BEFORE THE PUBLIC UTILITY COMMISSION OF OREGON
AR 499

In the Matter of the Adoption of Permanent Rules Implementing SB 408 Relating to Utility Taxes.	REPLY COMMENTS OF THE CITY OF PORTLAND

In considering which, if any, of the approaches being discussed in this proceeding, it is important to first consider the concerns that SB 408 was designed to address. It was at heart an attempt to address the impacts of the changing regulatory treatment of utilities, high finance interests in utilities, loss of PUHCA's consumer protections, and a changing tax regulatory world. SB 408 was written broadly with its draftees believing that the Oregon Public Utility Commission ("Commission") would draft rules that did not simply authorize business as usual.

But the utility proposals do just that. Staff's support of these utility proposals reflects backward thinking, an assumption that we know the limit of utility creativity in collecting but not paying monies that were designated as taxes to the relevant taxing authorities. What the drafters saw was that the old approach robbed both customers who paid higher rates and the local and state governments who depended upon tax revenue to fund essential services. Between giving utility investors extraordinary profits or using these monies to fund important governmental functions or lowering utility rates, the drafters chose Oregon and the voters they represent.

Make no mistake, this is big money with a potentially huge impact. If there is any doubt, just look to the amount of the money spent by PacifiCorp and its parent in

defeating SB 408 and limiting its impact when it passed. As reported by *The Oregonian*, PacifiCorp has spent $623,000 in legal costs in the fiscal year ending March 31, 2006 to avoid or limit the effect of SB 408.

While customers naively believe that the investor owned utilities - each a monopoly - have a guaranteed rate of return commensurate with risk. It is abundantly clear that there are strategies in place that increase the rate of return beyond any reasonable point. The manner that utilities are allowed to recover "taxes" as a cost component, approved by the Commission, and then allowed to file a consolidated return with a multi-tiered entity, who then receives not just the allowed rate of return but the tax funds as well was the genesis of the bill. This secret tax scam is why Texas Pacific Group came to buy PGE, what drives investor such as Harbinger to buy up PGE stock, and in part why Mid American saw the purchase of PacifiCorp not just a good investment but an extraordinary one. Any effort to continue this scheme should be aggressively rejected. While the Commission is to protect the utilities in a way that would encourage investment, it has to do so in context of the obligation to give a "fair return of return" and to assure that customers are charged fair and reasonable rates. Rates that have been artificially inflated in this way are neither fair nor reasonable.

There are three areas that merit discussion. First, each of the utility proposals is a version of the tax approach of the Enron years. The fact that Staff supports the utilities possibly reflects a misunderstanding of the future, a misunderstanding of the Hope Doctrine, or an unacceptable bias toward the utilities. The turnaround by Staff to now support a utility proposal over the temporary rules that they drafted with industry input is a remarkable turnabout.

The Hope Doctrine does not mandate or even support the approaches suggested. While utilities receive protections in a way that would encourage investment, it is in context of fair and reasonable rates. No where in the relevant statutes or the

legislative history is there any suggestion that making utilities attractive to investors is a predominant goal. It is, despite claims to the contrary, a balancing. Moreover, even if one were to accept the idea that utilities have some sort of special status, it has to be put into context: recovery of no more than the allowed rate of return. This was despite a regulatory scheme in which consumers were protected by PUHCA and before the idea of multi-tiered non utility investments funds. There were no utility investment trusts, no investment funds not subject to Commission oversight, and no tax mechanism by which to collect unconscionable profits.

Second, the rules implementing SB 408 must be written in a way to accommodate changes in corporate ownership, tax structures, and regulation. Using the old approach implies that it's still 1988, that utilities can only be owned by other utilities, and that the Commission had regulatory oversight over them all. It's not true now and it's not true in the future. While the parties might debate the Commission's jurisdiction over upstream investors under ORS 757.511, it's clear that the Commission has only enforced its jurisdiction by conditions on utility actions. Therefore these rules must address a number of unknowns and establish mechanisms to address an uncertain future. No one can guarantee that new, more clever ways will not be developed to redirect customers' funds into the pockets of upstream owners. No one can prevent or even identify what new tax incentives that will be offered to investors or utilities. By drafting rules to address now existing tax benefits, the Commission only creates incentives to utilities and investors to find other ways to accomplish the same ends, to the ultimate detriment of the customers. The "Enron Problem" was not that Enron was inherently evil, (although it may have been). Rather, the men and women working for Enron developed more and more clever ways to pull money out of the utility. The fact that PGE continues to pay Enron "taxes," as stated by Jim Piro in the recent investors' conference call available on PGE's website, should set off alarms for every customer as well as for the Commission.

Finally the City has specific concerns that require discussion:

a) The utility proposals share a desire to have the customers share in the downside - "stand alone tax liability" without sharing the upside: "allocation of tax benefits" due to the utility's ownership by a multitiered parent. They will certainly result in a continuation of the same old tax scheme. Moreover, as tax laws and utility regulations change, the proposals will allow the utility parent to reap even greater profits at the expense of the customers. Staff's support of these proposals is inappropriately short sighted.

b) The earnings test does not show up in the bill as passed nor does it show up in the legislative history. It would be an inappropriate interpretation of the statute to read such a test into the rules, certain to generate a successful challenge on the basis that the Commission overstepped its delegated statutory authority. It would be more appropriate and far more practical to consider the problems that are allegedly being fixed in the context of a general rate case and determined on a case by case basis. Taxes, or the collection of monies ostensibly for taxes due, was not intended to reward the utility for imprudent decisions or to cover other costs, such as those incurred for political lobbying that are not the burden of the ratepayers. The type of examination necessary is too great to be part of an SB 408 tax calculation. It is particularly important because the Hope Doctrine requires a big picture examination of all costs and revenue sources, regulatory treatment, costs adjustment provisions, and the like. While the utilities like to claim, "unconstitutional taking" that determination can only be made, if at all, in a general rate case.

c) These rules should neither include nor exclude identified tax offsets, credits, tax treatment under deferred accounting, and similar devices. That means that there should be no exclusion for tax benefits for such things as energy tax

credits, green tags, investment tax incentives, and other artificial regulatory mechanisms. No one can guarantee that next month, next year, or at some point in time the applications of these mechanisms will not change. And while we can claim an ability to change the rules if that should happen, inertia and a lack of appreciation of the impact on the utilities and their customers has historically meant that the Commission rules change not soon enough. It is better to simply describe the offsets generally as the drafters of SB 408 assumed and to have the customers share in all of the costs and all of the offsets, tax benefits, and modifiers.

SB 408 was an honest effort to address what was seen as a regulatory loophole - a legal travesty that reduced governmental revenues and increased customers' rates. It was simple: if the utility rate included a tax component in the cost calculations or a tax was a separate charge, all of the funds collected were to be paid to the relevant governmental tax entities. If there was a refund due from such entities as a result of decisions made by the filing entity, the utility customers would share in that refund. If the parent corporation filing the unitary returns elects not to pay 100% of the funds so collected to a taxing authority due to its determination of taxes due on a multi-tiered basis, then the customers would receive the monies that were over collected back as refunds or in some fund to be used for future tax obligations. The idea was to match as carefully as possible what was collected to what was actually paid to the taxing authorities.

The term "directly attributable" was first used in the context of whether to allocate tax offsets or to limit the use of those funds within the parent family. The term was intended to prevent the tax dollars paid in Oregon being used to pay tax liabilities of entities not regulated by this Commission. To prevent that occurrence, consideration was given on how to properly allocate benefits so that Oregon customers got their fair share of write-offs, offsets, credits and paid no more than their fair

share. It was never meant to be applied for protection of the upstream parent corporation. This is important because parent entities often make the decisions that determine which subsidiaries generate revenues and which generate liabilities. Enron was masterful at the game of assembling and disassembling "related" entities to shelter income. Energy tax credits arise as a result of utility ownership. Siphoning resources into a FERC regulated affiliate doesn't change that. The label applied to revenues sent to parent corporations - whether "dividends" or "interest" - makes a significant difference in who carries tax liabilities. But in the final analysis, the customers should only shoulder the burden of what is paid to the taxing authorities. That burden should be limited to a proportionate share, no more, no less.

The City of Portland urges the Commission to reject the utility proposals despite Staffs' support. The utilities' proposals reflect bad policy, short sighted thinking, and a continuation of a "business as usual" approach. The utilities are urging the Commission to continue having upstream parents receiving exorbitant profits in excess of the allowed rate of return. The City urges the Commission to adopt the proposal of ICNU and the Gas Users. Alternatively, the Commission should retain the "temporary rules" for a defined period of up to three years to find out how well they work before undertaking to revise them. Staff's proposal to adopt the utilities' approach will send Oregon backwards down a long and ugly path.

Dated this May 19, 2006

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CERTIFICATE OF SERVICE

I hereby certify that I served a copy of the foregoing REPLY COMMENTS OF THE CITY OF PORTLAND to:

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on the 19th day of May, 2006, by electronic copy to the Case Manager, Judy Johnson, e-mail address: judy.johnson@state.or.us and by mailing the original and two copies of said document, contained in a sealed envelope with postage paid, and deposited in the post office at Portland, Oregon on said day.

I further certify that I served a copy of the foregoing REPLY COMMENTS OF THE CITY OF PORTLAND on the individuals identified on the attached Service List by electronic mail and sending a true, exact and full copy by regular mail, postage prepaid on said day.

DATED this 19th day of May, 2006.

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