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November 18, 2005

**VIA ELECTRONIC MAIL
AND U.S. MAIL**

Oregon Public Utility Commission
Attn: Filing Center
550 Capitol Street, N.E., #215
P.O. Box 2148
Salem, Oregon 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 one (1) copy of the **Northwest Industrial Gas Users' Reply Comments on Section 3(13)(e)(B) and (C)** in the above-referenced Docket. This was filed electronically with the OPUC on this date, and will be served both electronically and by U.S. Mail on those parties listed on the OPUC's current Service List.

Thank you for your assistance.

Respectfully submitted,

/s/ Edward A. Finklea

Edward A. Finklea

EAF/nh
Enclosures
cc: Current Service List

**BEFORE THE PUBLIC UTILITY COMMISSION
OF OREGON**

AR 499

In the Matter of the Adoption of Permanent)	
Rules Implementing SB 408 Relating to)	NORTHWEST INDUSTRIAL GAS
Utility Taxes)	USERS' REPLY COMMENTS ON
)	SECTION 3(13)(e)(B) AND (C)
)	
)	

Pursuant to the schedule adopted by Administrative Law Judge ("ALJ") Logan in the above-referenced docket, the Northwest Industrial Gas Users ("NWIGU") submit these Reply Comments regarding the meaning of Section 3(13)(e)(B) and(C). By Order dated November 3, 2005, ALJ Logan posed the following additional question:

Does SB 408 require that the Oregon Public Utility Commission ("OPUC" or "Commission"), in determining the amounts identified in 3(13)(e)(B)(C), to use the numbers calculated from test year data that the Commission has previously authorized?

NWIGU hereby responds to the Opening Comments of NW Natural and Portland General Electric with these Reply Comments.

- 1. The language of SB 408 and the purpose of the law requires the Commission to use test year data used when establishing rates to determine the amounts identified in 3(13)(e)(B) and (C).**

Section 3(13)(e) of SB 5408 states:

"Taxes authorized to be collected in rates means the product determined by multiplying the following three values:

- “(A) The revenues the utility collects from ratepayers in Oregon adjusted for any rate adjustment imposed under this section;
- “(B) The ratio of the net revenues from regulated operations of the utility to gross revenues from regulated operations of the utility, as determined by the commission in establishing rates; and
- “(C) The effective tax rate used by the commission in establishing rates.”

As NWIGU noted in its Opening Comments on this issue, by choosing the phrases “as determined by the commission in establishing rates” and “used by the commission in establishing rates” Section 3(13)(e) is clear on its face that to measure “taxes authorized to be collected in rates” the focus must be on the tax figures used when establishing current rates. The tax figure used when establishing rates will reflect the utility’s share of the consolidated company’s tax liability. Any adjustment in subsequent years must continue to focus on the portion of the consolidated Company’s tax liability that is properly attributed to the utility’s operations, not simply on the tax liability of the utility as if it were a stand alone entity.

NW Natural claims that “serious anomalies” could follow if the Commission used the net revenue and effective tax rate from a prior rate proceeding when measuring taxes authorized in the annual filings. NW Natural wants the Commission to make adjustments in the annual filings so that additional taxes are simply a function of the utility’s revenues. It is NW Natural’s focus on the utility as a stand-alone entity that could undermine the intent behind SB 408.

A simple example helps focus the debate over this provision of SB 408. Assume that in a 2005 rate proceeding the utility affiliate of a consolidated company was allowed to include in its

rates \$75 million as its tax liability. When the 2005 tax report is filed, the consolidated company shows a \$100 million total tax liability. The consolidated company, however, had losses from unregulated affiliates such that the tax liability properly attributed to the utility affiliate is \$50 million. Thus, when the 2005 tax report is filed, due to SB 408, the utility's ratepayers will receive a rate credit in order to shelter the customers from paying \$25 million in what otherwise would be phantom taxes.

Under SB 408, if no 2006 rate case is filed by the utility affiliate mentioned above, but when actual results of 2006 are available, the utility will file its tax report. Assuming the utility's revenues have grown in the ensuing year, the utility's tax liability, as a stand-alone entity, will also have grown. Does that fact alone mean that an upward adjustment in the utility's rates is warranted under SB 408? NWIGU does not believe that SB 408 intended such a result.

Instead, the focus must still be on the utility's share of the consolidated company's tax liability. Continuing with the above example, assume that the consolidated company's tax liability declines in 2006 by \$20 million due to even greater losses by an unregulated affiliate than in 2005. On a stand-alone basis, the utility affiliate can show that its revenues have increased enough to cause the utility to have a 5 percent higher tax liability than the \$75 million assumed in rates. NW Natural claims that under these circumstances, its ratepayers should see a rate increase to reflect the higher tax liability of the stand-alone entity, even though the consolidated company has a lower overall tax liability than it did in the year rates were set.

What would be the proper adjustment under this circumstance? If the utility is allowed to adjust rates upward to reflect its higher tax liability as a stand alone-entity, even though the tax liability of the consolidated company has declined, then phantom taxes will be in the utility's rates in

2006. Under this example, the very purpose of SB 408 would be eroded in the year after rates were set. Neither the language of Section 3(13)(e) nor the intent of the law can support such a result. The proper result under this example is that taxes paid properly attributed to the utility in 2006 are lower than in 2005, and thus ratepayers should see more than a \$25 million downward adjustment to rates. Otherwise phantom taxes are allowed to creep back into rates in 2006.

The above example illustrates that the focus of SB 408 always starts with what the tax liability is in rates compared to what tax liability is properly attributed to the utility affiliate of a consolidated company. The focus should not be on the tax liability of the stand-alone entity.

Under normal circumstances, a utility's revenues will grow year to year so long as it has a growing customer base. But if in its implementation of SB 408 the Commission shifts its focus to the stand-alone utility, rather than the utility's proper share of a consolidated entities tax liability, the purpose of SB 408 will be eroded. The Commission must maintain its focus on the utility's share of the consolidated company's overall tax liability when implementing SB 408, or phantom taxes will continue to be collected in rates despite the clear intention of the Legislature in enacting SB 408.

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DATED: This 18th day of November, 2005.

/s/ Edward A. Finklea

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that I caused to be served the foregoing NORTHWEST INDUSTRIAL GAS USERS' REPLY COMMENTS ON SECTION 3(13)(e)(B) AND (C) on the attached Service List obtained on November 18, 2005 from the Oregon Public Utility Commission's Website as follows:

[XX] by **MAILING** a full, true and correct copy thereof in a sealed, postage-paid envelope, addressed as shown on the attached Service List, and deposited with the U.S. Postal Service at Portland, Oregon, on the date set forth below;

[XX] **and** by **electronic mail** ("e-mail") to those parties on the Oregon Public Utility Commission's Website Service List who listed an e-mail address.

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