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August 4, 2005

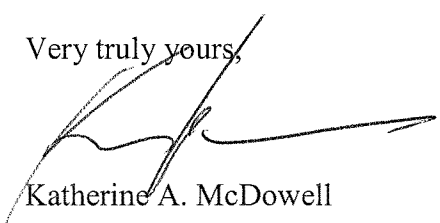
VIA ELECTRONIC FILING

PUC Filing Center
Public Utility Commission of Oregon
PO Box 2148
Salem, OR 97308-2148

Re: PacifiCorp's Opening Posthearing Brief
Docket UE 170

Enclosed for filing please find an original and five copies of PacifiCorp's Opening Posthearing Brief in the above-referenced docket. A copy of this filing was served on all parties to this proceeding as indicated in the attached certificated of service.

Very truly yours,



Katherine A. McDowell

KAM:knp
Enclosure
cc: Service List

BEFORE THE PUBLIC UTILITY COMMISSION
OF OREGON

UE 170

In the Matter of PACIFIC POWER & LIGHT's (d/b/a PacifiCorp) Request for a General Rate Increase in the Company's Oregon Annual Revenues.	**PACIFICORP'S OPENING POSTHEARING BRIEF**

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Pursuant to Administrative Law Judge Logan's June 14, 2005 Memorandum, PacifiCorp (or the "Company") submits this Opening Posthearing Brief.

I. INTRODUCTION

After various stipulations and updates to the Company's filing, the Company now requests a revenue requirement increase of approximately $52.5 million with a rate effective date of October 4, 2005. This constitutes an overall increase of 6.3 percent. Taking into consideration the end of Schedule 94's UM 995 deferral on July 25, 2005, adoption of the Company's proposed revenue requirement would leave customers' rates virtually unchanged with only an 0.7 percent overall increase.

As PacifiCorp has stated since it first filed this case, the outcome is critical to PacifiCorp and its customers in terms of ensuring that PacifiCorp's credit ratings and financial status remain strong at a time when it faces significant capital investments. For this reason, we are grateful that the parties have worked closely and collaboratively with the Company to settle virtually all of the revenue requirement issues raised in this case. The major issues remaining in the case, consolidated tax adjustments and RVM, invoke legal or policy issues that created impediments to a negotiated outcome.

For legal and policy reasons, the Commission should reject the consolidated tax adjustments proposed by Staff, CUB and ICNU. These adjustments would contravene the Commission's statutory obligation to prevent cross-subsidization by maintaining the separation of regulated and unregulated utility operations and would also violate the Commission's current administrative rules. Moreover, none of the adjustments make the requisite factual showing that PacifiCorp has been burdened by the expense that created the consolidated tax savings in a manner that justifies the adjustment.

Another important policy issue in this case is the Company's proposed RVM for setting its Transition Adjustment beginning November 2005. The Company's proposal was filed to comply with Commission Order 04-516 in UM 1081, and was a product of the

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workshops held before and after that order. Staff supports the Company's RVM proposal and the power costs updates associated with it, as set forth in the third Partial Stipulation. While ICNU and CUB oppose the RVM, neither has proposed practical alternatives for calculation of the Transition Adjustment. To avoid returning to square one in UM 1081, and because its RVM is otherwise fair and reasonable, PacifiCorp urges adoption of its proposed RVM.

ICNU reserved a series of miscellaneous issues as the parties negotiated the various Partial Stipulations on revenue requirement in this case. Staff supports PacifiCorp's position on each of the reserved ICNU issues. None of these issues warrant additional downward adjustments in PacifiCorp's already moderate proposed revenue requirement.

II. PROCEDURAL BACKGROUND

PacifiCorp set forth a complete procedural history of this case in its Prehearing Brief. The following procedural milestones have occurred since that filing:

- On July 15, 2005, the Utility Reform Project withdrew its testimony submitted in this case.
- Hearings were held on July 20 and 21, 2005. Cross-examination was waived on all of the Company's witnesses, including its expert witnesses on tax, except Doug Larson, PacifiCorp's policy witness, and Christy Omohundro, PacifiCorp's witness for its Proposed Transition Adjustment Mechanism (or "RVM").
- The parties to the first and second Partial Stipulations entered into a fourth Partial Stipulation, dated July 29, 2005. The fourth Partial Stipulation resolved the majority of remaining issues in this case, as follows: (1) cost of capital, (2) pensions, (3) rate spread and rate design, (4) bill proration, and (5) rate change effective date. This Stipulation reduced PacifiCorp's revenue requirement in the November 12, 2004 filing to approximately $52.5 million.

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III. ARGUMENT

A. The Commission Should Reject Staff's and Intervenors' Proposed Consolidated Tax Adjustments Because They Are Contrary to Law and Commission Policy and Unsupported by the Evidence in This Case.

Pursuant to the requirements of Oregon law, PacifiCorp proposes to set its tax expense in this case based upon the stand-alone method for calculating utility taxation. No party to this case has contested the accuracy of PacifiCorp's proposed stand-alone tax expense. Instead, the Oregon Public Utility Commission Staff ("Staff"), Industrial Customers of Northwest Utilities ("ICNU") and the Citizens' Utility Board of Oregon ("CUB") propose adjustments to PacifiCorp's stand-alone tax expense based upon the tax liability of PacifiCorp's parent company, PacifiCorp Holdings, Inc. ("PHI"). Although each party focuses its proposed tax adjustment on the tax savings generated by PHI's interest payments on the loan it incurred to acquire PacifiCorp, the parties do not agree about the justification for the adjustment, the proper method for computing the adjustment or the impact on PacifiCorp's revenue requirement. Indeed, the three proposed adjustments vary by many millions of dollars, as follows:

- Staff proposes to reduce PacifiCorp's Oregon-allocated revenue requirement by $4.6 million, arguing that $4.6 million "may" represent the cost of the burden on customers of PHI's debt. (Staff/1000, Conway-Johnson/9, 16.)
- CUB proposes to reduce PacifiCorp's Oregon-allocated revenue requirement by $14.8 million, arguing that $14.8 million represents the value to customers of PHI's interest deduction. (CUB/100, Jenks/1-2; Cross-Examination of Bob Jenks, Tr. 166-67.)
- ICNU proposes to reduce PacifiCorp's Oregon-allocated revenue requirement by $27.6 million, arguing that, because PHI does not actually pay to taxing authorities PacifiCorp's stand-alone tax payment, permitting PHI to retain PacifiCorp's stand-alone tax payment provides PHI an excessive return on its investment in PacifiCorp. (ICNU/200, Selecky/17; ICNU/211, Selecky/2.)

The Commission should reject all of the proposed tax adjustments because they are unlawful and unsupported by the evidence. The proposals conflict with long-standing Commission precedent, the statutory prohibition against cross-subsidization of regulated and

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nonregulated operations, Oregon Administrative Rules and the Department of Justice's (the "DOJ") advice on the legality of consolidated tax adjustments. Absent a legislative change or rulemaking proceeding altering or rescinding the current stand-alone tax rule, adoption of any of the proposed tax adjustments would violate the Administrative Procedures Act.

Furthermore, even if the Commission properly changed its stand-alone tax rule, the DOJ has advised the Commission that a consolidated tax adjustment must meet the "benefits and burdens" test to be lawful. Here, none of the three adjustments satisfies that test. Additionally, the proposed adjustments are flawed in other ways: all three proposals arbitrarily pick and choose which nonutility revenues and expenses to include for purposes of setting Oregon customers' rates; Staff's and CUB's proposals are supported by nothing more than speculation; and all three proposals use allocation methodologies that are not rationally connected to the basis for the adjustment.

1. Current Law and Commission Policy Require the Tax Expense in Rates to Reflect the Utility's Stand-Alone Tax Liability Without Regard to Tax Liabilities or Benefits of Other Members of the Utility's Consolidated Group.

To prevent cross-subsidization, Oregon law requires the Commission to calculate tax expense in utility rates using the stand-alone method, whether or not the utility is part of a consolidated group for federal and state tax filing purposes. *See* ORS 757.646(2)(c) (requiring Commission to adopt rules that "prohibit[] cross-subsidization between competitive operations and regulated operations"); OAR 860-027-0048 (requiring calculation of utility tax expense on stand-alone basis).

Under the stand-alone method, tax savings or liabilities created by nonregulated operations, including those created by affiliated entities such as parents, affiliates and subsidiaries, are not allocated to customers. Instead, the tax expense in rates is determined by looking at the revenues and expenses generated by the regulated operations of the utility

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only. *See In re Util. Reform Project*, Order No. 03-214, app A at 2 (Or Pub Util Comm'n Apr. 10, 2003) (basing tax expense in rates on cost of regulated operations and ignoring tax effect of parent's operations is "[c]onsistent with long-standing OPUC policy," which "'protect[s] customers, competitors, and the public generally'" (citation omitted)); *In re Util. Reform Project*, UCB 13, Order No. 03-401, at 6-7 (July 9, 2003) ("[I]n a rate proceeding, [Portland General Electric] rates are set based on its own revenues * * * Income taxes are calculated using PGE's net operating income. The tax effects of Enron's other operations are ignored for purposes of setting rates. This is consistent with standard ratemaking principles."), *rev'd in part by letter ruling*; *Re Or. Exch. Carrier Ass'n*, Order No. 93-325, 1993 WL 117620 at *5 (Or Pub Util Comm'n Mar. 12, 1993) (Commission's policy is to "calculate tax liability on a stand alone basis"), *reconsideration den*, Order No. 93-879, 1993 WL 390953 (Or Pub Util Comm'n June 28, 1993).

Any approach to utility taxes that allocates tax liabilities or savings resulting from nonregulated operations to ratepayers would be contrary to the Commission's statutory obligation to prevent cross-subsidization between regulated and nonregulated operations. *Re Or. Exch. Carrier Ass'n*, 1993 WL 117620, at *6. (*See also* Cross-Examination of Bryan Conway and Judy Johnson, Tr. 184 (agreeing that one of the concerns expressed throughout Commission Staff's White Paper on Treatment of Income Taxes in Utility Ratemaking (the "White Paper") was that change from stand-alone method to alternative tax method might create risk of cross-subsidization); *id.* at 185 (testifying that stand-alone method is superior to other methods); PPL/1806/12 (White Paper) (identifying risks associated with consolidated tax adjustments); PPL/1806/14 (recognizing that "ratemaking principles prohibit cross-subsidization between utility and non-utility operations" and "[a]s a result, most states calculate utility income taxes for ratemaking on a stand-alone utility basis").)

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As PacifiCorp's tax expert, Bernard L. Uffelman, explained in his rebuttal testimony, ratemaking tax expense that is calculated under the stand-alone method is based on the items of income and expense included in the regulated utility's revenue requirement calculation. (PPL/1400, Uffelman/3.) *See also In re Util. Reform Project*, Order No. 03-214, app A at 2 (denying petition for investigation of PGE income tax rates; "For ratemaking purposes, the Commission sets PGE's rates to reflect the costs of the company's regulated operations. That is, in a rate proceeding, PGE's rates are set based on its own revenues, costs and rate base for a given test year."). In this way, both tax obligations and tax savings created by activities of nonregulated operations, including those created by affiliated entities such as parents, brother and sister affiliates, and subsidiaries, are not allocated to customers. As Mr. Uffelman observes, this approach is consistent with ratemaking principles that segregate regulated and nonregulated operations, often referred to as "ring fencing." *Id.* at 4, 7; *see In re PacifiCorp*, Order No. 03-726, app at 5 (stand-alone method prevents "cross-subsidization"); *see also Re Midwest Gas*, 133 Pub Util Rep 4th (PUR) at 396-97 ("If the Board allowed the benefits of [nonregulated affiliate] losses to go to the ratepayers, stockholders would be forced to subsidize the utility cost of service."); *Re Delmarva Power & Light Co.*, Order No. 3389, 1992 WL 465021 at *18 (Del Pub Serv Comm'n Mar. 31, 1992) (true-up methods are "'short-sighted[]' and * * * violate[] the 'fundamental' ratemaking principle that a utility's costs and revenues should be kept separate from those of its non-regulated subsidiaries" (citation omitted)). Indeed, "[t]he *only* approach that is consistent with standard ratemaking principles that prohibit cross-subsidization between utility and non-utility activities is to put the regulated operation on a 'stand-alone' basis and to assign the full tax burden to the taxable gain source and [the] full tax benefit to the tax loss source." *Accounting for Public Utilities* § 7.08[3] (2003) (emphasis added).

This Commission has consistently rejected attempts to include in rates the tax savings of the utility's consolidated affiliates. *See, e.g., In re Util. Reform Project*, Order No. 03-

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214, app A at 2; *see also Re Or. Exch. Carrier Ass'n*, 1993 WL 117620 at *6 (rejecting attempt by utility to include in rates tax liabilities of utility's consolidated affiliates). In every instance, the Commission has rejected proposed consolidated tax adjustments on the basis that such adjustments are contrary to the Commission's obligation to prevent cross-subsidization of regulated and unregulated activities. *See, e.g., In re PacifiCorp*, Order No. 03-726, app A at 5 (requiring use by PacifiCorp of the stand-alone method to prevent "any cross-subsidization of [ScottishPower UK plc] ("ScottishPower") operations by PacifiCorp's regulated operations"); *In re Util. Reform Project*, Order No. 03-214, app A at 2; *Re Or. Exch. Carrier Ass'n*, 1993 WL 117620 at *6.

> "The benefits to customers are obvious. Our [stand-alone] policy prevents a holding company from transferring unjustifiable expenses to the utility or taking actions that would improperly inflate the utility's cost of capital. It also prevents the parent from imposing costs on ratepayers by using utility assets for purposes unrelated to customer needs."

In re Util. Reform Project, Order No. 03-401 at 6.

Consistent with its long-standing prohibition against cross-subsidization, just over one year ago, the Commission adopted a rule that requires electric utilities in Oregon to calculate and report income taxes on a stand-alone basis for regulatory and ratemaking purposes, even if a utility is a member of a consolidated group for tax-filing purposes. OAR 860-027-0048, adopted in December 2003, provides, in pertinent part:

> "(3) The energy utility shall use the following cost allocation methods when transferring assets or supplies, or providing or receiving services between regulated and nonregulated activities:
>
> "* * * * *
>
> "(g) Income taxes shall be calculated for the regulated activity on a standalone basis for both ratemaking purposes and regulatory reporting. When income taxes are determined on a consolidated basis, the regulated activity shall record income tax expense as if it were determined for the regulated activity separately for all time periods.

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> "(4) The energy utility shall use the following cost allocation methods when transferring assets or supplies or providing or receiving services involving its affiliates:
>
> "* * * * *
>
> "(h) Income taxes shall be calculated for the energy utility on a standalone basis for both ratemaking purposes and regulatory reporting. When income taxes are determined on a consolidated basis, the energy utility shall record income tax expense as if it were determined for the energy utility separately for all time periods."

The stated purpose of the rule is to prevent cross-subsidization between regulated utilities and nonregulated affiliates. *Re Affiliated Transactions for Energy Utils.*, Order No. 03-691, 2003 WL 23305011 at *1 (Or Pub Util Comm'n Dec. 1, 2003) (establishing OAR 860-027-0048 to govern the Commission's transfer pricing policy and prevent cross-subsidization between regulated activities of utility and its nonregulated activities, affiliates and competitive operations); OAR 860-038-0580 (requiring compliance with OAR 860-027-0048 to prevent cross-subsidization between competitive operations and regulated operations).

2. Staff and Intervenors Propose Adjustments That Disregard the Prohibition Against Cross-Subsidization and Contravene the Commission's Stand-Alone Tax Rule and Long-Standing Precedent.

Staff, ICNU and CUB propose that PacifiCorp's tax expense, which is calculated for ratemaking purposes based on the expenses and revenues of regulated operations, be decreased to reflect a portion of the consolidated tax savings created by PHI's interest payments. Although CUB was loath to use the term "consolidated tax adjustment" (Tr. 154-55), each of these adjustments is just that.

The stand-alone method means that:

> "The Commission 'view[s] utility operations separately from the financial operations of the parent company. That means that the expenses used to calculate rates are solely those of the utility. For taxes, [the Commission] look[s] at the utility as a stand-alone enterprise. We do not explore the holding

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> company's tax liability, only the regulated utility's liability as though it were operating without the holding company.'"

In re Util. Reform Project, Order No. 03-401 at 6 (emphasis added).

In contrast, Staff and intervenors base their proposals on an aspect of the taxable income of the holding company, not on the net taxable income of the utility "as though it were operating without the holding company." (Tr. 155 (CUB is "attempting to get the Commission to recognize the tax deduction at the holding company."); PPL/1804/4 (CUB response to PacifiCorp discovery request 1.13, stating that proposal is designed to align tax expense in rates with federal taxes that are paid by consolidated group); Staff/1000, Conway-Johnson/16 (basing adjustment on burden on customers from PHI's debt); ICNU/200, Selecky/17 (basing adjustment on PHI's tax structure).)

3. Absent a Legislative Change or Revision of the Commission's Rule Pursuant to a Rulemaking Proceeding, Adoption of Staff's or Intervenors' Proposed Consolidated Tax Adjustments Would Violate the Administrative Procedures Act.

The Commission does not have discretion to deviate from OAR 860-027-0048 in this case. *Harsh Inv. Corp. v. State*, 88 Or App 151, 157, 744 P2d 588 (1987) ("An agency is not authorized to act contrary to its rules * * * If it were otherwise, the rules would become meaningless."); *Peek v. Thompson*, 160 Or App 260, 264-65, 980 P2d 178 (1999) ("It is, of course, axiomatic that an agency must follow its own rules. Even if an agency is not required to adopt a rule, once it has done so it must follow what it adopted." (citations omitted)).

The Commission has not reserved its ability to waive OAR 860-027-0048. The Commission cannot waive a rule absent a specific reservation to that effect in the rules, such as the express waiver provision in OAR 860-038-0001(4) applicable to the New Resource Rule. *See Harsh Inv.*, 88 Or App at 158 ("Neither could [a state agency] waive a legal prerequisite to its actions; to permit it to do so would render meaningless the statutory

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procedures for suspending a rule.");[1] OAR 860-011-0000(6) (Commission may waive rules contained in chapter 860, divisions 11 through 14 for good cause shown); OAR 860-038-0001(4) (Commission may relieve entity of obligations under Chapter 860, Division 38 for "good cause shown").

Thus OAR 860-027-0048 has the force of law "as binding as if the legislature itself had acted." *Harsh Inv.*, 88 Or App at 157.

> "The rule may limit what an agency would otherwise be able to do. 'An agency which is vested with discretion by statute may limit its own discretion in its regulations.' Thus, the question is not * * * what the statute requires; rather, the question is what the rule requires."

Peek, 160 Or App at 264-65 (citations omitted).

If the Commission decides to change its tax policy, it must do so in an orderly, deliberate and forward-looking manner by opening a rulemaking to consider changes to its current stand-alone utility taxation rule. ORS 183.335. In advance of a change in the Commission's rule, it may not approve ad hoc consolidated tax adjustments.

4. Even if the Commission Amended, Repealed or Suspended its Stand-Alone Tax Rule, the Consolidated Tax Adjustments Proposed by Staff and Intervenors in This Case Are Nevertheless Unlawful Because They Fail to Satisfy the "Benefits and Burdens" Test.

Even if the Commission were to choose to change the stand-alone tax rule, Staff and intervenors have failed to establish the "burden" that the DOJ has advised is necessary to justify a consolidated tax adjustment. (*See* Staff/1002, Conway-Johnson/7 (DOJ memorandum regarding legality of setting utility rates based on tax liability of parent, dated Feb. 18, 2005); PPL/1807/1 and 3 (DOJ memorandum regarding the Utility Reform Project's comments on tax treatment in utility ratemaking, dated Mar. 22, 2005).)

[1] The statutory procedures for promulgating, amending, suspending or repealing a rule are set forth at ORS 183.325 through 183.410.

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a. The Commission May Order a Consolidated Tax Adjustment Only if Customers Bear the Burden of the Deductible Expense That Gave Rise to the Consolidated Tax Savings—That Is, Only if the Adjustment Satisfies the "Benefits and Burdens" Test.

As PacifiCorp, Staff and CUB observe in their testimony, the DOJ recently advised the Commission that it may order a consolidated tax adjustment only if the adjustment satisfies the "benefits and burdens" test. (PPL/1300, Martin/6; PPL/1301, Martin/3-4; Staff/1000, Conway-Johnson/4; CUB/100, Jenks/4; s*ee also* PPL/1807/1 (Commission may change current stand-alone policy only "so long as the [new] policy is rational, including taking into account the benefits and burdens of its policy, and meets minimum constitutional requirements"); *id.* at 3 (acknowledging that state regulators may choose between different methods of calculating tax allowances, but "whichever method is chosen it should be *applied* in a way that matches benefits and burdens" (emphasis in original)).)

The "benefits and burdens" test requires the Commission to give consolidated tax savings to customers only "if the customers bore the burden of *paying the deductible expense that generated the savings*." (Staff/1002, Conway-Johnson/1 (emphasis added); *see also id.* at 7 ("The benefits and burdens test can be simply stated as: the benefits of consolidated tax savings are given to ratepayers (by reducing the utilities tax allowance) if the customers bore the burden of *paying the deductible expenses that generated the savings*." (emphasis added)).) *See also Charlottesville v. FERC*, 774 F2d 1205, 1217 (DC Cir 1985) (deductions are attributable to utility's jurisdictional activities if "'the customers of a regulated entity contributed to the expenses which created the loss deductions'" (citation omitted)).

This principle was reflected in the White Paper, which stated:

> "Unless the underlying revenues and costs of the parent and subsidiaries were also reflected in rates, setting rates based on consolidated tax payments would be considered poor regulatory policy * * *. Regulators should reflect tax benefits in rates to the same extent that customers bear the expenses creating those benefits. There is no economic rationale for a regulatory body to pick and choose which non-utility revenues

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> and expenses—including tax savings—to include for purposes of setting Oregon customers' rates."

(PPL/1806/12.)

Indeed, the DOJ has advised the Commission that changing its policy on utility taxes to one that "picks and chooses in an arbitrary manner how it treats expenses and investments" implicates the serious constitutional concerns raised by the U.S. Supreme Court in *Duquesne Light Co. v. Barasch*, 488 US 299 (1989). (PPL/1807/3.)

In *Duquesne Light*, the Court reaffirmed the *Hope* standard and also cautioned state regulators that decisions to "arbitrarily switch back and forth between methodologies in a way which required 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." 488 US at 314-15; *see also In re Util. Reform Project*, Order No. 03-214, App. A at 2-3 (allocation of affiliate tax benefits to utility "may lead to confiscatory rates"); *Re Potomac Elec. Power Co.*, 150 Pub Util Rep 4th PUR 528, 1994 WL 109204; *Iowa Elec. Light & Power Co.*, Pub Util Rep 135 4th PUR 527 ("The affiliates' financial losses which create the tax savings exist only because of the investment and expenses borne by the stockholders. It is clear the losses which created the tax savings belong to the affiliates * * *."). Thus the DOJ summarized its advice to the Commission as follows:

> "Any change in policy must be consistent with Oregon law and constitutional requirements. A policy that considers the benefits and burdens of the utility's participation in a consolidated tax group, consistent with the *Hope* standard, would result in [a] decision that would be consistent with *Duquesne* and administrative law requirements."

(Staff/1002, Conway-Johnson/3.)

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b. Intervenors Fail to Present Compelling Evidence That Their Proposed Consolidated Tax Adjustments Satisfy the "Benefits and Burdens" Test.

Although Staff and CUB acknowledge the benefits and burdens test, both fail to present evidence that their proposed adjustments satisfy the test. Specifically, neither presents evidence that customers bear the burden of "paying the deductible expense that generated the savings." (Staff/1002, Conway-Johnson/1.) Instead, Staff and CUB acknowledge that PHI bears the burden of "paying the deductible expense that generated the savings," but argue that the existence of the debt nevertheless places a burden on customers sufficient to take the tax savings from PHI and allocate it to customers. (Cross-Examination of Mr. Conway and Ms. Johnson, Tr. 191-92 (testifying that PHI has legal obligation to pay debt and interest on debt), Tr. 189 (testifying that burden is not interest rate on debt at PHI, but rather "the likely effect that the debt at PHI, when viewed in a consolidated entity, had, and then in this case primarily on the cost of debt of PacifiCorp over the last four or five years"); CUB/200, Jenks/4 (referring to PHI's obligation to pay its debt).)

ICNU, on the other hand, eschews the benefits and burdens test in favor of a so-called "actual taxes paid" approach to the utility tax expense rates:

> "Mr. Martin argues * * * that PacifiCorp's affiliation with Scottish Power has benefited PacifiCorp's ratepayers. Hence, he concludes that [ICNU's] adjustment fails the "benefits-burdens" test.
>
> "* * * * *
>
> "Mr. Martin's arguments are simply off base. The issue here is whether PacifiCorp will actually incur income tax expense and should therefore recover that expense from customers."

(ICNU/211, Selecky/2-3; *see also* PPL Exhibit 1811 (ICNU response to PacifiCorp discovery request 4.9 ("Mr. Selecky has not claimed there is a nexus between the interest expense of PHI's loan and the cost of capital of the utility.")).) ICNU's proposal ignores OAR 860-027-0048, as well as the DOJ's advice on this matter and long-standing Commission precedent.

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The DOJ specifically considered the issue of whether the actual tax liability of the consolidated tax filer reflects the utility's cost of service and concluded that the Commission may only consider the parent's tax expenses in calculating the utility's cost-of-service if the Commission "takes into account the benefits and burdens of the utility's participation in the consolidated tax group." (Staff/1002, Conway-Johnson 2.)

i. Staff's and CUB's Burden Arguments Are Flawed in Two Key Respects: (1) They Fail to Appreciate That Ring-Fencing Protects Customers from Negative—as Opposed to Positive—Economic Impacts of Nonregulated Operations, and (2) They Focus on the PHI Debt in Isolation.

Staff and CUB argue that the acquisition indebtedness of PHI places a burden on PacifiCorp's customers that justifies the proposed consolidated tax adjustments. (Staff/1000, Conway-Johnson/16; CUB/200, Jenks/2.) Specifically, they assert that rating agencies examine the debt of the entire consolidated group, which includes PHI, when setting PacifiCorp's credit rating and that the agencies have expressed concern with respect to PHI's debt burden. (Staff/1000, Conway-Johnson/6-7; CUB/100, Jenks/10-11.) Both extrapolate that this concern creates a burden on customers. (Staff/1000, Conway-Johnson/9 ("[i]t is possible that customers are bearing a "burden" to the extent the parent caused PacifiCorp's debt costs to be higher"); CUB/200, Jenks/2.)

Staff's and CUB's burden arguments are flawed. *First*, they fail to appreciate the significance of the fact that the financial strength of PacifiCorp's parent *benefits* rather than *burdens* customers—a fact which neither disputes. (*See* Staff/1000, Conway-Johnson/8 ("PacifiCorp's ratings are currently benefited by PacifiCorp's relation to ScottishPower"); Cross-Examination of Mr. Jenks, Tr. 162 (testifying that Standard & Poor's May 2005 report "shows that the entire consolidated credit is a positive"); *see also* CUB/200, Jenks/4 ("The nexus between PacifiCorp customers and the interest-related tax deductions at PHI is this credit-evaluation relationship between PacifiCorp and its holding company, not that the relationship is positive or negative at any given moment.").)

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Second, they focus their analyses on a single aspect of PacifiCorp's parent's financial structure, the PHI debt, without regard to any offsetting or positive attributes of the parent's financial structure.

> "My understanding of the benefits/burdens test is that you can look at the burdens presented by the debt, holding all else equal. So you're not concerned about whether or not there's an equal and offsetting benefit due to something unrelated in another portion of the Company."

(Redirect-Examination of Mr. Conway and Ms. Johnson, Tr. 212-13.)

> "Q. But if [the burden of the debt] is offset by equity at the parent level that is equal to or greater than that debt, then the net impact is [going to] be positive so that the consolidated impact is a positive, not a negative, impact. A benefit, not a burden. Isn't that correct?
>
> "A. [By Mr. Conway.] My understanding of the memorandum written by Jason Jones is that you do not need to take into account all of the other ramifications of a consolidated company. You're not looking at all other possible benefits in weighing out whether or not it's on balance there. You're looking at one item, the debt at PHI. And the question is whether or not the debt at PHI, in isolation, causes harm to PacifiCorp.
>
> "* * * * *
>
> "Q. On page 12 of the white paper, * * * it states, 'There is no economic rationale for a regulatory body to pick and choose which non-utility revenues and expenses, including tax savings, to include for purposes of setting Oregon customer's [sic] rates.'
>
> "* * * * *
>
> "Q. And isn't that precisely what you're doing by looking at one piece of the consolidated debt, consolidated financial structure, in isolation from all other impacts of the consolidated tax—or financial structure?
>
> "A. This was written February 1st; Jason's memo's February 18th. I'm relying on the latter, the February 18th memo, for this adjustment in this case.
>
> "Q. And Ms Johnson, isn't it your testimony that this white paper remains—that you stand by what you wrote in this white paper?

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"A. (By Ms. Johnson.) Yes."

(Recross-Examination of Mr. Conway and Ms. Johnson, Tr. 216-17.)

(*See also* Cross-Examination of Mr. Jenks, Tr. 156 (testifying that CUB's adjustment is addressing "risk associated with one identifiable parent company cost.").) Staff and CUB focus on this single aspect of the parent's financial structure despite the fact that they acknowledge that credit rating agencies consider the debt along with all the other debt and equity in the consolidated capital structure. (Cross-Examination of Mr. Jenks, Tr. 163 (admitting that credit rating agencies consider PHI's debt along with all other debt and equity in consolidated capital structure); Cross-Examination of Mr. Conway and Ms. Johnson, Tr. 203 (testifying that credit rating agencies consider all debt and equity).)

ii. By Focusing on Just One Aspect of the Parent Financials, Staff's and CUB's Analysis Avoids the Fact That PacifiCorp's Customers Have in Fact *Benefited* from PacifiCorp's Relationship with ScottishPower.

By arbitrarily focusing on just one aspect of the parent financial picture, Staff and CUB avoid the fact that PacifiCorp's customers have in fact benefited from PacifiCorp's relationship with ScottishPower. Absent a showing of a negative credit impact from the affiliation with ScottishPower, no rational basis exists for making adjustments for speculative impacts of one aspect of parent debt, divorced from other aspects of the parent financial structure. (Cross-Examination of Mr. Conway and Ms. Johnson, Tr. 193 (testifying that ring-fencing attempts to insulate utilities from credit risk of unregulated affiliate); *id.* at 194 (testifying that intent of ring-fencing is to insulate regulated utility from harm that could come from unregulated operations).)

Here, PacifiCorp's credit rating is not constrained by its parent's credit rating—and therefore no burden is shown—because ScottishPower's and PHI's credit ratings are not weaker than PacifiCorp's. (Cross-Examination of Mr. Conway and Ms. Johnson, Tr. 200 (testifying that "the ratings aren't constrained by the three-notch rule because they're the

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same"); *id.* at 199 (testifying that Mr. Conway knows of no evidence that PacifiCorp's rating is being held back by three-notch rule).)

> "Q. Now, the quotation ["The parent company debt impacts all of the companies in the corporate family."] is—really addresses the situation of a financially-healthy subsidiary constrained by the rating of a weaker parent, doesn't it?
>
> "A. Specifically, yes.
>
> "Q. Now, based on the credit rating we just went through,[2] that's not the scenario with ScottishPower, PHI and PacifiCorp, is it?
>
> "A. At the time of those particular ratings, that, that is true."

(Cross-Examination of Mr. Jenks, Tr. 159.) *See also* PPL/304, Williams/12 (quoting Standard & Poor's May 25, 2005 *Research Update*, which stated: "[T]he current corporate credit rating on PacifiCorp is based on ScottishPower's consolidated credit profile, whose solid financial performance compensated for the U.S. *utility's weaker stand-alone metrics*." (emphasis added)).)

In fact, PacifiCorp's credit rating is currently higher than its stand-alone metrics and financial targets warrant. (Cross-Examination of Mr. Conway and Ms. Johnson, Tr. 204.)

> "Q. Okay. Well, we've just established that PacifiCorp's metrics and financial targets are actually, you know, worse than what its current A minus rating would warrant. That there [*sic*] really put it in the double B to triple B range, based strictly on the metrics and –
>
> "A. Okay.
>
> "Q. – financial targets.
>
> "A. Correct.
>
> "Q. And my question to you is if S&P were imputing 2.4 billion dollars of debt to PacifiCorp's balance

[2] BBB+ for PacifiCorp unsecured, A- for PacifiCorp unsecured, A- for PHI, and BBB+ for ScottishPower unsecured. (Cross-Examination of Mr. Jenks, Tr. 158-59.)

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sheet, wouldn't you expect that the rating would be lower than the mechanical calculations would suggest, not higher?

"A. Again, I'm having a problem with the mechanical calculations part. If you imputed debt onto PacifiCorp's books and it was not being viewed that way today, the only thing that could happen would be PacifiCorp's ratings would suffer."

(*Id.* at 205.)

Indeed, Staff acknowledges repeatedly that customers may not be harmed by PacifiCorp's relationship with ScottishPower:

"This would imply that the ring fencing was not 100 percent effective. However, other conditions of the merger could be sufficient to ensure customers are held harmless, such as the merger credits."

(Staff/1000, Conway-Johnson/7.)

"[W]e conclude that PacifiCorp's ratings suffer due to debt at PHI but, PacifiCorp's ratings are currently benefited by PacifiCorp's relation to ScottishPower. The net result of these two effects is unknown."

(*Id.*)

Staff admits that PacifiCorp's evidence

"indicate[s] the following benefits:

"1. ScottishPower has implemented operational efficiencies and fortified relations with state regulators.

"2. In May 2005, ScottishPower's consolidated credit profile compensated for the U.S. utility's weaker stand-alone metrics."

(Staff/1000, Conway-Johnson/7.)

Despite this, Staff nevertheless speculates that PacifiCorp's affiliation with Scottish Power may harm customers. (Staff/1000, Conway-Johnson/8.) Staff asserts that customers may be harmed by the relationship with ScottishPower because the level of operational efficiency or fortified relations with regulators PacifiCorp may have achieved absent the

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merger is not known. (*Id.*) Likewise, Staff questions the impact ScottishPower has had on PacifiCorp's credit metrics, stating that "we cannot readily observe what PacifiCorp's stand-alone metrics would have been absent the merger. Perhaps a high dividend payout requirement at ScottishPower resulted in increased demands for cash at PacifiCorp and depressed PacifiCorp's credit metrics." (*Id.*; Cross-Examination of Mr. Jenks, Tr. 165 (testifying that he has no reason to dispute that PacifiCorp's dividend payments are lower than they were before ScottishPower merger).) This speculation is wholly unsupported. Rather than requiring an increased dividend payout, ScottishPower accepted major reductions in dividend levels from levels PacifiCorp paid prior to the ScottishPower merger. (PPL/312, Williams/12-13.)

Likewise, Staff offers no evidence that PacifiCorp's operational efficiencies, relations with regulators or stand-alone credit metrics have been harmed by its relationship with ScottishPower.

> "[W]e do not know with certainty to what extent PacifiCorp's borrowings have been more costly [as concerns about PacifiCorp's parent] * * *. Due to the ring fencing provisions adopted in Order Number 99-616, there is some degree of separation between the credit quality of PacifiCorp and its parent. However, the ring fencing may not be 100 percent effective, so some customer harm may have occurred."

(Staff/1000, Conway-Johnson/10.)

Rather than providing evidence of a harm or burden, Staff impliedly asks the Commission to relitigate UM 918, lamenting that "there is insufficient analysis provided by PacifiCorp to conclude that equity infusions and other actions demonstrate that PacifiCorp's cost of capital is lower due to the merger."[3] (Staff/1000, Conway-Johnson/8-9; *see also*

[3] To address Staff's speculation about whether the merger conditions have effectively held customers harmless, Staff recommends that PacifiCorp request an advisory report or study from a ratings agency. (Staff/1000, Conway-Johnson/12.) Staff's recommendation is inappropriate for many reasons, including the fact that Staff first introduced its proposed tax adjustment in its surrebuttal testimony, filed only three weeks before the hearing. Furthermore, a proposed adjustment to PacifiCorp's tax expense in a general rate case is not the appropriate vehicle for determining whether PacifiCorp is out of compliance with the

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Cross-Examination of Mr. Jenks, Tr. 156 (testifying that CUB has not reviewed whether alleged risk to customers of PHI debt is offset by benefits provided by parent, stating "you would need [a] 'but for' case to make that kind of analysis").)

Staff and CUB argue that the debt creates a burden by increasing PacifiCorp's costs of borrowing despite the fact that PacifiCorp's parents have stronger credit metrics than PacifiCorp, the debt has decreased since the Commission determined that the affiliation with ScottishPower would not harm customers, and dividend payments are lower than they were before the merger. (Cross-Examination of Mr. Conway and Ms. Johnson, Tr. 199-200; Cross-Examination of Mr. Jenks, Tr. 159, 165, 177.) Staff's and CUB's speculation that PHI debt, in isolation, burdens customers whether or not customers are in fact benefited overall by PacifiCorp's relationship with ScottishPower is arbitrary and irrational.

iii. In Any Event, Intervenors Fail to Allocate to PHI That Portion of the Interest Deduction Commensurate with the Burden Borne by PHI.

Staff allocates 100 percent of the PHI debt to PacifiCorp even though Staff claims that customers bear the burden of some portion of the debt that is far less than 100 percent. Indeed, Staff acknowledges that PHI bears the legal obligation to pay the debt, that the ring-fence has been effective, that the merger conditions and credits have already compensated customers for some—or even all—of the alleged burden of PacifiCorp's affiliation with ScottishPower, and that credit agencies do not impute 100 percent of the PHI debt to PacifiCorp. (Cross-Examination of Mr. Conway and Ms. Johnson, Tr. 191-93, 206;

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merger order. *See In re Application of ScottishPower plc and PacifiCorp*, UM 918, Order No. 99-616 at 19 and app-Stipulation 5 at 10 (Oct. 6, 1999) (providing for written notice to ScottishPower and/or PacifiCorp from Commission of any violation of merger conditions, opportunity to cure, opening of investigation to determine whether and to what extent violation has occurred, and that Commission will seek penalties for uncured violations in action in circuit court). In an action brought by the Commission against PacifiCorp or ScottishPower alleging violation of a merger condition, the Commission would have burden of proof.

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Staff/1000, Conway-Johnson/7 ("other conditions of the merger could be sufficient to ensure that customers are held harmless, such as the merger credits").)

Nevertheless, Staff's adjustment is calculated by imputing 100 percent of the PHI debt onto PacifiCorp's balance sheet. (Staff/1000, Conway-Johnson/12; Cross-Examination of Mr. Conway and Ms. Johnson, Tr. 203.) This is despite the fact that credit rating agencies do not impute the PHI debt to PacifiCorp. (PPL/312, Williams/11 ("I have never seen [Standard & Poor's or Moody's] make any debt adjustment related to the debt of PHI, ScottishPower, or any other affiliate when calculating debt ratios used to rate PacifiCorp's debt."); Cross-Examination of Mr. Conway and Ms. Johnson, Tr. 206 (testifying that credit agencies probably do not impute 100 percent of debt to PacifiCorp); Cross-Examination of Mr. Jenks, Tr. 163; *see also* Cross-Examination of Mr. Jenks, Tr. 164 (testifying that, to Mr. Jenks knowledge, no credit rating agency report has ever called out PHI debt).)

Like Staff, CUB also fails to allocate a portion of the interest deduction to PHI commensurate with the burden PHI bears. Instead, CUB allocates the tax benefit of PHI's interest payments "among the subsidiaries of PHI" based on their relative contribution to the consolidated group's gross profits. (Cross-Examination of Mr. Jenks, Tr. 168; CUB/102 (confidential), Jenks/1.) Not only does this allocation methodology fail to allocate a portion of the tax benefit to the one entity that has the obligation to pay the deductible expense, it distributes the tax benefit based on relative gross profits, which have no rational connection to income taxes. (PPL/1300, Martin/8 ("Normally, inter-company allocations are based on relative taxable incomes."); Cross-Examination of Mr. Jenks, Tr. 170 (testifying that he has no reason to dispute that relative taxable income is usual method for allocating taxable income).)

Staff and CUB do this even though both acknowledge that ring-fencing has been effective and that it certainly has not been entirely ineffective. (Cross-Examination of Mr. Conway and Ms. Johnson, Tr. 197, 200 (burden on customers is difference between

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100 percent effective and effective ring-fencing; "I did testify that this ring fence is effective."); Cross-Examination of Mr. Jenks, Tr. 156 (testifying that CUB does not know whether benefits provided by parent have offset burdens); CUB/200, Jenks/5 (testifying that ring-fencing measures help insulate utility from its corporate parent).) Staff also acknowledges that PHI bears the burden of actually paying the PHI debt. (Staff/1000, Conway-Johnson/4.) Indeed, Staff acknowledges that customers have no legal obligation to pay the debt, that PacifiCorp does not have a guarantee obligation, that all interest on the debt is paid by PHI and that the expense is not on PacifiCorp's books. (Cross-Examination of Mr. Conway and Ms. Johnson, Tr. 191-93.)

B. PacifiCorp's Proposed Transition Adjustment Mechanism Complies with the Commission's Directive in UM 1081 and Strikes the Proper Balance Between the Competing Needs of Accuracy and Efficiency.

PacifiCorp's RVM filing in this case is a compliance filing in response to the Commission's Order 04-516 in UM 1081. In UM 1081, the Commission adopted an interim Transition Adjustment Mechanism and directed PacifiCorp to file a permanent Transition Adjustment Mechanism by November 15, 2004 for use beginning with the fall 2005 enrollment window. *In re Industrial and Commercial Customers Under SB 1149*, Order No. 04-516, UM 1081, 2004 WL 2294131 at 1 (Or Pub Util Comm'n Sept. 14, 2004). Consistent with the Commission's directive, PacifiCorp conducted stakeholder workshops focused on development of a permanent RVM that met those requirements. (PPL/700, Omohundro/3.) The Company then filed an RVM proposal in this case that reflects the feedback from these workshops.

The Commission made clear in UM 1081 that PacifiCorp's long-term Transition Adjustment Mechanism should value the resources affected by Direct Access "based on actual, appropriate operational responses." 2004 WL 2294131 at 11. In addition, the Commission made clear that it expected the RVM to reflect the fact that PacifiCorp's

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operational responses to Direct Access load loss are "multidimensional," *i.e.*, involving more than one or two system responses. *Id.*

In response to the Commission's directive for a Transition Adjustment Mechanism that reflects actual operational responses, PacifiCorp's RVM relies on GRID, PacifiCorp's power cost model. The Company's proposed RVM uses two GRID runs to calculate the weighted market value of the energy previously used to serve Direct Access customers. The RVM then calculates the Transition Adjustment by comparing the weighed market value to the cost of service rate under the customers' specific, energy-only tariff schedules. (PPL/700, Omohundro/3.) The mechanism includes an annual power cost update to ensure that both aspects of the Transition Adjustment—weighted market value and cost of service—are calculated for the same period using the same data. (PPL/701, Omohundro/8-10.)

To minimize the time and resources involved in this process, PacifiCorp's proposed RVM is largely mechanical and is conceptually based on PGE's existing RVM. (PPL/701, Omohundro/3.) A Transition Adjustment Mechanism modeled after PGE's RVM makes sense because the Commission has already reviewed and approved PGE's RVM and because PGE's RVM has already been in place for three annual cycles. (*Id.*) In addition, by basing its RVM on an existing and approved model, the Company can avoid the complexities (and concomitant costs) associated with a new and unfamiliar mechanism and process. (*Id.*)

Staff supports PacifiCorp's proposed RVM on the basis that it accomplishes a reasonable balance of the interests implicated. (Staff/700, Galbraith/23 ("PacifiCorp's proposed Transition Adjustment provides an accurate accounting of the likely impacts of [D]irect [A]ccess on PacifiCorp's system operations and can be expected to result in transition adjustment rates that reasonably balance the interests of retail electricity consumers and utility investors.").)[4]

[4] In his surrebuttal testimony, Staff witness Maury Galbraith objected to the exclusion of variable costs associated with new resources until the plant is providing utility service, as

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ICNU and CUB oppose the RVM for a variety of reasons. ICNU's main objection is that the RVM relies on the GRID model. (ICNU Pretrial Brief at 9-10.) CUB's main objection is that the RVM applies to residential customers. (CUB Pretrial Brief at 2.) Staff does not believe that these concerns are well founded. (Staff/700, Galbraith/13, 15.) Because neither ICNU nor CUB has proposed valid alternatives that fully address the Commission's mandate in UM 1081, the Commission should reject their objections and approve PacifiCorp's RVM.

1. ICNU's Objections to PacifiCorp's Proposed RVM Are Unreasonable and Should Be Rejected.

a. ICNU's Proposed Transition Adjustment Mechanism Is Contrary to the Commission's Order in UM 1081.

ICNU was one of the parties in UM 1081, a docket in which considerable time was spent focusing on PacifiCorp's Transition Adjustment Mechanism. (Cross-Examination of Randall Falkenberg, Tr. 89.) In UM 1081, ICNU developed the "market-plus" method as its short-term position for the transition adjustment. (Tr. 90.) This is essentially the same transition adjustment method INCU proposes in this case. (ICNU/100, Falkenberg/53, Tr. 95-96.)

ICNU's "market-plus" proposal in this case is contrary to the Commission's order in UM 1081, in which the Commission rejected this approach in favor of an interim "market-even" approach. It also referred to all of the interim methodologies, including ICNU's "market-plus" method, as "conjectural," in contrast to the "actual operational response" model it directed PacifiCorp to develop and file. *In re Industrial and Commercial*

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contemplated by Oregon statute, and matching fixed costs are included in the Company's rate base. (Staff/700, Galbraith/18, 23.) As explained by Ms. Omohundro in her sur-surrebuttal testimony, PacifiCorp has agreed to include the variable costs of its new resources in the RVM even if the fixed costs are not yet in rates. (PPL/702, Omohundro/2.) The impact of this concession is a potential reduction in costs and a benefit to customers.

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Customers, 2004 WL 2294131 at 11. At hearing, ICNU provided no explanation as to how its proposed mechanism in this case could be reconciled with the Commission's Order in UM 1081. (*See* Tr. 95-97.)

b. ICNU's Objection Based on PacifiCorp's RVM's Similarity to PGE's RVM Is Unfair and Invalid.

ICNU objects to PacifiCorp's RVM because it is modeled after PGE's RVM. This objection is inconsistent with ICNU's position in UM 1081, in which ICNU advocated the exact opposite. *See, e.g.*, Cross-Examination of Lincoln Wolverton, PPL/1801/4 ("all of the parties agree that PacifiCorp ought to work longer-term on a methodology that looks more like PGE's method in the sense that it integrates the setting of power costs with the setting of a transition adjustment"); Direct Testimony of Mr. Wolverton on Behalf of ICNU, PPL/1803/1 ("I propose that the Commission require PacifiCorp to use a Transition Adjustment based on a methodology similar to PGE's.").)

In UM 1081, ICNU advocated that PacifiCorp emulate the PGE model in UM 1081 because customers were familiar with it, it appeared to encourage direct access and it was fair to customers. PacifiCorp responded to feedback from ICNU and others in UM 1081 in designing its RVM filing after PGE's. (*See, e.g.*, PPL/701, Omohundro/3.) In light of this history, ICNU's current objections to PacifiCorp's proposed RVM because it is "patterned too closely after PGE's" should be rejected. (ICNU/111, Falkenberg/16.)

c. The Graveyard Hour Market Liquidity Cap Is a Moot Argument.

ICNU alleges that the graveyard hour market liquidity cap used in PacifiCorp's GRID model results in a situation in which the value of the energy freed up by Direct Access will always be lower than the market price paid by an electricity service supplier (or "ESS") to serve a Direct Access customer, and that it is therefore impossible for a customer to benefit by switching to Direct Access. (ICNU/100, Falkenberg/48-53.) As explained by Staff's witness Mr. Galbraith, the parties in this case have responded to this issue in the first Partial

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Stipulation by relaxing the graveyard caps for the amount of Direct Access load assumed in the transition adjustment. (Staff/700, Galbraith/4.) In cross-examination, Mr. Falkenberg agreed that the first Partial Stipulation eliminated this problem. (Tr. 98.) ICNU's graveyard cap argument is moot.

d. GRID Simulates Transmission Costs.

ICNU takes the position that "GRID does little to simulate transmission costs" and therefore does not accurately assess the impact of Direct Access participation on the Company's operations. (ICNU/100, Falkenberg/53.) This position is unfounded, because expenses associated with the Company's wheeling contracts are direct inputs into the GRID model, and expenses associated with additional day-ahead firm wheeling are developed by the Company's Commercial and Trading department. (PPL/600, Widmer/15; Staff/700, Galbraith/6.) PacifiCorp's GRID model has the capacity to reflect the impact of Direct Access on the Company's transmission costs, which is one of the reasons the Company proposed to use the GRID model in its RVM. (*See* Staff/700, Galbraith/6.) In any event, to the extent that ICNU believes that transmission costs are not covered in a manner that properly promotes Direct Access, it can propose adoption of a transmission adder or credit to the RVM, such as that previously adopted by the Commission in the Company's Kick-Start program. ICNU has made no such proposal in this case or elsewhere.

e. PacifiCorp Must Continue to Plan on Serving the Entire Forecasted Load in Oregon.

ICNU argues that the GRID model does not plan in advance for Direct Access load loss. (Tr. 101.) Mr. Falkenberg states that "GRID does not simulate changes in planning that might have a much more important impact on operations" and therefore is a questionable tool to use for determining the Company's RVM. (ICNU/100, Falkenberg/53.) While ICNU levels its criticism at the GRID model, the issue really pertains to the Company's approach to resource planning, currently before the Commission in LC 39. (Staff/700, Galbraith/8.)

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The proposed order now before the Commission in LC 39 directs PacifiCorp to continue to plan to serve the entire forecasted load in its Oregon service territory on a long-term basis, given the level of participation in Direct Access to date and customers' ability to return to cost-of-service rates each year. (*See also* Staff Comments, PPL/1802/2.) No party has objected to this language. ICNU has not participated in PacifiCorp's Integrated Resource Plan ("IRP") public process or submitted comments in LC 39. (Tr. 102.)

f. PacifiCorp's Annual Updates of Cost-of-Service Rates Are Not Unnecessarily Burdensome.

ICNU generally argues that the annual update of cost-of-service rates is an unnecessary regulatory complication. (ICNU/100, Falkenberg/57.) Updating the Company's official forward price curve and net power costs ensures that the adjustment applied to departing customers is as accurate as possible and is in the best interest of all customers. (PPL/701, Omohundro/3-4.) Staff agrees. (Staff/700, Galbraith/13.) So did ICNU in UM 1081. (*See, e.g.*, Cross-Examination of Mr. Wolverton, PPL/1801/4 (testifying that "all of the parties agree that PacifiCorp ought to work longer-term on a methodology that looks more like PGE's method in the sense that it integrates the setting of power costs with the setting of a transition adjustment."); Direct Testimony of Mr. Wolverton on Behalf of ICNU, PPL/1803/10 ("there needs to be a method for establishing the resource cost component of the transition adjustment").)

2. CUB's Objections to PacifiCorp's Proposed RVM Are Unreasonable and Should Be Rejected Because Residential Customers Are Properly Included in PacifiCorp's RVM.

CUB's overarching objection to PacifiCorp's proposed RVM is that it impacts residential customers. (CUB Pretrial Brief at 2.) CUB's position is based on CUB's belief that PacifiCorp's RVM has nothing to do with residential customers, and that applying the Company's proposed RVM to only those customers who are eligible for Direct Access can be "easily done," according to CUB's witness Bob Jenks. (CUB/100, Jenks/22, 25.)

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Updating power costs for only a subset of PacifiCorp's customer base would be complex and difficult to achieve in the time frame required for the Direct Access enrollment process. (PPL/702, Omohundro/4.) It also could result in large and arbitrary differentials between those whose rates are updated and those whose are not, a result inconsistent with price discrimination principles. This is why PacifiCorp's RVM includes all customers, not just customers eligible for Direct Access. (PPL/701, Omohundro/2-3; PPL/701, Omohundro/4.)

Staff supports PacifiCorp on this issue, submitting that CUB intentionally exaggerates the lack of relationship between PacifiCorp's Transition Adjustment and its residential customers. (Staff/700, Galbraith/15.) Staff concludes that an update for only some customers would be difficult to implement and would result "in two sets of cost-of-service rates, one for [D]irect [A]ccess eligible customers, and one for non-[D]irect [A]ccess eligible customers." (Staff/700, Galbraith/17.) Consequently, Mr. Galbraith recommends that it makes more sense to update the cost-of-service rates for all customers, not just those eligible for Direct Access. (Staff/700, Galbraith/17.)

C. The Commission Should Reject ICNU's Objections to PacifiCorp's RVM Net Power Costs Updates.

PacifiCorp proposed to make several adjustments and updates to its originally filed power costs as part of the RVM process. In the third Partial Stipulation, Staff and PacifiCorp agreed that if the RVM is implemented to set the Company's Transition Adjustment, these updates and adjustments should increase power costs by approximately $4.3 million, effective January 1, 2006 when the RVM goes into effect.[5]

[5] Because it is important during a general rate case to include the most current information that is available as it is for an RVM proceeding, the Company requests that the Commission incorporate the Company's RVM update adjustments, with the exception of the planned outages and the outage period update (because those are specific to the RVM process), even if the RVM is not adopted. (PPL/611, Widmer/6.) The RVM adjustments

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ICNU objects to the following five RVM power cost adjustments: (1) deferred maintenance adjustment, (2) thermal ramping, (3) station service,[6] (4) planned outages and (5) outage period update. ICNU reserved these adjustments from the fourth Partial Stipulation.

1. Deferred Maintenance Is Often Conducted During Peak Hours.

Mr. Falkenberg claims that the Company's maintenance outages do not need to be scheduled during hours when market prices are at peak because they are deferrable, and recommends that this adjustment be reversed. (ICNU/111, Falkenberg/26.) However, simply because maintenance outage is deferrable does not mean that it is going to be performed on weekends. (PPL/611, Widmer/9.) In fact, the Company's plant records show that 42 percent of deferrable maintenance occurs during peak hours. (PPL/611, Widmer/9.) Therefore, the Company's adjustment is representative of actual operations and should be included. (*See id.*)

2. The Thermal Ramping and Station Service Adjustments Do Not Result in an Understatement of Thermal Generation.

Mr. Falkenberg recommends that the Commission reverse the Company's proposed adjustments related to thermal ramping and station service because he mistakenly concludes that they result in an understatement of coal-fired generation. (ICNU/100, Falkenberg/3.) This conclusion is based on faulty assumptions and an incomplete analysis, because as further explained in Mark Widmer's rebuttal testimony, GRID was *overstating* coal generation before ramping, station service and deferrable maintenance adjustments, and in

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would increase net power costs by about $4.9 million on an Oregon basis (which is slightly higher than the $4.3 million level stipulated to by the Company and Staff).

[6] Because Mr. Falkenberg addresses thermal ramping and station service together, this brief likewise addresses them together.

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fact, is still somewhat overstating thermal generation. (PPL/609, Widmer/11.) Therefore, Mr. Falkenberg's proposed adjustment should be rejected.

3. The Company's Planned Outages Adjustment Was Made Pursuant to the Commission's Schedule for This Case.

Mr. Falkenberg recommends against the use of the 2005 scheduled outages in GRID in the March GRID update because this adjustment was not "timely" made and runs contrary to Commission precedent. (ICNU/100, Falkenberg/3.) This argument is unfair and unreasonable because the adjustment was made in the Company's March 15, 2005 update along with 18 other adjustments in compliance with the schedule established for this case by the Commission on December 8, 2004. (*See* PPL/609, Widmer/19, *referring to* December 8, 2004 Prehearing Conference Memorandum by Administrative Law Judge Traci A. G. Kirkpatrick, setting March 15, 2005 as the date for PacifiCorp to submit GRID update.) Accordingly, ICNU's proposed reversal of the Company's adjustment related to planned outages should be rejected.

4. The Company's Outage Period Update Adjustment Was Made Pursuant to the Commission's Schedule for This Case.

Mr. Falkenberg argues that PacifiCorp's outage period update is a last-minute selective update of the GRID model. (ICNU/100, Falkenberg/47-48.) This argument is groundless, because, as explained above for the planned outages, the outage period adjustment was made in the Company's March 15, 2005 update along with 18 other adjustments pursuant to the schedule established for this case by the Commission on December 8, 2004. (PPL/609, Widmer/10.) In addition, the adjustment was proposed at earlier workshops held by the Company at which ICNU was present. (*Id.*) Therefore, ICNU was not disadvantaged by the procedural process as Mr. Falkenberg suggests, and ICNU's proposed reversal of the Company's adjustment related to the outage period update should be rejected.

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D. The Commission Should Reject ICNU's Proposed Adjustments, as Excluded by ICNU in the Fourth Partial Stipulation, Because They Are Unfair and Unreasonable.

ICNU proposes adjustments to PacifiCorp's requested revenue requirement in addition to those proposed by the other intervenors in this case. In the fourth Partial Stipulation, ICNU excluded the following six issues from settlement:

1. The treatment of PacifiCorp's new Qualifying Facility ("QF") contracts under the Revised PacifiCorp Inter-Jurisdictional Cost Allocation Protocol (the "Revised Protocol");
2. The prudence of PacifiCorp's new generation resources;
3. PacifiCorp's request for waiver of the market price rule;
4. PacifiCorp's fuel handling charge;
5. The UM 995 deferral period outages; and
6. Costs related to development of the Regional Transmission Organization ("RTO").

ICNU's adjustments, which would reduce PacifiCorp's Oregon revenue requirement by approximately $93.3 million, resulting in an approximately $16.1 million rate *reduction*, are not fair and reasonable for the reasons set out below.

1. PacifiCorp's New QF Contracts Are Properly Classified Under the Revised Protocol as "New QF Contracts."

In accordance with Commission Order No. 05-021 in UM 1050, *In Re PacifiCorp*, No. 05-021, 2005 WL 293533 (Or PUC Jan. 12, 2005), PacifiCorp determined its target revenue requirements and allocated system costs to Oregon using the Revised Protocol. (*See* PPL/400, Taylor/2.) The Revised Protocol was ratified in Oregon by the Commission on January 12, 2005 "for use in future rate cases to determine how costs and wholesale revenues will be allocated among its six-state service territory. 2005 WL 293533, att A at 1. As described in Erich Taylor's direct testimony, the Revised Protocol allocation methodology differs in three ways from the Modified Accord methodology, and application of the Revised

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Protocol as opposed to the Modified Accord allocation method in this case produces a net benefit to Oregon customers of $12.7 million. (PPL/400, Taylor/2-3.)

One category of costs that is affected by the Revised Protocol is QF contracts. ICNU does not contest the applicability of the Revised Protocol to this rate case. (Tr. 112.) The major issue of controversy raised by ICNU related to the Revised Protocol is whether the Company's new QF contracts in this case, US Magnesium, Desert Power, Kennecott and Tesoro, should be treated as "New" or "Existing" under the Revised Protocol. (ICNU/100, Falkenberg/6-7.) The treatment of QF contracts is important in this case because the four QF contracts at issue are not located in Oregon and their classification as "Existing QF Contracts" would lower Oregon's allocated costs.

Under the Revised Protocol, the costs of "New QF Contracts" are allocated on a system basis. (PPL/400, Taylor/7.) Conversely, the costs of "Existing QF Contracts" are allocated on a situs basis. (*Id.*) Because the four QF contracts at issue were entered into after the effective date of the Revised Protocol, PacifiCorp properly classified these contracts as "New QF Contracts." Although this results in allocation of these costs on a system basis, the net effect of implementation of the Revised Protocol in this case is positive for Oregon customers. As noted above, the revenue requirement as originally filed in this case was $12.7 million less than what it would have been under the Modified Accord method.

ICNU objects to PacifiCorp's classification, based on its interpretation of the effective date of the Revised Protocol. (ICNU/100, Falkenberg/6-8.) ICNU argues that the Revised Protocol's earliest effective date is the date the Commission approved the ratification of the Revised Protocol, January 12, 2005. (*Id.* Falkenberg/7; ICNU Prehearing Brief at 15.)

ICNU's interpretation of the effective date is erroneous because the Revised Protocol has a clearly defined effective date of June 1, 2004 and plainly classifies New QF Contracts as contracts that were entered into after that date. *In re PacifiCorp* 2005 WL 293533,

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att A at 1. ICNU's witness Mr. Falkenberg relies on the fact that the June 1, 2004 date is designated as the "Proposed" effective date in the Revised Protocol, and as such is not a "defined term." (ICNU/111, Falkenberg/3.) However, Mr. Falkenberg conveniently ignores the fact that at the time of the May 20, 2004 filing of the Revised Protocol, it was fully expected by all parties concerned that the June 1, 2004 effective date, which was less than two weeks after the filing, would precede the date of final ratification and that the effective date of the Revised Protocol would remain June 1, 2004 *unless specifically modified* by one or more of the four state commission approval orders. (PPL/412, Taylor/4 (emphasis added).)

Clearly, had the parties intended for the Revised Protocol to become effective upon ratification of each state or upon ratification of the last state, as Mr. Falkenberg asserts, then the effective date definition could have simply stated so. Instead, there is no mention in the Revised Protocol that the effective date is related in any way to the date that it is ratified by the states.

Staff agrees with PacifiCorp's interpretation of the Revised Protocol's effective date and recommends that the Commission reject ICNU's proposed adjustment on this issue. (Staff/800, Wordley/1, 5-6; *see also* Tr. 146 ("[The Revised Protocol] has been developed by the parties as an integrated, independent, organic whole. Therefore final ratification of the Protocol by any of the Commissions of Oregon, Utah, Wyoming and Idaho is expressly conditioned upon similar ratification of the Protocol by the other mentioned commissions, without any deletion or alteration of a material term or the addition of other material terms or conditions.").) Moreover, Staff takes the position that ICNU's interpretation of the Revised Protocol's effective date would result in a material violation of the Revised Protocol. (Tr. 146 ("[Staff's view of whether] the four QFs in question are existing or new, and in considering them existing, which would imply the later effective date, the January effective date, would be a violation—a material violation. And Staff is unwilling to violate the

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Protocol before it gets off the ground.").) In the third Partial Stipulation, Staff agreed to support PacifiCorp's treatment of the four QF contracts under the Revised Protocol.

Because the Commission did not change the effective date of the Revised Protocol upon its approval in UM 1050, the June 1, 2004 date remains the effective date. Therefore, the Commission should reject Mr. Falkenberg's unfounded arguments, and conclude that PacifiCorp has properly treated these transactions as "New QF Contracts."

2. The Acquisition of the Company's New Generation Resources Was Prudent.

Net power costs in this docket include the Company's three new Utah resources: (1) Phase One of the Currant Creek Project, a natural gas-fired simple cycle combustion turbine project located adjacent to PacifiCorp's Mona Substation in Juab County, Utah (the "Currant Creek project"); (2) the Gadsby gas turbine simple cycle project located in Salt Lake City, Utah; and (3) the West Valley lease, a 15-year contract with PPM Energy, Inc. (PPL/900, Tallman/2.) The Company acquired these resources based on the conclusions of its 2003 IRP. (*Id.*)

PacifiCorp's rates have included the West Valley lease as a component of net power costs since June 2002 and have reflected the operation and maintenance capital costs of the Gadsby project since August 2003. (PPL/901, Tallman/2.) The Company only included Phase One of the Currant Creek project in this case, because Phase Two of the project will not be completed until after PacifiCorp's rates go into effect in 2005. (PPL/900, Tallman/5.)

Mr. Falkenberg contends in his direct and surrebuttal testimony that these new resources are imprudent, nonbeneficial and above-market, and as such should be removed from Oregon retail rates even though the Company has provided ample evidence to the contrary. (*See* ICNU Prehearing Brief at 13.)

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a. The Acquisition of the Currant Creek Project Was Prudent.

The Company made the decision to construct the Currant Creek project after evaluating the alternatives presented via RFP 2003-A. (PPL/900, Tallman/5.) In addition, as Mr. Tallman explains in his direct testimony, the external consultant hired by the Company to evaluate the bids obtained through RFP 2003-A, Navigant Consulting, Inc., agreed with the Company's decision, stating that the Currant Creek project "was determined to be the lowest cost resource option within the context of the RFP process." (PPL/900, Tallman/5.) The Utah Public Service Commission also concluded that the Currant Creek project is required by public convenience and necessity. *In re PacifiCorp*, Docket No. 04-035-30, 2004 WL 3094815 (Utah PSC Nov. 12, 2004). Because the Currant Creek project was priced below market at the time it was acquired, the Company's decision to acquire this resource was prudent. Therefore, the Commission should reject ICNU's proposed adjustments related to the prudence of this resource.

b. The Acquisition of the Gadsby CTs Was Prudent.

During the Hunter outage and the Western power crisis, the Company leased mobile combustion turbines ("CTs") and installed them at Gadsby to help mitigate production costs (the "Gadsby leased peakers"). (PPL/1600, Wrigley/5.) However, even when Hunter returned to full production the Company realized that additional capacity was required to serve retail load, and entered into an agreement with General Electric ("GE") to extend the lease of this equipment through September 2002. (*Id.*, Wrigley/6.) During the same period, a variety of other peakers were being considered, and Pratt & Whitney were selected. (*Id.*) In August 2001, GE was able to locate larger and more efficient equipment, the GE LM6000, that had a cost equivalent to the Pratt & Whitney installation. (*Id.*) GE offered to terminate the Company's $7.5 million lease obligation on the Gadsby leased peakers if PacifiCorp agreed to purchase the GE LM6000. (*Id.*) Because the GE LM6000 was the better

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alternative, even excluding GE's offer to terminate the lease, the Company accepted GE's offer. (*Id.*)

Mr. Falkenberg proposes that the investment in the CTs at Gadsby should be reduced by $7.5 million, and that PacifiCorp had a conflict of interest in its negotiations with GE because PacifiCorp was more interested in obtaining a waiver of the $7.5 million lease than in getting a reduction in the purchase cost of the equipment. (ICNU/100, Falkenberg/30-31; ICNU/111, Falkenberg/13-15.) This argument is unpersuasive based on two key points.

First, customers were never charged for the cost of the $7.5 million lease and, therefore, cancellation of that lease should not result in a credit to customers. (PPL/1600, Wrigley/5.) Because the nonpayment on the lease is reflected in lower expenses in fiscal year 2002, the base year for determining the revenue requirement in UE 147, Oregon ratepayers have benefited from this nonpayment. (PPL/1601, Wrigley/4.) Second, GE's offer to purchase the LM6000 was a better offer, even before accounting for GE's waiver of the remaining lease obligation. (Staff/800, Wordley/8.) Therefore, PacifiCorp's decision to purchase this equipment was prudent and the Commission should reject ICNU's proposed adjustments related to the prudence of this resource.

c. Entering Into and Extending the West Valley Lease Was Prudent.

PacifiCorp executed the West Valley lease on March 5, 2002. (*See* PPL/901, Tallman/2.) PacifiCorp sought Commission approval of the lease the following day, March 6, 2002. (*Id.*) The Commission approved the lease on May 31, 2002 in UI 196, *In re PacifiCorp*, Order No. 02-361, 2002 WL 31116076 (Or PUC, May 31, 2002), and the costs of the West Valley lease went into the Company's rates on June 1, 2002 (PPL/901, Tallman/2.). In approving the Company's lease, the Commission adopted and incorporated by reference Staff's report on the West Valley lease, which concluded that the lease satisfied the Commission's "lower of cost or market" standard for affiliated interest transactions. 2002 WL 31116076, app A at 6.

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In the summer of 2004, the Company issued a second RFP, RFP 2004-X, to determine whether there was a lower-cost alternative to the lease, but no such alternative was found. (PPL/901, Tallman/7.) Consequently, the Company decided not to exercise its option to terminate the lease. (*Id.*)

Mr. Falkenberg criticizes PacifiCorp's decision to extend the West Valley lease, asserting that PacifiCorp could have met this need at lower cost through RFP 2003-A, but he does not specifically identify any such bid, nor does he conduct an analysis of the bid compared to the West Valley lease. (ICNU/111, Falkenberg/10.) However, when the Company's witness Mr. Tallman undertook such an analysis, by comparing the lease with the market alternatives from RFP 2003-A, he discovered that the market alternative is *$181 million less economical* than the West Valley lease if costs of direct debt are included. (PPL/903, Tallman/2.)

Staff maintains its position that the initial acquisition of the West Valley resource was prudent, as well as PacifiCorp's decision in 2004 to continue the lease, based on Staff's economic evaluation of alternatives. (Staff/800, Wordley/7-8.) Staff recommends that the Commission reject ICNU's proposed adjustment related to the prudence of the West Valley lease. (*Id.*, Wordley/8.) Because the West Valley lease clearly continues to meet the "lower of cost or market" standard, the Commission should reject ICNU's proposed adjustments related to the prudence of this resource.

3. PacifiCorp Has Met the Standard Set by the Commission to Obtain a Waiver of the New Resources Rule.

On June 6, 2005, pursuant to OAR 860-038-0001(4), PacifiCorp filed an application in this docket for a waiver of OAR 860-038-0080(1)(b) (the "New Resource Rule") with regard to its acquisition of the three Utah generating resources. In the direct, rebuttal and surrebuttal testimony of Mr. Tallman, PacifiCorp provided significant evidence that each of these resources was priced below market at the time the resource was acquired. (Currant

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Creek: PPL/900, Tallman/5, PPL/903, Tallman/4; Gadsby: PPL/903, Tallman/4; West Valley lease: PPL/900Tallman/7, PPL/901, Tallman/6-7, PPL/903, Tallman/3.) Therefore, the waiver of the rule benefits customers.

Staff supports PacifiCorp's application for waiver and the inclusion of Currant Creek, Gadsby, and the West Valley lease at cost in this docket based on Staff's independent analysis of these three resources, which demonstrated that the resources are competitively priced as compared with market alternatives. (Third Partial Stipulation, June 29, 2005; Staff/800, Wordley/4-5, Tr. 135.)

ICNU claims that PacifiCorp's request for a waiver was not timely raised in this case. (ICNU/111, Falkenberg/11 (classifying PacifiCorp's waiver application as an "eleventh hour" request).) ICNU also takes the position that a waiver of the New Resource Rule should ideally be filed at the time the Company files for certification of the resource in Utah. (ICNU/111, Falkenberg/11-12.) Mr. Falkenberg's arguments are unreasonable and unfounded.

PacifiCorp filed its request for a waiver in the round of testimony in UE 170 that immediately followed the Commission's order holding UM 1066 in abeyance and suggesting that utilities seek a waiver of the New Resource Rule in the interim. (*See* PPL/903, Tallman/3.) It is difficult to see how this is untimely, especially given the significant uncertainty that has surrounded the status and meaning of this rule since its adoption. Staff agrees that the issue of timing in this case is not related to when the plants were constructed, but rather to when the Company first had an opportunity to apply for a waiver given the lack of resolution in UM 1066. (Tr. 133.)

Because both PacifiCorp's and Staff's evidence indicates that the best interests of customers are served by granting the waiver, the Commission should reject ICNU's arguments on this issue and grant PacifiCorp request for a waiver of the New Resource Rule in this docket.

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4. The Company's Fuel Handling Charge Is Properly Included in Rates.

Fuel handling costs are incurred by each of PacifiCorp's plants to unload the coal, manage the coal inventory, analyze and blend the coal, and deliver it from the stockpile to the boiler for use. (PPL/1600, Wrigley/3.) Start-up costs reflect the costs for diesel or gas used to start the coal plants. (*Id.*) During fiscal year 2004, the Company's fuel handling and start-up costs (hereinafter simply referred to as the "fuel handling charge") totaled approximately $8.9 million, increasing Oregon's fuel expense by $2.43 million. (*Id.*)

The Company's original November 12, 2005 filing mistakenly failed to include the Company's fuel handling and start-up costs. The Company discovered this oversight while researching the Georgia Pacific contract in the process of responding to Staff data request 433. (*See* PacifiCorp's Response to ICNU Data Request 17.7, ICNU/109, Falkenberg/3.) The Company promptly corrected this oversight by amending its filing in its rebuttal case. (S*ee* rebuttal testimony of Paul Wrigley, PPL/1600.) The Company also provided its work papers in support of this adjustment in its response to Staff Data Request 433 (providing FERC account detail that isolated the fuel handling charge).

Staff agreed to the fuel handling charge adjustment in the third Partial Stipulation. Staff's witness Jack Breen agreed that this charge should be included because its omission was inadvertent. (Staff/900, Breen/2.) ICNU objects to the Company's fuel handling charge, calling it "arbitrary and one-sided." (ICNU's Prehearing Brief at 11.) However, other than stating that the Company's adjustment is "late-filed and not adequately supported," ICNU fails to provide any reasoned explanation for its objection to this adjustment. (ICNU Prehearing Brief at 12; ICNU/100, Falkenberg/35-36.) Because PacifiCorp's fuel handling charge adjustment was timely filed and was properly supported by documentation, the Commission should disregard ICNU's unsupported allegations.

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5. The Company's Inclusion of the UM 995 Deferral Period Outages Will Not Result in a "Double Count" of These Outages.

ICNU has proposed an adjustment in this case based on excluding all outages that occurred during the UM 995 deferral period in calculating the four-year average outage rates. ICNU takes the position that the Company's inclusion of the UM 995 outages will result in a "double count" of these outage costs because the Company is already collecting these costs as a result of the Commission's UM 995 deferral order. (ICNU/111, Falkenberg/20.) Staff does not support ICNU's position and recommends that the Commission reject ICNU's proposed adjustment regarding UM 995 period plant outages. (Staff/800, Wordley/10-11.)

Mr. Falkenberg's proposed adjustment is flawed because the justification for it, an alleged double count, does not exist. (PPL/609, Widmer/4.) This is because all outages that occurred during the UM 995 deferral period, other than the Hunter outage, were consistent with the normal four-year average outage level reflected in power costs in base rates in effect during that period. (PPL/609, Widmer/3; PPL/611, Widmer/1; *see also* Staff/800, Wordley/11.) To avoid a double count of the Hunter outage, the Company normalized the Hunter outage rate by excluding from the four-year outage rate calculation the time period over which the outage occurred. (PPL/609, Widmer/3.) Because the Company is only requesting recovery of normalized costs in this case and because the Company has already removed the Hunter outage from its calculations, there is no double count with costs related to the UM 995 deferral period. (PPL/609, Widmer/3.) Mr. Falkenberg's proposed adjustment is not supported by the evidence in the record, and the Commission should reject it.

6. The Company's RTO Costs Are Useful and Should Not Be Deferred.

In an effort to boost competition and to bring consumers the lowest possible prices for electricity, the Federal Energy Regulatory Commission ("FERC") requires all transmission owners to join RTOs. FERC Order No. 2000, Docket No. RM 99-2-00, 89 FERC ¶ 61,285,

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1999 WL 33505505, (Dec. 20, 1999). Likewise, the Commission has made clear that it views the formation of an effective RTO as essential for a fair and efficient wholesale electricity market in the Northwest. (Testimony of Ron Eachus, Commission Chair, Public Utility Commission of Oregon (House Smart Growth and Commerce Committee, January 24, 2001); *see also* April 14, 2000 Commission Press Release (2000-018).)

The Oregon-allocated amount of the Company's total expenditures related to development of an RTO is properly included in this proceeding as an ongoing regulatory expense. Current RTO-related costs are useful, because the Company needs to comply with current FERC requirements in order to continue operations as a transmission provider. (PPL/1700, Larson/15.) Staff agrees that the RTO costs are reasonable and recommends that they be included in the Company's revenue requirement. (Staff/1400, Brown/3.)

ICNU's position is that RTO costs are not currently benefiting Oregon ratepayers and that PacifiCorp should not be permitted to recover RTO costs until an RTO is operating. (ICNU Prehearing Brief (July 13, 2005).) This position is short-sighted, however, because as PacifiCorp's witness Mr. Larson explained, PacifiCorp's customers directly benefit from the Company's transmission services and, consequently, from the ordinary, necessary, and reasonable expenditures that are associated with the provision of such services, including the Company's efforts to aid in the formation of an RTO for the Pacific Northwest, Grid West. (PPL/1700, Larson/16.) Excluding RTO costs in this case would unfairly limit PacifiCorp's role in this effort.

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IV. CONCLUSION

For all of the reasons stated in PacifiCorp's testimony, at the hearings and in the foregoing Brief, the Company requests that the Commission grant PacifiCorp's rate change as requested.

DATED: August 4, 2005.

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CERTIFICATE OF SERVICE

I hereby certify that I served a true and correct copy of the foregoing document in Docket UE 170 on the following named person(s) on the date indicated below by email and first-class mail addressed to said person(s) at his or her last-known address(es) indicated below.

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