energy efficiency savings that exceed benchmark levels. Order No. 91-98 at 3. In fact, the Commission regularly permits the utility to share the savings or gains in order to provide appropriate incentives to the utility and align interests. In utility property sales dockets, the Commission frequently authorizes the utility to retain 5 percent of the gains generated in order to give the utility incentive to maximize the sales price. *See* In re PacifiCorp, UP 168, Order No. 00-112 at 12 (February 29, 2000). The Commission has authorized power cost adjustment clauses with sharing formulas that permit the utility to keep a portion of savings because the Commission believes such a sharing mechanism motivates the utility to undertake actions beneficial to its customers. *See* In re Portland General Electric, UE 115, Order No. 01-777 at Appendix D (August 31, 2001).

In UE 88, the Commission's cost-based net benefits analysis yielded a slightly negative amount. The Commission might have reached a different result if it had examined whether the retirement of Trojan to achieve the least cost for customers created efficiency benefits that justify a departure from strict cost analysis. In these remand proceedings, the Commission should take up this issue. It should consider how the positive effects of Trojan's

closure should be reflected in subsequent rates.

E. A JUST AND REASONABLE RATE WILL ALLOW PGE A RETURN ON THE FACILITIES THAT REMAINED IN SERVICE FOLLOWING TROJAN'S CLOSURE

Facilities at Trojan continued to provide important service to customers and to the public at large. PGE continued to operate certain Trojan facilities following plant closure: the spent fuel pool, its related systems and the administrative buildings at Trojan. Indeed, it was required to operate these facilities because it is under a legal duty to ensure the security of the site and protect public health and safety. *See* Quennoz/Peterson/Dahlgren.

PGE raised the question of how these facilities should be categorized in the original UE 88 proceedings. The issue at that time was whether, for accounting purposes, these facilities should be included in FERC Account 101 (Plant in Service) or FERC Account 182.2 (Unrecovered Plant and Regulatory Study Costs). PGE sought inclusion of the facilities in Account 101 because they protect public health and safety, provide security, and provide office space and facilities for the employees who remain on the site. The Commission disagreed, concluding that "the continuing activities at Trojan are related to decommissioning, not productive operation of the facility." Because both accounts were included in PGE's rate base, the Commission's decision on this accounting issue had no effect on the rates set in UE 88.

It is now consequential whether the facilities remaining in service at Trojan should be distinguished from other facilities on the site. The Commission should include these facilities in rate base because they remain "used and useful in the public service." Lesh Section IV D. Moreover, ORS 757.355 does not forbid this result.

ORS 757.355 provides that a utility cannot include in rate base property "not presently used for providing utility service to the customer." In *CUB*, the Court of Appeals began its analysis of ORS 757.355 by noting that "rate base" is a term of art in utility law,

and that rate base has historically excluded property that is "neither used nor . . . useful to the public service." 154 Or App at 709, quoting *Pacific Tel. & Tel. Co. v. Wallace*, 158 Or. 210, 231 (1938). The Court found that ORS 757.355 merely expresses this traditional ratemaking principle:

> ORS 757.355 would appear to be less an innovative new form of restraint on utility rates than the embodiment of an old one: property that is not "reasonably necessary to and actually providing utility service" is ineligible for either inclusion in the rate base or for a rate of return payable by utility customers. 154 Or App at 710.

It then concluded that property that has ceased to be reasonably necessary and actually used is governed by the same principles as property that has not yet been placed in service. Id.

CUB did not address what it means for property to be "reasonably necessary and actually used." The Court made clear that ORS 757.355 simply embodies traditional ratemaking principles and must be understood in light of other statutory provisions.

The first step in determining whether property is "used for providing utility service to the customer" for purposes of ORS 757.355 is to develop a full understanding of "utility service." Oregon utility law defines "service" very broadly. ORS 756.010(8) states that "'[s]ervice' is used in its broadest and most inclusive sense and includes equipment and facilities related to providing the service or the product served." *See Northwest Climate Conditioning Ass'n. v. Lobdell*, 79 Or App 560, 565 (1986) (infrequent repair activity falls within definition of service). In the telephone context, the Commission has held that a service provider's publication of a Yellow Pages directory is a "telecommunications service." *In re Pacific Northwest Bell Tel. Co.*, 110 PUR 4th 132, 1989 WL 418536 (OPUC Dec. 29, 1989). *See also West Penn Power Co. v. Pa. PUC*, 578 A2d 75, 76 (Pa. Commw. Ct. 1990) ("utility service" is not limited to the distribution of electricity but also "includes 'any and all acts' related to that function."); *Bookstaber v. PECO Energy Co.*, 2004 WL 2983032 (Pa. PUC Nov. 23, 2004) (utility violated its statutory duty to provide reasonable "service" by

failing to give a customer adequate information about its policies and procedures).

These cases show that "utility service" includes activities that are ancillary to the actual delivery of power. A recent Florida case shows that rate base can include property that is presently used to perform necessary and ongoing functions related to past services. In *In Re Gulf Power Co.*, 218 PUR 4th 205, 2002 WL 1349501 (Fla. PSC June 10, 2002), the utility sought to include in rate base an office building floor that it partly used for storage and records retention. The premise that a records storage area can be included in rate base was not controversial. These records relate to the past provision of utility service, but the utility was allowed to include the storage area in rate base because records retention is an ongoing activity relating to past utility service.

The Commission should find that property used for ongoing functions related to the past provision of utility service is "presently used for providing utility service to the customer." This reading of ORS 757.355 recognizes that idle property must be excluded from rate base. However, it also acknowledges that modern safety and environmental laws require a utility to engage in significant activities that benefit customers at a retired plant.

The era when utilities could simply lock up and walk away from a retired plant has long passed. The concept of "used and useful in the public service" should reflect this reality, and the Commission should find that PGE is "providing utility service" when it discharges its obligations at Trojan. These activities arise directly from the production of electricity in the past. Furthermore, the facilities PGE continues to operate at Trojan are also "used and useful" because, as PGE noted in the UE 88 proceedings, its employees use them to perform crucial public health and safety functions.

F. THE COMMISSION CAN CONSIDER BALANCE SHEET OPTIONS IN THESE PROCEEDINGS

At the time of the original UE 88 proceedings, PGE's balance sheet included a customer credit of approximately $111 million from the sale of Boardman ("Boardman

Gain"). Just eight months later, in UE 93, the Commission took up the Boardman Gain. It approved a Stipulation between Staff and PGE which offset most of the Boardman Gain against the unamortized balance of the power cost deferrals previously authorized in UM 529, UM 594, and UM 692, the AMAX deferral approved in UE 79, and the SAVE incentive. The Stipulation offset the remaining $20 million in Boardman Gain against a portion of the unamortized Trojan investment. See Appendix B, *In re Portland Gen'l Electric Co.*, UE 93, Order No. 95-1216 (Nov. 20, 1995).

If PGE could have anticipated the Court of Appeals' decision in *CUB* at the time of UE 88, it would have advocated offsetting the entire Boardman Gain against its Trojan investment. Now that UE 88 has been reopened, the Commission can consider whether such an offset is appropriate. Lesh Section IV E. The Commission has broad authority to prescribe accounting rules for recovery and depreciation. See UM 989, Order No. 02-227 at 12-13, citing ORS 757.105-.140. Moreover, the decisions in UE 93 and UM 989 attest to the Commission's authority to use the offset principle to simplify a utility's balance sheet if it is in the interests of customers and the utility.

G. THE COMMISSION MAY CHOOSE TO CONSIDER A POWER COST DEFERRAL

If the Commission shortens the amortization period for the Trojan investment, it may choose to consider a deferral of a portion of the UE 88 test year power costs for one year beginning upon the effective date of UE 88 rates. Lesh Section IV F. This one-year deferral of power costs would coincide with the one-year recovery period of the Trojan balance. It would serve to reduce rates for the one-year period and spread those costs over the recovery period of the deferred balance. Accordingly, we suggest the possibility of a power cost deferral only under a one-year recovery period. An appropriate recovery period for the deferred balance would be through March 2005.

Deferred accounting is a well-recognized ratemaking tool, particularly

appropriate in extraordinary circumstances like the Trojan shutdown. In fact, from 1992 through 1994, the Commission authorized three deferred accounting orders for replacement power costs caused by the Trojan outage and shutdown. Along with the 2000-2001 California Power Crisis, the Trojan shutdown is a paradigm example of the type of extraordinary event that warrants deferred accounting treatment. UM 1071, Order No. 04-108.

ORS 757.259(2)(e) authorizes deferred accounting for "identifiable utility expenses or revenues, the recovery or refund of which the commission finds should be deferred in order to minimize the frequency of rate changes or the fluctuation of rate levels or to match appropriately the costs borne by and benefits received by ratepayers." Spreading the 1995 power costs through 2005 matches "costs borne by and benefits received by ratepayers." If Trojan is recovered in one year, customers after 1995 will pay lower power costs. A deferral of 1995 power costs matches the customers that receive that benefit with the power cost payments that create it.

H. A "FAIR AND REASONABLE" RATE WILL ALLOW PGE TO RECOVER THE DEBT COSTS FOR ITS INVESTMENT IN TROJAN

After the closure of Trojan, PGE continued to carry significant long-term debt costs that it recovered through UE 88 rates. Now that the Court of Appeals has held that PGE cannot receive a "profit" on its investment in Trojan, the Commission should take these debt costs into account in determining what a "fair and reasonable" rate would have been at the time of the UE 88 proceedings. Lesh Section IV G. PGE should be allowed to recover the interest paid on the debt portion of its Trojan investment.

At least one other utility commission has permitted recovery of debt costs for investments that were reasonable and prudent, but not "used and useful." In *In re Commonwealth Edison Co.*, No. 87-0427, 139 PUR 4th 165, 1993 WL 73575 (Ill. Commerce Comm'n 1993), the Illinois Commission concluded that the utility's generating facility was

not used and useful to the extent it exceeded the weather-adjusted peak load plus a 20 percent margin. Applying its "needs and economic benefits" test, the Commission disallowed a return on equity for a plant that was not used and useful. However, it allowed "a full return on the preferred stock and debt portions of reasonable and prudent new plant investment, and a full recovery of all reasonable and prudent costs . . . ." 1993 WL 73575 at * 37.

Here, as in the Illinois case, PGE borrowed funds and prudently incurred long-term financing costs when it built Trojan. Including these costs in rates comports with the Commission's duty to "balance the interests of the utility investor and the consumer in establishing fair and reasonable rates." ORS 756.020; see also DR 10 (noting that ratemaking may involve cost sharing between customers and investors).

The inclusion of long-term financing costs in rates does not conflict with the Court of Appeals' decision in *CUB* or the statutes it construed. The Court of Appeals had no occasion to consider this issue in *CUB*. ORS 757.355 does not implicate the recovery of long-term financing costs because they are an expense for PGE, and not a source of profits. If anything, these costs are akin to PGE's unamortized investment in Trojan because PGE incurred them to build Trojan in the first place.

VI. THE COMMISSION HAS A CONSTITUTIONAL DUTY NOT TO SET A CONFISCATORY RATE

The Commission is not only under a statutory duty to set a just and reasonable rate in these proceedings, it must also avoid setting a confiscatory rate in violation of the federal Constitution. An unreasonably low utility rate can constitute a taking under the Fifth Amendment. *Duquesne Light Co. v. Barasch*, 488 US 299, 310, 109 S Ct 609, 617(1989).

A utility rate is constitutionally permissible if it "enable[s] a company to operate successfully, to maintain its financial integrity, to attract capital, and to compensate its investors for the risk assumed . . . . " *FPC v. Hope Natural Gas Co.*, 320 US 591, 605, 64 S Ct 281, 289 (1944); *see also Bluefield Water Works & Improvement Co. v. Public Service*

Comm'n of West Virginia, 262 US 679, 692-93, 43 S Ct 675, 679 (1923) ("A public utility is entitled to such rates as will permit it to earn a return . . . equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties."). In *Duquesne*, the Supreme Court noted that the risks a utility faces stem in large part from the rate methodology because it is otherwise relatively immune to market risks. The Court cautioned that a change in regulatory scheme that requires investors to bear the risk of bad investments at some times while denying them the benefit of good investments at others "would raise serious constitutional questions." 320 US at 315.

The Court of Appeals' interpretation of ORS 757.355 significantly alters the ratemaking principles that informed UE 88. It therefore raises the constitutional dangers highlighted in *Hope* and *Duquesne*. The Commission should develop a rate structure that provides full recovery of its Trojan investment and a reasonable rate of return on equity given the costs and risks PGE now faces in the wake of the Court of Appeals' decision.

VII. THE COMMISSION MAY RELY ON EVIDENCE FROM THE ORIGINAL DR 10, UE 88 AND UM 989 PROCEEDINGS AS WELL AS TAKE NEW EVIDENCE

The unique procedural posture we are in leads to a somewhat cumbersome record. The Commission may rely on both the evidence originally presented a decade ago and the evidence presented today. The Commission has broad fact-finding powers in these proceedings. When an administrative agency reopens a matter, the new proceedings are part of the original case, and the agency "may base its decision on the record of the original hearing and on the evidence presented at the rehearing." *Village of Prentice v. Transp. Comm'n of Wisconsin*, 123 Wis 2d 113, 122-23, 365 NW 2d 899, 903 (1985); *see also City of Omaha v. Wade*, 1 Neb App 1168, 1173, 510 NW 2d 564, 567 (1993); *Lambert Constr. Co. v. State of New Hampshire*, 115 NH 516, 519, 345 A2d 396, 398 (1975).

The Commission may also consider new evidence. When a reviewing court remands a case to an administrative agency after finding that it erred as a matter of law, the agency must respect the court's resolution of the legal issue. On remand, however, the agency is not constrained from enforcing the legislative policy committed to its jurisdiction. *Securities & Exchange Comm'n. v. Chenery Corp.*, 332 US 194, 201 (1947). The agency can reopen the factual record, make new findings, and consider different approaches and rationales. *See Federal Trade Comm'n. v. Morton Salt Co.*, 334 US 37, 55, 68 S Ct 822 (1948) (Commission may hear other evidence and make other findings on remand); *United States v. Morgan*, 307 US 183, 192, 59 S Ct 795, 800 (1939) (same); *City of Charlottesville v. FERC*, 774 F2d 1205, 1212 (DC Cir 1985) (same).

These basic principles of administrative law apply to the Commission. As the Oregon Supreme Court has confirmed, a reviewing court does not tell the Commission what evidence to hear or what formula to apply. *See Pacific Tel. & Tel. Co. v. Hill*, 229 Or 437, 486, 367 P2d 790 (1962). Rather, it is for the Commission to determine what additional evidence to receive and what additional findings to make. Id. The Commission is free to receive more testimony if it wishes. Id. at 472.

There is also statutory authority for the Commission's power to rely on new evidence. As the ALJ noted, ORS 756.568 expressly authorizes the Commission to "rescind, suspend or amend any order," after giving the public utility an opportunity to be heard pursuant to ORS 756.500 to 756.610, which necessarily entails the unrestricted power to consider additional evidence. (ALJ's Ruling on Scope at 14.)

In these proceedings, therefore, the Commission will need to consider both the existing record and the new evidence presented. We highlight in our opening testimony those portions of the existing factual record that seem most relevant to the determination now at issue.

VIII. THE COMMISSION SHOULD IDENTIFY THE EIGHT-MONTH PERIOD WHEN ORDER NO. 95-322 WAS IN EFFECT AS THE RELEVANT PERIOD FOR RETROACTIVE REVIEW OF RATES

Finally, the Commission must define the appropriate rate period under consideration in these remand proceedings. URP has contended that the Commission should reexamine rates for the entire period between April 1, 1995, when UE 88 rates were implemented, and October 1, 2000, when Trojan was removed from PGE's rate base.

URP ignores the inconvenient fact that it never sought judicial review of the intervening rates set in UE 93 and UE 100, Order Nos. 95-1216 and 96-306. Each of those orders became conclusively final 60 days after the Commission set them. They were outside the scope of the court proceedings that led to these remanded proceedings, and they are beyond challenge today. The only period that should be at issue in these remanded proceedings is the eight months during which Order No. 95-322 was in effect.

A. PROCEDURAL HISTORY

To understand the proper scope of these proceedings, it is helpful to recall the decade-long odyssey that led to the Circuit Court's remand orders. On January 4, 1993, PGE closed Trojan, and on February 9, 1993, it filed a request for a declaratory ruling on issues regarding ratemaking for a retired utility plant. The Commission opened DR 10, and on August 9, 1993, it issued Order No. 93-1117. This order stated that the Commission would consider allowing return on investment in retired plant if it found such recovery to be in the public interest under ORS 757.140(2)(b). The Commission denied reconsideration in Order No. 93-1763. URP, CUB and the PPC appealed the DR 10 Orders to the Marion County Circuit Court ("Circuit Court"), which affirmed them in Circuit Court Nos. 94C-10372 and 94C-10417 ("DR 10 Circuit Court Orders").

On November 9, 1993, PGE filed a request for a general rate increase. The Commission opened UE 88. On March 25, 1995, the Commission entered Order No. 95-322. Pursuant to the DR 10 Orders, the Commission allowed return on investment. CUB and

URP appealed Order No. 95-322 to the Circuit Court.

While the appeal was pending, the Commission opened UE 93 and set new rates in Order No. 95-1216. This Order took effect on November 28, 1995. It was never appealed.

In April and May of 1996, the Circuit Court issued Order Nos. 95C-11300 and 95C-12542 ("UE 88 Circuit Court Orders"). These Orders affirmed the portion of Order No. 95-322 that allowed PGE to recover its Trojan investment, but reversed the portion of the Order that allowed PGE to earn a return on that investment.

In late 1996, the Commission opened UE 100 and entered a new rate order, Order No. 96-306. It took effect on December 1, 1996, and like the rates in UE 93, these rates were never challenged.

The Oregon Court of Appeals considered both the DR 10 and UE 88 Circuit Court orders in a consolidated proceeding. In *CUB*, the Court ruled that the Commission was authorized to compensate utilities only for the principal amount of undepreciated investment in unused or retired property, but could not authorize return on investment. 154 Or App at 716-17. The Court reversed and remanded the DR 10 Circuit Court Orders and affirmed the UE 88 Circuit Court Orders.

On April 28, 1999, the Oregon Supreme Court granted petitions for review of the Court of Appeals' decision, but it held the case in abeyance pending settlement discussions and legislative action. On August 22, 2000, PGE entered into settlement agreements with Staff and CUB. PGE filed an Application for an Accounting Order and Revised Tariff Sheets that sought Commission approval of the settlements. The Commission opened UM 989, and on September 29, 2000 it entered Order No. 00-601, which approved the settlements and allowed the tariff sheets to go into effect. Pursuant to the settlements, the rates set in UM 989 removed Trojan from rate base. URP challenged the settlements. On

March 25, 2002, the Commission upheld the settlements and denied the complaint in Order No. 02-227. URP then appealed Order No. 02-227 to the Circuit Court.

In November of 2003, the Circuit Court remanded the DR 10 and UE 88 Orders (Order Nos. 93-117, 93-1763, and 95-322) to the Commission. On January 9, 2004, the Circuit Court reversed Order No. 02-227 and remanded it to the Commission.

The Commission reopened the dockets in DR 10, UE 88 and UM 989 in compliance with the Circuit Court's two remand orders.

1. THESE PROCEEDINGS ARE LIMITED TO REVISITING THE RATE DETERMINATIONS IN UE 88

There is good reason why both ALJ Kirkpatrick and the Commission have emphasized that these remand proceedings focus on the rate determinations in UE 88. The only Commission orders that were ever before the courts were those in DR 10, UE 88 and UM 989. All of these orders related to the UE 88 rates in effect from April to November of 1995.

Although the UE 88 rates were superseded in UE 93 and UE 100, no party ever sought judicial review of the intervening rate orders. Oregon law regarding the jurisdiction of the courts to review the Commission's orders is quite clear. ORS 756.565 provides:

> All rates, tariffs, classifications, regulations, practices and service fixed, approved or prescribed by the Public Utility Commission and any order made or entered upon any matter within the jurisdiction of the commission shall be in force and shall be prima facie lawful and reasonable, until found otherwise in a proceeding brought for that purpose under ORS 756.580 to 756.610.

ORS 756.580, in turn, grants certain circuit courts jurisdiction over suits to set aside findings and orders of the Commission. However, this statute places an important limit on the courts' powers of review. ORS 756.580(4) provides that "[u]nless application is made for rehearing or reconsideration of the order, any such suit must be commenced within 60 days after the

date of service of the order in the proceeding before the commission" (emphasis added).

Pursuant to this statutory scheme, the rates set in UE 93 and UE 100 are final and conclusive. Even if the courts had attempted to assert jurisdiction over the UE 93 and UE 100 rates, they would have been barred for the simple reason that no one ever filed a timely suit under ORS 756.580. These rates—and the revenues PGE collected during the five-year period they were in effect—are thus outside the scope of the remand orders.

B. THE COMMISSION SHOULD ADDRESS THE EFFECT OF *CUB* ON THE RATES SET IN UE 93 AND UE 100

As we have argued in the previous section, these proceedings are limited to the eight-month period that UE 88 was in effect. Nevertheless, we ask the Commission to make findings relative to the periods when UE 93 and UE 100 were effective. Then if the courts rule on appeal that the rate period in question includes UE 93 and UE 100, the Commission and the parties will not have to go through this process again to determine the effect for that period.

IX. CONCLUSION

For the foregoing reasons, the Commission should find that the relevant rate period is the eight-month term when UE 88 rates were in effect. The Commission should find that UE 88 rates were fair and reasonable. The Commission should reaffirm its approval

of the stipulations reached in UM 989 and find the $10 million rate reduction approved in Order No. 00-227 fair and reasonable and a proper exercise of the Commission's discretion.

DATED this 15th day of February, 2005.

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