BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

AR 499

In the Matter of the Adoption of Permanent Rules Implementing SB 408 Relating to Utility Taxes.	))))))	OPENING COMMENTS OF THE INDUSTRIAL CUSTOMERS OF NORTHWEST UTILITIES ON PROPOSED RULES

Pursuant to the procedural schedule in this Docket, the Industrial Customers of Northwest Utilities ("ICNU") submits these Opening Comments regarding the draft rules to implement Senate Bill ("SB") 408 distributed by Public Utility Commission of Oregon ("OPUC" or "Commission") Staff on July 25, 2006. ICNU supports adoption of the draft rules, with the minor revisions discussed in these Opening Comments, as accurately implementing the letter and spirit of SB 408. ICNU applauds the Commission's decision in Order No. 06-400, which resolved the implementation of SB 408's "properly attributed" language by providing thoughtful, straightforward, and balanced guidance regarding a controversial issue. Staff's draft rules correctly apply the "Apportionment method" adopted by the Commission and appropriately address the other aspects of the statute.

ICNU addresses issues raised in the July 21, 2006 workshop and explains its concerns about the proposed Section 11 of the draft rules in the comments below. Attached to ICNU's Opening Comments as Attachment 1 are ICNU's proposed revisions to the draft rules.

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I. The Commission Should Follow the Department of Revenue's Practice of Applying the Apportionment Method on a Situs Basis

ICNU supports the Commission's adoption of the Apportionment method to implement SB 408's "properly attributed" language. As the Commission described in Order No. 06-400, the Apportionment method is well established, widely accepted, and has a lengthy history of application in Oregon. Furthermore, the Apportionment method is easy for customers to understand and will allow the Commission and other parties to look to existing Oregon tax policies, statutes, and rules for guidance regarding attribution issues that arise in the future. The Commission's resolution of this important issue establishes an equitable and workable means of addressing the problems that SB 408 was enacted to correct.

Staff's draft rules correctly apply the Apportionment method as described by the Commission, and ICNU supports adoption of the codification of the method in Section 3 of Staff's draft rules. During the July 21, 2006 workshop, certain investor-owned utilities ("IOUs") questioned whether determining the amount of the utility's property, sales, and payroll for purposes of the Apportionment method should include all utility property everywhere or just the utility property located in Oregon. The 1985 Oregon Supreme Court case that the Commission cited in Order No. 06-400 unequivocally states that the Apportionment method compares the amounts of property, sales, and payroll in Oregon to the total value everywhere:

> The three-factor formula works in the following way: Dollar values are assessed to each of three aspects of taxpayer's business: property, sales and payroll. Each of these factors is a fraction. The numerator of each fraction is the *Oregon* portion of the value and the denominator is the total value everywhere.

Order No. 06-400 at 5 (*quoting* Twentieth Century-Fox Film v. Dep't of Rev., 299 Or. 220, 224 (1985) (emphasis added). Section 3 of Staff's draft rules correctly reflects the Apportionment

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method's comparison of the property, sales, and payroll *in Oregon* to the total amounts for the affiliated group. ICNU believes that the draft rules accurately reflect both the Commission's decision in Order No. 06-400 and the Oregon Supreme Court's description of how Oregon has applied the Apportionment method.

The IOUs have argued that the application of the Apportionment method on a state "situs" basis for the utility would produce undesirable results because it excludes from the calculation utility property or payroll outside of Oregon, but this argument ignores the nature of the Apportionment method. First, the calculations using the multi-factor formula in the Apportionment method ultimately produce a value that represents the overall percentage of taxes paid that are "properly attributed" to regulated utility operations in Oregon.

Second, using the Apportionment method to determine the amount of taxes paid that is properly attributed to regulated utility operations is no different than the many other aspects of ratemaking that produce a result that is reasonable, but potentially imprecise. Indeed, one of the fundamental premises of ratemaking is that utility rates will be set in an instant in time, knowing that the assumptions upon which rates are based will not turn out as expected. Re PacifiCorp, OPUC Docket No. UE 170, Order No. 06-379 at 13 (July 10, 2006). In PacifiCorp's case, for example, a certain portion of utility payroll in Oregon may be related to providing service in other states, but that portion would nevertheless be included in the utility-specific value (the numerator) of the "payroll" ratio for purposes of the Apportionment method. Likewise, a certain portion of PacifiCorp's payroll in other states may be related to serving Oregon customers, but that portion would be excluded from the utility-specific amount in calculating the payroll ratio. Although neither of these hypothetical amounts will be exact, the

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overall result will produce a reasonable outcome with an acceptable margin of error, and it represents only one of three factors to consider in the Apportionment method.

Third, if the Commission is concerned that applying the property, sales, and payroll factors on a situs basis would lead to skewed results, Order No. 06-400 identifies a means to address that issue that does not involve departing from how Oregon has applied the Apportionment method in the past. Order No. 06-400 at 5 n.4. The Commission specifically stated that it would consider suggestions regarding how to weight the various factors in applying the Apportionment method. Id. ICNU believes that weighting the factors to address concerns about applying the Apportionment method on a situs basis is more appropriate than requiring the Commission to develop a separate method for determining the amount of property, sales, and payroll that is attributable to Oregon regulated utility operations. Part of the benefit of applying the Apportionment method is the opportunity to look to the Department of Revenue's statutes, rules, and application of the policy for guidance when questions arise. If the Commission develops its own method for determining the property, sales, and payroll from Oregon regulated utility operations, its ability to rely on the Department of Revenue's decisions will be severely limited.

Finally, the standard by which electric rates are judged is whether the outcome is just and reasonable overall, not whether the methods used to determine the rates are reasonable. Federal Power Comm'n et al. v. Hope Natural Gas Co., 320 U.S. 591 (1944). In other words, the Commission has broad discretion to apply the Apportionment method on a situs basis to determine the amount of "taxes paid" that is properly attributed to regulated utility operations as long as the utility's overall rates are not unjust or unreasonable.

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ICNU proposes one clarification of Section 3 of the draft rules. Staff proposes to adopt the definitions for property, payroll, and sales that are contained in ORS §§ 314.650 through 314.675. In the tax code, these ratios are used to allocate total business income to Oregon, to which an Oregon tax rate is applied to produce Oregon tax amounts. In the proposed rules, federal taxes paid are already determined, and the ratios are used to apportion a share of total taxes to Oregon regulated utility operations. As defined in the tax rules, "sales" may not always include all items that are taken into account in determining taxes paid, e.g., in certain circumstances, dividend income. The OPUC has already modified the Apportionment method as appropriate (e.g., the numerator of the ratios includes only regulated property, not all Oregon property), and the Commission needs to clarify that all income that is taken into account to calculate the amount of taxes paid must also be included in "sales" for developing the sales ratio. The Commission's rules should be clarified on this point.

II. The Rules Should Include a Consistent Process to Determine the Amount of Taxes Paid That Is Properly Attributed to Regulated Utility Operations but Provide Some Flexibility to Address the Specifics of Local Income Taxes

The Commission stated in Order No. 06-400 that the process for determining the amount of local income taxes paid that is properly attributed to regulated utility operations should be the same as for state and federal taxes. ICNU believes that having a consistent method to make the determinations under SB 408 for federal, state, and local taxes is important, and the draft rules appropriately establish such a procedure. It is unclear what local income taxes may apply in the future, and having a well-established and consistent methodology for making the necessary determinations is a benefit for all parties involved. As such, ICNU urges the Commission to adopt the provisions in the draft rules that call for determining the amount of

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local income taxes paid that is properly attributed to regulated utility operations according to the process outlined in Order No. 06-400.

ICNU recognizes that the current discussion of rate adjustments based on local income taxes focuses primarily on the Multnomah County Business Income Tax, which utilities collect from customers through an amount that is separately stated on customer bills. See OAR § 860-022-0045. In cases in which the utility collects amounts from customers as a separate line-item charge and the utility also is the taxpayer that actually pays the local income tax, it may be sufficient for the Commission to authorize a SB 408 rate adjustment that merely reflects a "true up" of the amount of taxes collected from customers to the amount of taxes that the utility pays to the local taxing authority. In order to recognize that local taxes may present unique circumstances to consider, ICNU recommends that the Commission retain some flexibility in its rules regarding local income taxes in order to provide the ability to address the specific local income tax issues that may arise in the future.

III. SB 408 Provides the Commission the Authority to Order an Adjustment to Ensure Compliance with IRS Normalization Requirements

The parties also discussed during the July 21, 2006 workshop whether application of the Apportionment method could result in a violation of Internal Revenue Service ("IRS") normalization requirements if a SB 408 rate adjustment included amounts related to deferred taxes associated with regulated operations outside of Oregon. ICNU believes that Section 3(8) of SB 408 provides the Commission with the authority to ensure that an SB 408 rate adjustment does not violate IRS normalization requirements. That Section states:

> Notwithstanding subsections (1) to (7) of this section, the commission may authorize a public utility to include in rates:

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> (a) Deferred taxes resulting from accelerated depreciation or other tax treatment of utility investment; and
>
> (b) Tax requirements and benefits that are required to be included in order to ensure compliance with the normalization requirements of federal tax law.

Regardless of disputes over any other Section of SB 408, it was the unequivocal purpose of this Section that a SB 408 rate adjustment would not result in violation of IRS normalization principles. Both the plain language of SB 408 and the legislative history confirm this fact. See, e.g., Work Session on SB 408, Senate Comm. on Bus. and Economic Development, 73d Leg., Regular Sess., 4-5 (May 31, 2005) (Statements of Dexter Johnson, Legislative Counsel). Avoiding any potential violation of IRS normalization requirements was an issue that was raised early and often in the legislative debate regarding SB 408, and there is no dispute that the statute is intended to avoid such a result.

In order to fully address any concerns that a particular adjustment to rates would violate normalization requirements or any other provision of the tax code, it would be appropriate for a utility to make known at the time that it files the tax report that such a violation could occur and propose an adjustment to address the issue. If, for example, a utility is concerned that a proposed surcredit included in the tax report would include amounts related to deferred taxes associated with regulated operations outside of Oregon, the utility should state that concern to the Commission in the tax report filing. Informing the Commission about this potential issue as soon as possible will facilitate addressing any concerns and help enable the Commission to make the appropriate modifications to the proposed surcredit. As such, ICNU urges the Commission to add a provision to the draft rules that would require a utility to address in the tax report that the utility believes at the time of tax report filing whether authorizing the

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surcharge or surcredit in the tax report would violate the normalization requirements of federal tax law. The utility should also be required to explain how the normalization requirements would be violated and propose a solution to address the issue. The specific language that ICNU proposes is included in Attachment 1.

IV. The Commission Should Calculate the SB 408 § 3(12)(a) "Cap" to Reflect Taxes Paid Based on all Operations Supported by the Utility's Regulated Revenues

The Commission correctly recognized in Order No. 06-400 that the language in SB 408 § 3(12)(a) does not represent merely the taxes that would be paid if the utility was a stand-alone operation and that this provision calls for some attribution of taxes paid. Order No. 06-400 at 4 n.3. ICNU is not proposing a specific method for the calculation of the "with" and "without" amounts, but ICNU believes that any method that the Commission adopts for this calculation must account for all tax liabilities and credits that are supported, directly or indirectly, by the utility's regulated revenues. Specifically, the "with" calculation must reflect the actual corporate structure, including the utility. However, the "without" calculation must not simply consist of the "with" calculation after removing the utility. Instead, the utility and all financial impacts within the affiliated group that would not exist but for the participation of the utility in the affiliated group must also be removed in the "without" calculation. This includes tax deductions to affiliates rising from debt-related interest payments when those payments are supported by utility revenues. The Commission noted in Order No. 06-400 that Section 3(12)(a) identifies the portion of total taxes paid that would have been received by government "but for" the utility's regulated operations. As such, it is appropriate and necessary to devise a method of performing the "with and without" calculation taking into account the interest deductions on such debt.

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V. The Calculation of Properly Attributed for State Income Taxes Should Be Based on the Taxes Paid by the Companies in the Affiliated Group

Order No. 06-400 addresses whether the amount of state income taxes paid that is properly attributed to regulated utility operations should be based on the consolidated group that files a consolidated federal income tax return or the unitary group that files a state income tax return. Order No. 06-400 at 6. The Commission explicitly recognized in the Order that the federal affiliated group might not necessarily include the same companies as the state unitary group, and the Commission stated that to "comply with the language of SB 408 . . . the various unitary groups that include entities in the consolidated federal return must be aggregated to determine the amounts of taxes paid by the affiliated group in Oregon." Id. ICNU believes that the Commission's decision is consistent with the language and intent of SB 408. The statute explicitly defines "affiliated group" as the group of corporations of which the utility is a member "and that files a consolidated federal income tax return" and states that ratepayers should not be charged for more tax than "the affiliated group pays to units of government and that is properly attributed to the regulated operations of the utility." ORS § 757.268(6), (13). Determining the amount of state taxes paid that is properly attributed to regulated utility operations based on aggregating the members of the affiliated group that pay income taxes in Oregon reflects the plain language of SB 408.

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VI. The Rules Implementing SB 408 Should Not Create an Additional Procedural Right for Utilities to Challenge Rate Adjustments Ordered by the Commission

ICNU disagrees with the proposal in Section 11 of the draft rules to create a procedural right to challenge an SB 408 rate adjustment order by the Commission. Section 11 provides:

> At any time, a utility may file a claim that a rate adjustment under the automatic adjustment clause violates ORS 756.040 or other applicable law. In making a determination regarding a potential violation of ORS 756.040, the Commission will perform an earnings review using the utility's results of operations report for the applicable tax year. The utility filing the claim will bear the burden of proof to substantiate the claim.

This rule would create an additional procedural right for a utility to challenge any SB 408 rate adjustment despite the fact that such a procedure lacks any basis in either SB 408 itself or any other statute that governs proceedings before the Commission. ICNU urges the Commission to remove this provision from the final rule, because it is contrary to SB 408 and creates a mechanism for constant regulatory litigation. This would represent poor public policy.

The legislature specifically articulated in SB 408 the procedures that it intended to govern the establishment, implementation, and review of rate adjustments under an SB 408 automatic adjustment clause, and the Commission's rules should not create procedural rights that are inconsistent with that intent. SB 408 § 3(4) sets out specific timeframes for the Commission to review the tax reports, determine whether an automatic adjustment clause is required, and, if so, order the utility to establish such a clause. Subsections 3(9) and 3(10) set out the reasons for the Commission to review a particular rate adjustment and the procedure that the Commission should follow in such a review. These subsections provide that the Commission may terminate an adjustment clause that would have a material adverse effect on customers, and the statute

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specifies that the Commission must hold a hearing and issue a written order before ordering such a termination.

The fact that SB 408 specifies particular procedures is significant, because this is the only process for post-decision review of an order authorizing an automatic adjustment clause. Despite the fact that the utilities argued in the legislature that SB 408 allegedly may result in violations of ORS § 756.040 or other standards, the legislature did not include in the statute any procedure for reviewing those claims. Indeed, other than the "material adverse impact" test that focuses on customers and the statutory right to seek reconsideration or judicial review of a Commission decision that applies to all parties in any proceeding, neither SB 408 nor any other statute or rule indicates that the legislature intended some alternative post-decision review process under SB 408.

The fact that Section 11 would create a utility-specific procedural right to challenge the Commission's decisions under SB 408 reflects a poor public policy that the Commission should not incorporate in its rules. ICNU believes that Section 11 of the draft rules should be rejected because the right that all parties have to request reconsideration or seek judicial review provides an adequate opportunity to challenge a Commission decision under SB 408, and any additional procedural rights are unnecessary. Nevertheless, if the Commission agrees that creating such a unique procedural right is appropriate, then sound policy dictates that all parties should have the benefit of that procedure. The broad language of Section 11 authorizes review of claims that an automatic adjustment clause "violates ORS 756.040 or other applicable law." Although ORS § 756.040 has been exclusively portrayed in the SB 408 debate as a statute that protects utility interests, the statute explicitly empowers the Commission to

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"represent" and "protect" customers. Thus, a claim regarding violation of ORS § 756.040 applies with equal force to customers. Furthermore, given that the rule allows challenges based on any applicable law, including SB 408 itself, the opportunity to assert such a challenge applies equally to customers as well.

If parties are concerned that the process governing the SB 408 automatic adjustment clause does not provide an opportunity to evaluate the constitutionality of a rate adjustment prior to that adjustment taking effect, then it would be appropriate for the parties and the Commission to address that issue earlier in the process of implementing a surcharge or surcredit. A simple means to ensure that the legality of a rate adjustment is addressed prior to the adjustment taking effect would be to include in the rules a requirement that the utility address in the tax report whether the utility believes that implementing the surcharge or surcredit proposed in the report result in confiscatory or otherwise unlawful rates. This will allow the Commission and the parties to address this issue in the course of determining the appropriate SB 408 rate adjustment, rather than creating a utility-specific right to assert an after-the-fact challenge to the Commission's decision. The specific language that ICNU proposes is included in Section 4 of the rule included in Attachment 1.

VII. Conclusion

ICNU appreciates the Commission's consideration of these comments and urges the adoption of Staff's draft rules with the exception of Section 11.

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Dated this 31st day of July, 2006.

Respectfully submitted,

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Attachment 1

860-022-0041

Annual Tax Reports and Automatic Adjustment Clauses Relating to Utility Taxes

(1) This rule applies to regulated investor-owned utilities that provided electric or natural gas service to an average of 50,000 or more customers in Oregon in 2003, or to any successors in interest of those utilities that continue to be regulated investor-owned utilities.

(2) As used in this rule:

(a) "Affiliated group" means the group of corporations of which the utility is a member and that files a consolidated federal income tax return.

(b) "Deferred taxes" for purposes of the utility means the total deferred tax expense of regulated operations as reported in the FERC deferred tax expense accounts that relate to the year being reported in the utility's results of operations report or tax returns.

(c) "FERC" means the Federal Energy Regulatory Commission.

(d) "Income" means taxable income as determined by the applicable taxing authority or regulatory taxable income when reporting or computing the stand-alone tax liability resulting from a utility's regulated operations.

(e) "Investment" means capital outlays for utility property used to provide regulated service to customers.

(f) "Local taxes collected" means the total amount collected from customers under the local tax line-item of customers' bills calculated on a separate city or county basis.

(g) "Pre-tax income" means the utility's net revenues before income taxes and interest expense, as determined by the Commission in a general rate proceeding.

(h) "Properly attributed" means the share of taxes paid that is apportioned to the Oregon regulated operations as calculated in section (3) of this rule.

(i) "Regulated operations of the utility" means those activities of a utility that are subject to rate regulation by the Commission.

(j) "Results of operations report" means the utility's annual results of operations report filed with the Commission.

(k) "Revenue" means retail revenues from ratepayers in Oregon as defined by FERC, excluding other operating revenues as defined by FERC and supplemental schedules not included in the utility's revenue requirement and adjusted for any rate adjustment imposed under this rule.

(l) “Revenue requirement” means the total revenue the Commission authorizes a utility an opportunity to recover in a general rate proceeding or other general rate revision, including an annual automatic adjustment clause under ORS 757.210.

(m) "Tax" means a federal, state or local tax or fee that is imposed on or measured by income and that is paid to a unit of government, but does not include a franchise fee or privilege tax.

(n) "Taxes authorized to be collected in rates” means the following for federal and state income taxes:

(A) The amount calculated by multiplying the following three values:

(i) The revenue the utility collects, using information from the utility’s results of operations report;

(ii) The ratio of the net revenues from regulated operations of the utility to gross revenues from regulated operations of the utility, calculated using the pre-tax income and revenue the Commission authorized in establishing rates and revenue requirement; and

(iii) The effective tax rate used by the Commission in establishing rates for the time period covered by the tax report as set forth in the most recent general rate order or other order that establishes an effective tax rate, calculated as the ratio of total income tax expense in revenue requirement to pre-tax income.

(B) For purposes of paragraph (2)(m)(A), when the Commission has authorized a change during the tax year for gross revenues, net revenues or effective tax rate, the amount will be calculated using a weighted average of months in effect.

(o) "Taxes paid" means net amounts received by units of government from the utility or from the affiliated group and properly attributed to regulated operations of the utility, adjusted as follows:

(A) Increased by the amount of tax savings realized as a result of charitable contribution deductions allowed because of the charitable contributions made by the utility;

(B) Increased by the amount of tax credits on the tax return that are associated with investment by the utility in the regulated operations of the utility, which may include, but are not limited to, tax credits associated with renewable electricity production, to the extent the expenditures giving rise to the tax credits and tax savings resulting from the tax credits have not been taken into account by the Commission in the utility's most recent general ratemaking proceeding; and

(C) Adjusted by deferred taxes related to the regulated operations of the utility. The utility must initially use its results of operations report to establish the amount of deferred taxes. If the utility does not believe that the results of operations report sufficiently reflects the amount of the utility’s deferred taxes for the applicable tax year, the utility may also use its tax returns for the tax year as a supplemental source for calculating the deferred taxes adjustment as a

separate submission. Deferred taxes do not include deferred tax items related to an adjustment under section (9) of this rule.

(p) “Taxpayer” means the utility or the affiliated group that files income tax returns with units of government.

(q) "Units of government" means federal, state and local taxing authorities.

(3) The amount of income taxes paid that is properly attributed to regulated operations of the utility is calculated as follows:

(a) The amount of federal income taxes paid to units of government that is properly attributed to the regulated operations of a utility is the product of the following two figures:

(A) The total amount of federal income taxes paid by the taxpayer; and

(B) The average of the ratios calculated for the utility’s property, payroll and sales, as defined in ORS 314.650 through 314.675, using amounts for regulated operations of the utility in Oregon in the numerator and amounts for the taxpayer in the denominator.

(b) The amount of state income taxes paid to units of government that is properly attributed to the regulated operations of a utility is the product of the following two figures:

(A) The total amount of Oregon income taxes that is paid by the taxpayer; and

(B) The average of the ratios calculated for the utility’s property, payroll and sales, as defined in ORS 314.650 through 314.675, using amounts for regulated operations of the utility in Oregon in the numerator and amounts for the taxpayer in Oregon in the denominator.

(c) The amount of local income taxes paid to units of government that is properly attributed to the regulated operations of a utility is the product of the following two figures for each local taxing authority in Oregon:

(A) The total amount of income taxes paid by the taxpayer to the local taxing authority; and

(B) The average of the ratios calculated for the utility’s property, payroll and sales, as defined in ORS 314.650 through 314.675, using amounts for regulated operations of the utility in the local taxing authority in the numerator and amounts for the taxpayer in the local taxing authority in the denominator.

(4) By October 15 of each year, each utility must file a tax report with the Commission.

(a) The tax report must contain the following information for each of the three preceding fiscal years:

(~~a~~A) The amount of federal and state income taxes paid to units of government by the taxpayer;

(~~b~~B) The amount of the federal and state income taxes paid that is incurred as a result of income generated by the Oregon regulated operations of the utility, calculated as the difference between the taxpayer's tax liability computed with and without the regulated operations of the utility;

(~~c~~C) The amount of federal and state income taxes paid to units of government by the taxpayer that is properly attributed to the Oregon regulated operations of the utility, as calculated in section (3) of this rule;

(~~d~~D) The amount of federal and state taxes income taxes authorized to be collected in rates for the Oregon regulated operations of the utility;

(~~e~~E) The amount of the difference between the amount in subsection (4)(d) of this rule and the lowest of the amounts in subsections (4)(a), (4)(b) and (4)(c), after making the adjustments defined in subsection (2)(o) of this rule;

(~~f~~F) The amount of local income taxes paid to units of government by the taxpayer, by local taxing authority;

(~~g~~G) The amount of local income taxes paid to units of government by the taxpayer that is incurred as a result of income generated by the regulated Oregon operations of the utility, calculated as the difference between the taxpayer's tax liability computed with and without the regulated operations of the utility, by local taxing authority;

(~~h~~H) The amount of local income taxes paid to units of government by the taxpayer that is properly attributed to Oregon regulated operations of the utility, as calculated in section (3) of this rule, by local taxing authority.

(~~i~~I) The amount of local income taxes collected from Oregon customers, by local taxing authority;

(~~j~~J) The amount of the difference between the amount in subsection (4)(i) of this rule and the lowest of the amounts in subsections (4)(f), (4)(g) and (4)(h) after making the adjustments defined in subsection (2)(o) of this rule, by local taxing authority; and

(~~k~~K) The proposed surcharge or surcredit rate adjustments for each customer rate schedule to charge or refund customers the amount of the differences in subsections (4)(e) and (4)(j) of this rule.

(b) The tax report also must include statements by the utility addressing:

(A) Whether the utility believes that authorizing the surcharge or surcredit rate adjustments in subsection (4)(a)(K) would violate any normalization requirement of federal tax law. If the utility states that authorizing the surcharge or surcredit rate adjustments would result in such a violation, the utility should provide a detailed explanation regarding the potential violation and propose an adjustment to resolve the potential violation.

(B) Whether the utility believes that that authorizing the surcharge or surcredit rate adjustments in subsection (4)(a)(K) would result in unconstitutional rates or would violate any other provision of applicable law. If the utility states that authorizing the surcharge or surcredit rate adjustments would result in such a violation, the utility should provide a detailed explanation regarding the potential violation.

(5) In calculating the amount of taxes paid under section (4) of this rule:

(a) "Taxes paid" must be allocated to each tax year employed by the utility for reporting its tax liability in the following manner:

(A) For each tax liability shown on an initial or amended tax return for the immediately preceding tax year, which return is filed on or before the date the tax report is due for such tax year, to the tax year for which such return is filed.

(B) For each tax liability or tax adjustment shown on an amended tax return or made as a result of a tax audit, that is filed, paid or received after the date the tax report is due for the applicable tax year, to the tax year in which the related tax liability or tax adjustment is recognized by the utility for accounting purposes.

(C) Taxes paid must include any interest paid to or interest received from units of government with respect to tax liabilities.

(b) When a utility's fiscal year or parent changes, and a partial year consolidated federal income tax return is filed during the year, taxes paid must be calculated in the manner defined by ORS 314.355 and OAR 150-314.355. For purposes of this rule, the taxes paid amount will reflect a weighted average of the months in effect related to each filing.

(6) The utility must explain the method used for calculating the amounts in this rule and provide copies of all workpapers and documents supporting the calculations. Each utility must obtain and provide any information requested by the Commission to implement and administer this rule.

(7) The Commission will establish an ongoing docket for each of the October 15th tax report filings. If a petitioner is granted intervention and becomes a party to the docket, they may have access to all such tax report filings at the time the tax report filings are filed with the Commission, subject to the terms of any protective order issued.

(a) Within 20 days following the October 15 tax report filings, an Administrative Law Judge will conduct a conference and adopt a schedule.

(b) Within 180 days of the tax report filings, the Commission will issue an order making the findings in section 8 of this rule.

(8) The Commission's order in subsection 7(b) of this rule will contain the following findings:

(a) Whether the taxes authorized to be collected in rates for any of the three preceding fiscal years differs by $100,000 or more from the amount of taxes paid to units of government that are properly attributed to the Oregon regulated operations of the utility;

(b) For the preceding fiscal year, the difference between the amount of federal and state income taxes paid to units of government by the taxpayer that is properly attributed to the Oregon regulated operations of the utility and the amount of taxes authorized to be collected in rates;

(c) For the preceding fiscal year, the difference between the amount of local income taxes paid to units of government by the taxpayer that is properly attributed to the Oregon regulated operations of the utility and the amount of local taxes collected in rates; and

(d) Any other finding or determination necessary to implement the automatic adjustment clause.

(9) Upon entry of an order finding a difference of $100,000 or more in section (8) of this rule, the utility must file an amendment to its automatic adjustment clause tariff to be effective each June 1, unless otherwise authorized by the Commission. The amended tariff must implement a rate adjustment applying to taxes paid to units of government and collected from ratepayers for each fiscal year beginning on or after January 1, 2006.

(a) The utility must establish a balancing account and automatic adjustment clause tariff to recover or refund the difference determined by the Commission in subsection (8)(b) of this rule through a surcharge or surcredit rate adjustment.

(b) A utility that is assessed a local income tax must establish a separate balancing account and automatic adjustment clause tariff for each local taxing authority assessing such tax. The utility must apply a surcharge or surcredit on the bills of customers within the local taxing authority assessing the tax. The amount of the surcharge or surcredit must be calculated to recover or refund the difference determined by the Commission in subsection (8)(c) of this rule.

(c) Any rate adjustment must be calculated to amortize the difference determined by the Commission in subsections (8)(b) and (8)(c) of this rule over a period authorized by the Commission.

(d) Any rate adjustment must be allocated by customer rate schedule according to equal percentage of margin for natural gas utilities and equal cents per kilowatt-hour for electric utilities, unless otherwise authorized by the Commission.

(e) Each balancing account must accrue interest at the Commission-authorized rate for deferred accounts. For purposes of calculating interest, the amount of the difference calculated in this

section of the rule will be deemed to be added to the balancing account on January 1 of the year following the tax year.

(f) The automatic adjustment clause must not operate in a manner that allocates to customers any portion of the benefits of deferred taxes resulting from accelerated depreciation or other tax treatment of utility investment or regulated affiliate investment required to ensure compliance with the normalization method of accounting or any other requirements of federal tax law.

(g) By October 15, 2006, each utility must seek a Private Letter Ruling from the Internal Revenue Service on whether the utility's compliance with Senate Bill 408, this rule, or any other relevant guidance or authorities would cause the utility to fail to comply with federal normalization requirements or other requirements of federal tax law. While a utility's request for a Private Letter Ruling is pending, or a related Revenue Ruling is pending, no rate adjustment will be implemented, but interest will accrue according to subsection (9)(e) of this rule on the amount of any rate adjustment determined by the Commission pursuant to subsections (8)(b) and (8)(c) of this rule.

(10) No later than 30 days following the Commission's findings in section (8) of this rule, any person may file to terminate the automatic adjustment clause on the basis that it would result in a material adverse effect on customers. In the event of a filing under this section, the applicable rate adjustment will not be implemented until the Commission makes its determination. If the Commission decides against termination, interest will accrue according to subsection (9)(e) of this rule on the final amount of the rate adjustment. The person filing the claim will bear the burden of proof to substantiate the claim.

~~(11) At any time, a utility may file a claim that a rate adjustment under the automatic adjustment clause violates ORS 756.040 or other applicable law. In making a determination regarding a potential violation of ORS 756.040, the Commission will perform an earnings review using the utility's results of operations report for the applicable tax year. The utility filing the claim will bear the burden of proof to substantiate the claim.~~

(11~~2~~) The Commission may disclose, or any intervenor in a utility tax report proceeding may obtain and disclose, the amount by which the amount of taxes that units of government received from the utility or from the affiliated group differs from the amount of costs for taxes collected, directly or indirectly, as part of rates paid by customers, including whether the difference is positive or negative. The Commission will not disclose or authorize disclosure of any information that is exempt from disclosure under the Public Records Law (ORS 192.410-192.505).

Stat. Auth.: ORS Ch. 183, 756, 757 & 759
Stats. Implemented: ORS 756.040, 756.060, 757.267 & 757.268
[Hist.: PUC 5-2005(Temp), f. & cert. ef. 9-15-05 thru 3-13-06]

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July 31, 2006

Via Electronically and US Mail

Public Utility Commission
Attn: Filing Center
550 Capitol St. NE #215
P.O. Box 2148
Salem OR 97308-2148

Re: In the Matter of the Adoption of Permanent Rules Implementing SB 408 Relating to Utility Taxes
Docket No. AR 499

Dear Filing Center:

Enclosed please find an original and two (2) copies of the Opening Comments of the Industrial Customers of Northwest Utilities on Proposed Rules in the above-captioned Docket.

Please return one file-stamped copy of the document in the self-addressed, stamped envelope provided. Thank you for your assistance.

Sincerely yours,

/s/ Ruth A. Miller
Ruth A. Miller

Enclosures
cc: Service List

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that I have this day served a copy of the foregoing Opening Comments of the Industrial Customers of Northwest Utilities on Proposed Rules, upon the parties, on the official service list for AR 499, by causing the same to be electronically served, to those parties with an email address, as well as mailed, postage-prepaid, through the U.S. Mail.

Dated at Portland, Oregon, this 31st day of July, 2006.

/s/ Ruth A. Miller
Ruth A. Miller

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