BEFORE THE PUBLIC UTILITY COMMISSION OF OREGON

AR 499

In the Matter of the Adoption of Permanent Rules to Implement SB 408, Relating to Matching Utility Taxes Paid with Taxes Collected.	**JOINT OPENING COMMENTS OF AVISTA CORPORATION AND PACIFICORP**

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PacifiCorp and Avista Corporation ("Avista") submit these comments jointly. The scope and meaning of SB 408 are now critical issues for Oregon, given the profoundly negative impacts this legislation could have on the financial integrity of the energy utilities that operate in this state. The proper statutory interpretation of SB 408 hinges on the definition and meaning of the term "properly attributed." This issue has particularly significant implications for Oregon's multi-state utilities PacifiCorp and Avista, and for utilities such as PacifiCorp and Avista that file taxes on a consolidated basis with an affiliated group.

I. INTRODUCTION

On September 2, 2005, Governor Theodore Kulongoski signed into law Senate Bill 408 ("SB 408" or the "Act"), noting that "the final version of the bill defers many of the difficult questions about the impact and implementation of SB 408 to the Oregon Public Utility Commission (OPUC)." *See* September 2, 2005 letter from Governor Kulongoski to Secretary of State Bill Bradbury. The Oregon Public Utility Commission ("Commission") initiated this rulemaking docket to answer, among other things, those "difficult questions about the impact and implementation of SB 408."

Recognizing that technical implementation issues cannot be resolved until overarching policy and legal issues are addressed, Administrative Law Judge Kathryn A. Logan designated four issues for early resolution by the Commission in this rulemaking docket. Those four issues are:

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1. How should the Commission apply the "properly attributed" standard as it appears in the individual sections of the bill?

2. What did the legislature intend in adoption of section 3(13)(f)(B)?

3. May the Commission terminate the automatic adjustment clause upon [a] showing by a utility that the automatic adjustment clause has a material adverse effect on the utility?

4. Section 3 of SB 408 requires the Commission to establish an automatic adjustment clause within 30 days (or later date, established by rule, not to exceed 60 days) once a determination is made regarding the $100,000 trigger amount. Section 4 states that if an automatic adjustment clause is established, it applies only to taxes paid to units of government and collected from ratepayers on or after January 1, 2006. If a utility pays quarterly estimated taxes, must the automatic adjustment clause be applied quarterly, or does the law allow it to be applied yearly?

ALJ Logan Memorandum at 1 (Oct. 5, 2005).

The Act leaves a number of its key terms undefined, including the terms "properly attributed" and "material adverse effect." These terms are not defined in other Oregon statutes or tax law. Nor are these terms unambiguously defined in the legislative history of SB 408. However, the legislative history and the Act itself make clear certain directives and policy goals, which must guide the interpretation of these terms. *State v. Bandon*, 582 P2d 52, 53 (Or App 1978) (statutes must be construed "with a view to effecting the overall policy which the statutes are intended to promote"). Although the Act is ambiguous in some respects, the following directives are clear:

- Rates are to be adjusted downward when a utility that is part of an affiliated group collected more taxes in rates than: (A) it incurred (net of certain adjustments specified in SB 408) as a result of its utility operations (*i.e.*, the utility's separate-return or stand-alone tax expense) or (B) its affiliated group paid in taxes to units of government (*i.e.*, the affiliated group's consolidated tax expense).

- Tax liabilities of affiliates may not be used to adjust rates upward or downward, except that affiliate tax benefits may be used to adjust rates downward when an affiliated group paid less tax to units of government than the utility collected in rates.

- Rates may not be adjusted under the Act if doing so would cause rates to be so high that customers would suffer material adverse effects or so low that utilities have no opportunity to recover their costs plus a reasonable return on their investments.

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- Calculations of "taxes paid" under the Act must be done in such a way as to protect incentives for utilities to be good corporate citizens and to invest in utility infrastructure.

- The first rate adjustment under the Act may not occur until some time after 2006, when the Commission can review the difference between taxes collected in rates and taxes actually paid to units of government in 2006.

It is clear from these statutory directives that the legislature intended SB 408 to address the so-called "Enron" problem (*i.e.*, when an affiliated group paid little or no taxes to government) while protecting against unintended consequences, such as penalizing affiliated groups that pay more tax in total than the utility collected in rates, creating disincentives for Oregon utility investment in unregulated businesses, including renewable energy, and discouraging financially attractive, positive tax-paying companies from making investments in Oregon utilities.[1]

In the context of these directives and policy goals, the participants in this docket were able to reach agreement at the first public workshop on the following important principles:[2]

- SB 408 may result in rate increases as well as rate decreases.

- The October 2005 and 2006 tax reports are for the sole purpose of determining whether there is a trigger for the automatic adjustment clause, not to support a rate change.

- The Commission may use historic data for the automatic adjustment clause.

- Whether or not the Act allows the Commission to use forecasted data, as a policy matter the Commission should base SB 408 adjustments on historic data only.

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[1] Although PacifiCorp and Avista find objectionable any allocation of affiliate losses to a utility because such allocations violate cost-causation principles and are likely unconstitutional, PacifiCorp and Avista nevertheless acknowledge that SB 408 clearly provides for the allocation of certain affiliated group losses to utilities when the consolidated group paid less tax to government than the utility collected in rates. However, a loss-allocation approach like that adopted in the temporary rule goes even further by guaranteeing a rate reduction whenever *any single affiliate* suffered a loss – that is, even when the consolidated group paid taxes far in excess of those collected in rates. This extreme overreaching was not the legislature's intent and it is not the premise of SB 408.

[2] *See* Letter from Paul Graham, Assistant Attorney General, to Participants in Docket AR 499 at 1-2 (Oct. 7, 2005) (summarizing agreements of participants) (attached hereto as Exhibit A).

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With the above directives, policy goals, and agreements in mind, PacifiCorp and Avista respectfully submit the following joint opening comments in response to the issues designated by ALJ Logan.

II. STANDARDS OF STATUTORY INTERPRETATION

The ultimate goal in interpreting a statute is to determine the intent of the legislature. *See, e.g., State ex rel. Click v. Brownhill*, 15 P3d 990, 992 (Or 2000); *see also* ORS 174.020(1)(a) ("In the construction of a statute, a court shall pursue the intention of the legislature if possible."); *PGE v. Bureau of Labor and Industries*, 859 P2d 1143, 1145-46 (Or 1993). The Oregon Supreme Court has set out the following three-step analytical framework to use in interpreting a statute:[3]

1. In the first step of the *PGE* analysis, the court looks to the text and context of the statute. *PGE*, 859 P2d at 1146. The text of the statute is considered the best evidence of the legislature's intent. *Id*. In interpreting the text, the court considers rules of construction that bear directly on how to read the text. *Id*. The cardinal rule of construction in this context is that "courts must presume that a legislature says in a statute what it means and means in a statute what it says there." *Connecticut Nat'l Bank v. Germain*, 503 US 249, 253-54. Consequently, courts must give the words of a statute their plain, natural, and ordinary meanings. *See, e.g.*, 859 P2d at 611; *Click*, 15 P3d 990, 992. Also at the first level of the *PGE* analysis, the court examines the context of the statutory provision, which includes other provisions of the same statute, as well as other related statutes. 859 P2d at 1146. Only when the intent of the legislature is not clear from this analysis does the court move to the second step of the analysis.

2. In the second step of the *PGE* analysis, the court examines the legislative history to inform the court's inquiry into legislative intent. *Id*. The court considers the legislative history along with the text and context of the statute to determine if all of these together make the legislative intent clear. *Id*. Again, only if this analysis does not yield an unambiguous result does the court move to the next step of the analysis.

3. In the third step of the *PGE* analysis, the court may resort to general maxims of statutory construction (either looking to Oregon's statutory interpretation statute or to case law) to determine legislative intent.

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[3] All three steps of the *PGE* analysis permit for the use of general rules of construction, some of which are mandated by statute, *e.g.*, ORS 174.010-.090, and others of which are found in case law.

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The *PGE* framework for statutory interpretation informs the responses to ALJ Logan's four issues designated for early resolution by the Commission in this rulemaking docket.

III. RESPONSES

A. "Properly Attributed" — How Should the Commission Apply the "Properly Attributed" Standard as It Appears in the Individual Sections of the Bill?

> Response: In applying SB 408, the Commission should recognize as "properly attributed" the tax liability that results from the economic activities of an entity, without consideration of the tax effects of other affiliated business entities. This stand-alone approach to attribution, combined with recognition of the "lesser of" standard in section 3(12), achieves the legislature's stated intent of decreasing rates when a utility's affiliated group paid less tax to government than the utility collected in rates, while otherwise complying with the legislative prohibition against attribution of affiliate tax liabilities to utilities.

1. It Is Clear from the Text and Context of SB 408, and Its Legislative History, That Taxes "Properly Attributed" Means Tax Payments Incurred as a Result of the Economic Activities of an Entity.

The text and context of SB 408 demonstrate that taxes "properly attributed" means tax payments incurred as a result of the economic activities of an entity without regard to the tax liabilities of other entities. SB 408 leaves the term "properly attributed" undefined, suggesting that the legislature intended the term to be given its common meaning. *See PGE*, 859 P2d at 611; *Click*, 15 P3d at 992. The common meaning of "attribute" is "belonging to, produced by, resulting from or originating in." *Webster's New World Dictionary* 92 (4th ed 2001).

This common meaning is consistent with the use of the term throughout the Act, including section 3(12), which is the only provision of the Act that provides any description of the meaning of the term "properly attributed." There, the Act describes an attribution to the utility of "taxes paid" based on the utility's operations only, stating:

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> "[T]axes paid that are properly attributed to the regulated operations of the public utility may not exceed the lesser of:
>
> "(a) That portion of the total taxes paid that is incurred as a result of income generated by the regulated operations of the utility[.]"

SB 408, 73d Or Legislative Assembly, Reg Sess § 3(12) (2005).

The phrase "portion of the total taxes paid that is incurred as a result of income generated by the regulated operations of the utility" describes an attribution to the utility of "taxes paid" based solely on the tax payments for the regulated operations, or otherwise stated, the tax obligations "produced by or resulting from" receipt of income from regulated operations.[4]

Some may argue that section 3(12)(a) does not require this stand-alone approach to attribution because that section says "taxes paid that is incurred" and "taxes paid" is defined, in part, as "amounts received by units of government." SB 408 § 3(13)(f). However, an interpretation of section 3(12)(a) that limits the amount "incurred as a result of income generated by the regulated operations of the utility" by the "amounts received by units of government" would render the "lesser of" language superfluous. Under such an interpretation, the section 3(12)(a) amount would always be the same or less than the section 3(12)(b) amount. It is also worthy to note that the only time "taxes paid" appears in the operative provisions of the Act without the words "to units of government" is in section 3(12)(a). The omission of "to units of government" and the "lesser of" language are given full effect only if section 3(12)(a) is interpreted to mean taxes incurred as a result of income generated by the regulated operations of the utility.

This interpretation also comports with other related statutes and the Commission's historic practice of computing taxes for ratemaking purposes based on the regulated

[4] Of course, the "lesser of" qualifier reduces the "taxes paid" if the affiliated group's consolidated taxes are lower than the utility's stand-alone taxes.

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operations of the utility only. Through its use of the term "properly attributed," SB 408 preserves the stand-alone approach to the calculation of tax liability. Moreover, section 3(7) reinforces this approach by expressly precluding consideration of affiliate tax liabilities in calculating the automatic adjustment clause except when the affiliated group paid less tax to units of government than the utility collected in rates.[5]

In particular, the "properly attributed" language and the description of attribution in section 3(7) are consistent with the Commission's statutory obligation to prevent cross-subsidization by maintaining the separation of regulated and unregulated utility operations. *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 whether or not utility is part of an affiliated group for federal and state tax filing purposes); *Re Affiliated Transactions for Energy Utils.*, AR 459, Order No. 03-691, 2003 WL 23305011 at *1 (Or Pub Util Comm'n Dec. 1, 2003) (Commission promulgated stand-alone rule to prevent cross-subsidization); *Re Affiliated Transactions for Energy Utils.*, AR 459, Staff Report at 4 (Or Pub Util Comm'n Aug. 7, 2003) (recommending that Commission initiate rulemaking proceeding to promulgate rules to prevent cross-subsidization); *In re PacifiCorp*, Order No. 03-726, App at 5 (stand-alone method prevents "cross-subsidization").

The legislative history confirms that the legislature intended the taxes attributed to the utility to be the taxes incurred as a result of income generated by regulated operations only, without regard to the tax liabilities of affiliates. In the following colloquy between Senator Rick Metsger, a proponent of SB 408, and Pamela Lesh, Portland General Electric

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[5] Section 3(7) expressly prohibits "adjustments to rates for taxes paid that are properly attributed to any unregulated affiliate of the public utility or to the parent of the utility."

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Company's Vice President for Regulatory Affairs, Senator Metsger explains that the amount attributable to utilities is the amount resulting from regulated operations:

> "Chair [Metsger]: [W]hen they file the report with the commission, it will be those taxes which are attributable only to the operations of that utility, even if you have multiple other affiliates. That's going to have to be figured in the tax report that in this case PacifiCorp would have to file, is to then break that down.
>
> "Lesh: Mr. Chairman, if I could ask a question. Would that work for the losses then as well if the other corporations had had losses and those are offset, would this tax report...
>
> "Chair: It has nothing to do with other corporations, it's only the utility itself. No other affiliations are affected by this. It would be your responsibility to delineate the utility in filing the report with the PUC, what their actual costs were, what their taxes are. It has nothing to do with any other affiliates you have. And that would be your responsibility is to have to extract that cost just like you did in your scenarios, but to actually be able to do that. * * *
>
> * * * * *
>
> "Chair: You can consolidate all you want, but you're not going to be allowed to collect other than the taxes that you owe on this particular, in this case, in the rates that you are collecting for the operation of actually that utility. File anywhere you want."

Work Session on SB 408 before the Senate Business and Economic Development Committee (May 26, 2005). Other portions of the legislative history similarly make clear that any rate adjustment clause should "not apply to the activities of other entities however they are related to the utility, but only to the utility itself." Work Session on SB 408 before the Senate Business and Economic Development Committee (May 31, 2005) (statement of Dexter Johnson, Legislative Counsel).

Moreover, a stand-alone attribution method makes sense in the context of SB 408's treatment of affiliate tax liabilities *in total*. SB 408 refers repeatedly to the taxes paid to units of government by the affiliated group in total, not just affiliates with positive or negative tax liabilities. "Affiliated group" is defined in SB 408 as "an affiliated group of corporations of

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which the public utility is a member and that files a consolidated federal income tax return." SB 408 § 3(13)(a). Rather than permitting (or requiring) examination of individual members of the affiliated group, this definition permits examination of the whole entity only – that is, the group of corporations that files a consolidated return. By looking at the total group, the Commission is able to consider the ultimate issue: whether taxes paid to units of government by the utility or group in total are less than the taxes incurred as a result of income generated by the regulated operations of the utility. *See* SB 408 § 3(12).

Indeed, the legislative history also demonstrates that SB 408 does not require an automatic adjustment whenever *any* affiliate suffers a loss, but instead only when a utility's affiliated group paid less tax than the utility collected in rates. Representative Brian Boquist explained this point when he carried the bill on the House floor. *See* House Floor Session (July 30, 2005) (statement of Rep. Brian Boquist). Representative Boquist's statement was consistent with the analysis by Deputy Attorney General Peter Shepherd, which was distributed to each member of the House during the floor debate. *See* House Floor Letter (memorandum from Dep. Att'y Gen. Peter Shepherd to Rep. Tom Butler, July 30, 2005). There, Deputy Attorney General Shepherd analyzed the impact of SB 408 and provided an outline of the various scenarios that would cause rates to "rise," "stay the same," or "go down" under the Act. He concluded that rates would "stay the same" if the affiliated group paid more tax to government than the utility collected in rates. *Id.* at 1. He did not conclude that rates would "go down" if any member of the group suffered a loss. *Id.* Rather, he concluded that two things could cause rates to "go down" for a utility that is part of an affiliated group: (1) the utility had less tax expense on a stand-alone basis than it collected in rates,[6] or (2) "losses incurred by affiliated companies offset the tax liability in the return so

[6] Deputy Attorney General Shepherd's analysis does not address the circumstances that would cause a utility's tax expense to decrease on a stand-alone basis nor the potential for mitigating the harmful effects of a rate reduction when a utility is already under-earning. As further reducing an under-earning utility's revenues raises clear constitutional and equity

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that the amount of tax received by the government is less than the amount allowed as estimated taxes [*i.e.*, in rates]." *Id.* at 2.

As demonstrated by Deputy Attorney General Shepherd's analysis, a stand-alone approach to attribution does not perpetuate the status quo. Instead, SB 408 requires rate adjustments when the taxes in rates exceed the lesser of the two measures of taxes paid defined in section 3(12). In this way, SB 408 creates an exception to the stand-alone attribution approach when affiliate losses *in total* result in the affiliated group's tax liability being less than the utility's stand-alone tax liability, such that the affiliated group's tax liability replaces the stand-alone tax liability as the utility's tax expense under the "lesser of" test. *See* SB 408 § 3(12).[7] Thus, when a utility collected more taxes in rates than its affiliated group paid to units of government,[8] SB 408 requires the Commission to direct the utility to establish an automatic adjustment clause to account for the difference. *See* SB 408 §§ 3(6), (12).

2. Stand-Alone Attribution Effectuates the Act's Stated Purpose of Aligning Amounts of Income Tax Collected in Rates with Taxes Actually Incurred and Paid by Utilities to Government Taxing Authorities.

Section 3(12) states that the attribution of "taxes paid" to the utility "may not exceed" the lesser of consolidated or stand-alone tax payments, demonstrating the legislature's intention that customers receive a rate adjustment when a utility collected tax in excess of the lesser of (a) its stand-alone tax expense or (b) the amount paid to government by the utility or

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issues, the Commission should carefully consider during this rulemaking proceeding whether the legislature actually intended for a utility with unexpectedly high costs or other events that cause the utility to under-earn (due to for example weather conditions or energy markets) to suffer further reductions in revenues through an SB 408 adjustment, and, if so, whether the Commission can or must put in place a regulatory mechanism to recover the extra costs.

[7] This approach to allocation of affiliate losses is sometimes referred to as a "*United Gas Pipe Line*" or "pour-over" approach to allocation of consolidated tax benefits. *See* discussion of *United Gas Pipe Line* at Section III.A.4.b, *infra.*

[8] "Taxes paid" is net of adjustments specified in SB 408, including deferred taxes, charitable contributions and non-recognized utility investments. SB 408 § 3(13)(f)(A)-(C).

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its affiliated group. In other words, SB 408 allows the utility to retain recovery in Oregon retail rates only for the lesser of these two amounts. In this way SB 408 effectuates the underlying policy of addressing the so-called "Enron problem" — by insuring that the affiliated group *in total* pays at least as much in tax as is embedded in Oregon rates.

a. The Stand-Alone Attribution Approach Solves the So-Called "Enron Problem" — That Is, It Results in a Rate Decrease When a Utility Collected More for Taxes Than Its Affiliated Group Paid to Units of Government.

To illustrate, take the examples provided in Staff's August 12, 2005 letter to Oregon utilities:[9]

	Utility A	Utility B	Utility C
Regulated Utility Operations (tax liability)	130	130	130
Affiliate X (tax liability)	130	65	-20
Affiliate Y (tax liability)	-60	-95	-60
Taxes Paid to Government	200	100	50

Pursuant to section 3(12)(a), the Commission would first ask what is the tax liability incurred as a result of income from regulated operations. For Utilities A, B, and C, that amount is $130. Then, pursuant to section 3(12)(b), the Commission would ask what is the amount of tax paid to units of government by the utility or its affiliated group. For Utility A, that amount is $200; for Utility B, it is $100; and for Utility C, it is $50. Thus, because the "taxes paid that are properly attributed to the regulated operations of the public utility may not exceed the lesser of" the section 3(12)(a) or (b) amounts, the taxes paid and properly attributed to each utility are as follows: for Utility A $130 (the lesser of (a) $130 and (b) $200); for Utility B $100 (the lesser of (a) $130 and (b) $100); and for Utility C $50 (the

[9] This example does not appear to address situations in which affiliates are regulated utilities or situations in which the Oregon regulated utility has a negative tax liability, both of which raise added layers of complexity. *See, e.g.*, discussion regarding regulated affiliates and normalization violations *supra* at 20-21.

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lesser of (a) $130 and (b) $50). Thus, Utility B would be subject to an automatic adjustment clause to refund to customers $30 and Utility C would be subject to an automatic adjustment clause to refund to customers $80.[10]

b. Loss-Allocation Approaches Base Tax Adjustments Solely on the Tax Liabilities of Individual Affiliates and the Corporate Organization of the Affiliated Group, Without Regard to the Taxes Incurred as a Result of Regulated Operations.

Consistent with the plain directives of SB 408, the stand-alone approach bases tax adjustments on whether taxes were incurred as a result of the regulated operations of the utility and paid to units of government. In contrast, whether a rate adjustment occurs under a loss-allocation approach such as the one adopted in the temporary rule, OAR 860-022-0039, may depend entirely on the tax liability of an individual affiliate or the corporate organization of the affiliated group. The arbitrary results produced by a loss-allocation approach can be illustrated by looking again to the examples provided by Staff.

Most notably, under a loss-allocation approach, the amount deemed to be paid and properly attributed to Utility A would not be $130 (the lesser of its stand-alone tax liability and the amount paid to government by its affiliated group); rather, the amount deemed to be paid and properly attributed to Utility A would be $100, because a loss-allocation approach requires the Commission to disregard Affiliate Y's negative tax liability and distribute the amount paid to units of government by the affiliated group among the members of the group with a positive tax liability (Utility A and Affiliate X). Thus, Utility A would be subject to an automatic adjustment clause to refund to customers $30.[11] This is despite the fact that the

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[10] This analysis assumes the amount of "tax authorized to be collected in rates" is the same as the utilities' stand-alone tax liability ($130 for all three utilities) and that the "taxes paid" figures are net of the adjustments required by SB 408.

[11] This analysis assumes the amount of "tax authorized to be collected in rates" is the same as the utility's stand-alone tax liability ($130) and that the "taxes paid" figures are net of the adjustments required by SB 408.

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amount of tax incurred by the utility as a result of income generated by its regulated operations was $130 and this amount was in fact paid by the affiliated group to units of government.

This result is particularly egregious and arbitrary in light of the fact that the utility incurred the full cost of its stand-alone tax liability. In other words, the utility generated tax income that "caused" this expense and this expense "caused" the affiliated group's payment to be higher by a corresponding amount. If the utility's tax liability had been less, the affiliated group's actual payment would have decreased by a corresponding amount. For example, if Utility A's stand-alone tax liability had been $120 ($10 less), the affiliated group would have paid to units of government $190 ($10 less). Likewise, if Utility A's stand-alone tax liability had been $0 ($130 less), the affiliated group would have paid to units of government $70 ($130 less). An approach that denies Utility A the opportunity to recover an incurred expense, which was actually paid to units of government, is contrary to SB 408 and a violation of Utility A's constitutional right to fair and symmetrical ratemaking and to rates that permit an opportunity to recover costs and earn a fair rate of return. *See FPV v. Hope Natural Gas Co.*, 320 US 591 (1944); ORS 756.040(1) (codifying *Hope* standard). Thus, adoption of a loss-allocation approach would reduce rates by allocating affiliate losses to the utility even when the utility incurred its full tax expense *and* the utility's consolidated group paid more taxes to government than the utility collected in rates. In this way, a loss-allocation approach would inevitably violate *Hope* and ORS 756.040.

When a statute is susceptible to more than one interpretation, and one is more consistent with the statute's constitutionality, the constitutional interpretation prevails. *Vorm v. David Douglas School Dist. No. 40*, 609 P2d 193, 195 (Or App 1980); *City of Portland v. Welch*, 364 P2d 1009, 1012 (Or 1961). Accordingly, the Commission is constrained by its statutory obligation under ORS 756.040 and the constitutional limits

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expressed in *Hope* from adopting a loss-allocation approach to the term "properly attributed."[12]

As further evidence of the arbitrary nature of this approach, a loss-allocation approach would also produce different results simply depending on the corporate organization of the utility's affiliated group. That is, whether a rate adjustment is required when a utility's affiliated group paid taxes in excess of the utility's stand-alone tax expense could depend entirely on whether the utility's affiliates were organized as separate companies or merged companies.

Taking the example of Utility A again, if Affiliate X and Affiliate Y were merged into one corporate entity, the amount of taxes paid and properly attributed to Utility A would be $130. However, if Affiliate X and Affiliate Y remain separate corporate entities, the amount of taxes paid and properly attributed to Utility A would be $100.

Thus, whether or not an adjustment occurs could depend entirely on whether the utility's affiliates were separate or merged companies, despite the fact that, under either scenario:

- Government units received the same amount in tax payments from the affiliated group;
- Utility A's cost-of-service, including its stand-alone tax expense, remained the same; and;
- The Affiliates' total tax expense remained the same.

[12] Although SB 408 *on its face* raises serious constitutional concerns, PacifiCorp and Avista do not intend to assert challenges to the statute's legality in this proceeding. Instead, PacifiCorp and Avista reserve their right under *England v. Louisiana Bd. of Med. Examiners*, 312 US 411, 84 S Ct 461, 11 L Ed 2d 440 (1964), to bring such challenges in an appropriate federal court.

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To illustrate:

			Effect if Affiliate X and Y Are Merged	
	Stand-Alone Tax Liability	Loss-Allocation "Properly Attributed" Amount	Stand-Alone Tax Liability	Loss-Allocation "Properly Attributed" Amount
Utility A	$130	$100	$130	$130
Aff. X	$130	$100	$70	$70
Aff. Y	($60)	$0		
Consolidated Tax Payment	$200	$200	$200	$200

Thus, if Affiliate X and Affiliate Y were merged into one corporate entity, Utility A would be allowed to retain recovery of $130. In contrast, if Affiliate X and Affiliate Y remain separate corporate entities, Utility A would be subject to an automatic adjustment clause to refund to customers $30.[13] This irrational outcome demonstrates the problematic nature of loss-allocation approaches.

3. A Stand-Alone Approach to the Term "Properly Attributed" Appropriately Limits the Commission's Review Function to the Taxes Paid by the Utility and Its Affiliated Group, Not Each of the Group's Members.

Additionally, unlike a loss-allocation approach, a stand-alone attribution approach would not require the Commission to review the tax returns of individual non-utility affiliates, but rather would require only that the Commission determine (a) the taxes paid and incurred by the stand-alone utility as a result of income generated by its regulated operations and (b) the total taxes paid to units of government by the utility's affiliated group. In contrast, a loss-allocation approach would require the Commission to review not only the

[13] This analysis assumes the amount of "tax authorized to be collected in rates" is the same as the utility's stand-alone tax liability ($130) and that the "taxes paid" figures are net of the adjustments required by SB 408.

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consolidated tax liability of the entire affiliated group but also the individual stand-alone tax liabilities of each non-utility affiliate. The Commission also might be required to audit the tax information of each affiliate to determine whether the reported tax liabilities were accurate.[14] The tax information of nonregulated affiliates is highly sensitive business information that is protected from disclosure by federal law. *See* IRC § 6103(a) (no officer or employee of any state may disclose any tax return or return information provided to the IRS). Thus, a loss-allocation approach to properly attributed would place the Commission in the inappropriate position of reviewing non-jurisdictional entities' confidential and highly sensitive business information.

4. Had the Legislature Intended the Term "Properly Attributed" to be Code for a Specific Allocation Formula, It Would Have Said So.

"Properly attributed" is not defined in other Oregon statutes or tax law. Nor does anything in the Act or legislative history indicate a legislative intent that the "properly attributed" language in SB 408 be code for a specific allocation formula. To interpret the words "properly attributed" as code for a formula that required the Commission to disregard certain losses and base an allocation on the taxable income of individual affiliates with positive taxable income would run afoul of the "cardinal" rule of construction, which requires courts to construe statutes according to their terms. *See PGE*, 317 Or at 611; *see also Connecticut Nat'l Bank*, 503 US at 253-54.

Proponents of a loss-allocation approach such as the one adopted in the temporary rule may point to the models employed in other states, such as Pennsylvania, as a basis for interpreting "properly attributed" in this way. However, the mere fact that other jurisdictions adopt a particular approach does not change the fact that Oregon has not adopted that approach. Nothing in the Act or legislative history indicates that the Oregon legislature

[14] As explained in Section III.A.5, *infra*, such a result would place the Commission outside of its regulatory jurisdiction.

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modeled SB 408 after existing law in another jurisdiction. Instead, the legislative history demonstrates that the Act's proponents believed that consolidated taxes are being considered in a number of states, but does not indicate any attempt to model SB 408 after the law of any particular state. *See* Statement by Sen. Rick Metsger, Senate Floor Debate on SB 408 (June 8, 2005) (listing seven jurisdictions that he believes use a consolidated approach).[15]

a. SB 408 Is Not Modeled After Pennsylvania.

The Pennsylvania approach was cited only twice in the entire legislative record relating to SB 171 and SB 408, and then only as a reference to one of several states that do not follow a stand-alone tax approach. *See id.*; Statement by Chair Sen. Ryan Deckert, Public Hearing on SB 171 before the Senate Revenue Committee (Apr. 14, 2005).[16] Indeed, when the Oregon legislators drafted, debated, and ultimately passed SB 408, they were aware that the Commission and the Oregon Department of Justice believed that the approach used in Pennsylvania was flawed. *See* Letter to Sen. Ryan Deckert, Chair Senate Revenue Committee, and Sen. Rick Metsger, Chair Senate Business and Economic Development Committee, from the Commission at p. 1 (attaching legal memorandum from Department of

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[15] Senator Metsger stated:

> "A couple of issues were brought about other states, and I wanted to talk a little bit about that. There are other states that take into account the taxes. Connecticut, this is from the Public Utility Commission in their white paper and their investigation. The study that was done. Connecticut, Florida, Indiana, Pennsylvania, Tennessee, Virginia and West Virginia, report that they do consider the savings from the consolidated returns and recognize those for the rate making purposes. Additionally, the Pennsylvania PUC, consistent with the state supreme court decisions, applies this same actual taxes paid standard by including a utility's share of federal taxes benefits when they do set the rates. Now, in Oregon, why do we have a situation in Oregon that's a little more difficult? Well, one of the major reasons is we're an income tax state."

[16] Chair Deckert stated: "Well, other states do, I mean, we've heard a lot about Pennsylvania, who does a true-up. We can get that, I mean, there are other states. I want to say 41 states have the consolidated form on their regulated utilities."

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Justice and noting that Commission had previously provided the committees with a copy of the Commission Staff's White Paper on the Treatment of Income Taxes in Utility Ratemaking (the "White Paper")). In that legal opinion, which the Commission brought to the legislature's attention, the Department of Justice analyzed Pennsylvania's approach, concluding:

> "The flaw with the Pennsylvania approach is not that it follows the actual taxes paid doctrine but that it patently fails to consider aligning the benefits and burdens of the consolidated tax structure. While I have concluded that this Commission could adopt an actual taxes paid doctrine to calculate tax expenses, it must do so in a rational, symmetrical way. This is why the Pennsylvania cases are incorrect – they do not even attempt to align the benefits and burdens of the tax treatment. In fact, the Pennsylvania approach does not look at all the consolidated companies in the parent's corporate family. It looks only at those who lost money in recent years. It ignores those that were profitable, except for the purpose of calculating the utility's share of tax savings from the losing companies."

Legal Memorandum to the Commission from Assistant Attorney General Jason Jones at 5 (Feb. 18, 2005) (footnote omitted); s*ee also* White Paper at 11-12 (Feb. 2005) (criticizing the Pennsylvania approach, stating that "[t]he Commission's counsel advises that those making a legal challenge to this approach will likely point to the lack of an economic rationale in attacking it"). Nowhere in the legislative history does anyone question or contradict the advice contained in these records.

The fact that Pennsylvania was not the Oregon legislature's model for SB 408 is also demonstrated by the many differences between the two states' approaches. Unlike SB 408, Pennsylvania's rule (a) is applied in general rate proceedings during which the parties and the Pennsylvania public utility commission have the opportunity to approve of an overall rate of return that is reasonable for both the customers and the utility; (b) is not based on statutory prescriptions; (c) does not apply to stand-alone utilities; (d) does not use an automatic adjustment clause; (e) does not true-up past taxes paid with past over- or under-collections;

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and (f) does not include statutory offsets for deferred taxes, unrecovered utility investments, and charitable deductions.

b. Nor Is SB 408 Modeled After Any Other Existing Law.

Nothing in the Act or legislative history indicates a legislative intent to model SB 408 after any other existing law. There is no uniformity in the approaches applied by the states that Senator Metsger identified. Some evaluate only the utility and its corporate parent's tax liabilities; others use methods that are not well explained in the applicable orders; Pennsylvania and West Virginia appear to allocate affiliate losses to utilities in the manner adopted in the temporary rule; and Connecticut appears to use the net-loss or stand-alone attribution approach described in SB 408. *See Re United Illuminating Co.*, 2002 WL 31720159 (Conn DPUC 2002). However, none of these states has a scheme that is entirely consistent with SB 408.

As in Connecticut, the Federal Energy Regulatory Commission's predecessor, the Federal Power Commission (the "FPC") used a net-loss allocation approach until 1972 that was similar to SB 408; this approach is often referred to as the *United Gas Pipe Line* approach. *See FPC v. United Gas Pipe Line*, 386 US 237, 87 S Ct 1003, 18 L Ed 2d 18 (1967) (FPC's approach was within FPC's statutory authority); *see also Florida Gas Transmission Company*, 47 FPC 341, 93 PUR 3d 477 (1972) (rejecting *United Gas Pipe Line* approach in favor of stand-alone approach).

The plain language of SB 408 is consistent with the allocation approach approved of in *United Gas Pipe Line*. There, affiliate losses were applied to reduce a utility's stand-alone tax expense only if such losses were not fully offset by affiliate gains. 386 US at 241; *see also Cities Service Gas Co.*, 30 FPC 158, 49 PUR 3d 229 (1963) (using approach). Under this approach, as intended by SB 408, affiliate losses are taken into account only if the consolidated tax liability is less than the utility's stand-alone tax liability. *See El Paso Natural Gas Co.*, 46 FPC 454, 90 PUR 3d 462 (1971) (applying *United Gas Pipe Line*

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approach, but making no consolidated tax adjustment, because there was no net loss to be applied to the regulated company's income).

c. Thus, an Approach That Allocates Affiliate Tax Losses to a Utility When the Affiliated Group Pays More Tax Than the Utility's Stand-Alone Tax Liability Is Not Within the Legislative Delegation of Authority.

Rules implementing a statute must be within the legislative delegation of authority and reasonably calculated to accomplish the legislative purpose. *Pacific Northwest Bell Telephone Co. v. Davis*, 43 Or App 999, 1005, 608 P2d 547 (1979) (citing *Crouse v. Workmen's Comp. Bd.*, 26 Or App 849, 852, 554 P2d 568 (1976)). Here, except when the section 3(12) cap is implicated, the Act does not authorize the Commission to allocate affiliate tax losses to the utility. Thus, the loss-allocation approach adopted in the temporary rule is wrong in its treatment of affiliate tax losses and is not in conformance with SB 408.

5. A Stand-Alone Approach to the Term "Properly Attributed" Limits Unintended Consequences.

Approaches that allocate affiliate losses to utilities, even when the affiliated group paid more tax than the utility collected in rates, implicate significant, negative unintended consequences. For example, under a loss-allocation approach, the Commission would be required to audit the stand-alone tax liability of each affiliate of the utility, ultimately expanding the purview of the Commission's regulatory oversight to non-jurisdictional entities. Thus a loss-allocation approach would place the Commission in the business of investigating affiliate and parent tax issues and the reasonableness of their business decisions, an area outside of its regulatory jurisdiction.[17]

[17] Information that is solely within the control of a utility's unregulated parent, subsidiary, or affiliate is outside the scope of the Commission's investigative powers, which are limited to regulated utilities within the Commission's jurisdiction. *See* ORS 756.070-.125 (Commission has authority to investigate management of "public utilities"); ORS § 757.005 (defining "public utility"). SB 408 does not expand these powers.

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This is especially problematic with respect to *utility* operations in other jurisdictions. SB 408 did not intend to capture tax benefits or losses of utility operations in other jurisdictions and assign those tax benefits to Oregon regulated utility operations. There is no mention in SB 408 of utility operations in jurisdictions other than Oregon. Indeed, if SB 408 treats utility operations in another jurisdiction the same as non-utility affiliates by apportioning a tax benefit from a utility operation in another jurisdiction to determine tax payment amounts attributed to Oregon utility operations, the result will likely be a violation of the normalization rules of the Internal Revenue Code (the "IRC").[18] A violation of the normalization rules would cause potentially extreme rate increases.[19] Indeed, the legislature recognized expressly the need to protect customers from such an outcome. *See* SB 408 §§ 3(8), 3(13)(f)(C).

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[18] Under the normalization rules, the investment tax credit and accelerated depreciation are available to companies that operate utilities only if they follow the normalization method of accounting. In order to use a normalization method of accounting, the utility must treat assets consistently in ratemaking and tax accounting. IRC § 168(i)(9); *see* Priv Ltr Rul 2004-18-001 (Apr. 30, 2004) (utility's maintenance of an accumulated deferred federal income tax reserve associated with property that was excluded from the utility's regulated books of account would violate the consistency requirement of section 168(i)(9)(B) and the normalization rules, because the utility's rate base, tax expense, and depreciation expense for ratemaking purposes would be determined without the cost of the excluded property). If SB 408 causes the deferred taxes of an out-of-state utility to be flowed through to ratepayers in Oregon, that utility property will be treated inconsistently in ratemaking and tax accounting — thereby violating the normalization rules.

[19] The consequence of violating the IRC normalization requirements is severe: the utility (or filing entity) would lose the right to claim accelerated depreciation on its federal tax returns. IRC § 168(f) (depreciation deduction determined under section 168 shall not apply to any public utility property if the taxpayer does not use a normalization method of accounting). This consequence may be permanent with respect to any utility property existing at the time of the violation. *See id.* The loss of accelerated depreciation would probably cause decreased investment in utilities and their affiliates, decreased diversification of utilities, and increased rates and prices in all jurisdictions in which the affected utilities and affiliates do business. *See* White Paper at 9 (identifying annual rate impact of the loss of normalization on Oregon customers of Portland General Electric and PacifiCorp as between $20 and $30 million).

B. Investments/Credits – What Did the Legislature Intend in Adoption of Section 3(13)(f)(B)?

Response: In adopting Section 3(13)(f)(B), the legislature intended to avoid confiscation of tax savings associated with unrecognized utility investments by providing for an adjustment to "taxes paid" for tax savings arising from expenditures in regulated operations of the utility that were not taken into account in ratemaking.

1. Section 3(13)(f)(B) Provides for an Adjustment to "Taxes Paid" for Tax Savings Arising from Unrecognized Expenditures in the Regulated Operations of the Utility.

According to the relevant sections of SB 408:

> "(f) 'Taxes paid' means amounts received by units of government from the utility or from the affiliated group of which the utility is a member, whichever is applicable, adjusted as follows:
>
> * * * * *
>
> "(B) Increased by the amount of tax savings realized as a result of tax credits associated with investment by the utility in the regulated operations of the utility, to the extent the expenditures giving rise to the tax credits and tax savings resulting from the tax credits have not been taken into account by the commission in the utility's last general ratemaking proceeding[.]"

On its face, section 3(13)(f)(B) lacks a plain meaning with respect to utility expenditures and investments.[20] It is only in the context of the Act's underlying policies and traditional ratemaking principles that the section's meaning becomes clear.[21] In that context, section 3(13)(f)(B) provides for an adjustment to "taxes paid" for tax savings arising from

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[20] The statute is clear that tax savings incurred as a result of affiliate activities do not serve to increase the amount of taxes paid.

[21] In determining legislative intent, it is proper for a court to consider the policy and purpose of a statute, and to consider in that connection whether or not such policy will be attained by a literal interpretation of the language used. *State v. Buck*, 262 P2d 495, 497 (Or 1953) (citing *Swift & Co. v. Peterson*, 233 P2d 216, 223 (Or 1951)).

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any expenditure in the regulated operations of a utility that was not taken into account in ratemaking. Thus, SB 408 allows utility investors to retain the tax benefits of, for example, Business Energy Tax Credits ("BETCs") that utilities purchase when the cost of such purchases are not included in rates. Likewise, SB 408 allows utility investors to retain tax benefits of other expenditures in regulated utility operations that were not taken into account in ratemaking. Such an interpretation is consistent with traditional cost-causation principles and the requirement to match "benefits and burdens," which the Department of Justice has advised is a legal standard for ratemaking in this context.

2. This Interpretation Is Supported by the Text of SB 408.

Although at first glance the text of section 3(13)(f)(B) is confusing, upon a close reading of the section, it appears that the legislature intended "tax credits" to mean any tax item that gives rise to a tax savings.[22] The Act provides that "taxes paid" are "[i]ncreased by the amount of tax savings realized as a result of tax credits" to the extent that "tax savings resulting from the tax credits have not been taken into account" for ratemaking purposes. SB 408 § 3(13)(f)(B). To give meaning to this provision, the Commission should reject any interpretation of "tax credits" that fails to give effect to both phrases. *See Murphy v. Nilsen*, 527 P2d 736, 739 (Or App 1974) (citing *Blyth & Co. v. City of Portland*, 282 P2d 363 (Or 1955) (statutes should be interpreted to give effect to every section, clause, phrase or word). The only interpretation that gives effect to both phrases is one that recognizes that the drafters intended "tax credits" to mean anything that gives rise to tax savings. In other words, the term "tax credits" includes not only items that are themselves tax savings, but also items that, when applied, produce tax savings (*i.e.*, deductions).

[22] The legislative record does not explain the intent of this provision. Although the record contains a number of references to "tax credit" and "investments," none of these references address these terms as they are used in section 3(13)(f)(B).

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3. This Interpretation Is Consistent with State of Oregon and Commission Policies Encouraging Energy Conservation and Investment in Utility Infrastructure.

This interpretation is consistent with state of Oregon and Commission policies encouraging energy conservation and investment in utility infrastructure. Indeed, any other interpretation of section 3(13)(f)(B) would eliminate the economic incentive for utility investors to make such investments. Lawmakers frequently use tax credits *and other tax benefits* to encourage investment in activities such as development of renewable resources. *See, e.g.*, ORS 469.190 (BETCs encourage use of renewable resources); Oregon Department of Energy, Oregon Renewable Energy Action Plan at 1 (2004) (*available at* http://egov.oregon.gov/ ENERGY/RENEW/docs/FinalREAP.pdf) ("We can make Oregon the national leader in renewable energy and renewable product manufacturing. …. Development of renewable energy will lessen our reliance on fossil fuels, protect Oregon's clean air and create jobs.") *quoting* Governor Kulongoski (2003)); Energy Policy Act of 2005, Title XV, "Energy Policy Tax Incentives Act," HR 6, 109th Cong (2005) (enacted) (encouraging investment in utility infrastructure).[23] Any approach that limits the effectiveness of these tax benefits or otherwise discourages investment in renewable energy and utility infrastructure would be contrary to state and federal energy policy. *See Re Nat'l Rates for Natural Gas*, 4 PUR 4th 401 (Fed. Power Comm'n 1974) ("'[T]o reduce the rates of a regulated pipeline because of . . . [tax losses resulting from] affiliated exploration and

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[23] *See also* White House Press Release (*available at* www.whitehouse.gov/news/releases/2005/08/print/20050808-4.html), which states:

> "The energy bill will help modernize our aging energy infrastructure to help reduce the risk of large-scale blackouts and minimize transmission bottlenecks. This will be accomplished by repealing outdated rules that discourage investment in new infrastructure, offering tax incentives for new transmission construction, and by encouraging the development of new technologies, such as superconducting power lines, to make the grid more efficient."

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development activities would be discouraging to the very enterprise we now want to encourage.'" (citation omitted)).

Allocating the tax benefits of participation in these ventures to entities that do not take the risk of investment would decrease or eliminate the economic value of these tax incentives. Thus, if "tax credits" in section 3(13)(f)(B) is interpreted narrowly to mean tax credits as defined by the IRC, SB 408 will discourage utility investors from investing in renewable energy and utility infrastructure and would therefore be contrary to state and federal energy policy. When utility investors bear the risk of such investments (*i.e.*, the costs are not included in rates), state and federal policy directs that they should receive the benefit.

Consistent with the interpretation of section 3(13)(f)(B) outlined above, in advocating for SB 408's passage, the Citizens' Utility Board of Oregon and Industrial Customers of Northwest Utilities assured legislators that section 3(13)(f)(B) broadly preserved tax benefits associated with renewable energy investment:

> "*The utilities say, 'The bill undermines Oregon's renewable energy industry.'*
>
> "**RESPONSE: Tax credits and tax incentives that exist today will exist after the bill's passage.**
>
> "Again, the bill changes nothing in utility ratemaking or tax policy. If a utility wishes to avail themselves of tax credits and incentives, customers can support that. The bill discourages nothing. In fact, Section 3[13](f)(B) allows the amount of taxes paid to be '**(i)ncreased by the amount of tax savings realized as a result of tax credits associated with investment by the utility in the regulated operations of the utility, to the extent the expenditures giving rise to the tax credits and tax savings resulting from the tax credits have not been taken into account by the commission in the utility's last general ratemaking proceeding.**' This means that the utility can take into account any tax credits or incentives when reporting its taxes paid, as long as those credits were not already accounted for in a previous rate case."

See Utility Customers Ask for Fairness and Equity: Taxes Collected Must Align with Taxes Paid; Vote Yes on SB 408-C (emphases in original), attached hereto as Exhibit B.

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C. "Material Adverse Effect" — May the Commission Terminate the Automatic Adjustment Clause upon [a] Showing by a Utility that the Automatic Adjustment Clause Has a Material Adverse Effect on the Utility?

Response: Pursuant to its duty to set rates that are fair, just and reasonable, the Commission must terminate any automatic adjustment clause that causes rates to be so low as to materially adversely affect the utility.

Section 5(1)(a) contains a downward limit on rate adjustments in that it prohibits the Commission from authorizing a rate or schedule of rates that is not "fair, just and reasonable." SB 408 § 5(1)(a). Conversely, section 3(9) contains an upward limit in that it requires the Commission to terminate any automatic adjustment clause that the Commission determines "would have a material adverse effect on customers of the public utility." SB 408 § 3(9). Accordingly, the Commission must terminate any automatic adjustment clause that would result in unreasonably high or low rates.

1. "Fair, Just and Reasonable" Provides a Downward Limit on Rate Adjustments.

SB 408 does not define the term "fair, just and reasonable." The terms "fair" and "just" are commonly defined as having interchangeable meanings; *e.g.*, "fair" is defined in part as "just," and "just" is defined in part as "fair." *See Webster's New World Dictionary* (4th ed 2001) (defining the term "fair" as "just and honest; impartial; unprejudiced; according to the rules;" defining the term "just" as "right or fair; equitable; impartial; well-founded; reasonable;" defining the term "reasonable" as "using or showing reason, or sound judgment, sensible; not extreme, immoderate, or excessive.").

This interchangeable meaning is consistent with usage of the terms in related statutes. As with ORS 757.210, as amended by SB 408, these statutes declare that the Commission must set fair, just, and reasonable utility rates — using the terms "fair" and "just" interchangeably. *See, e.g.*, ORS 756.040(1) (codifying the *Hope* standard by requiring the Commission to "balance the interests of the utility investor and consumer in establishing fair

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and reasonable rates"); ORS 757.273 ("All rates * * * by any public utility or telecommunications utility for any attachment by a licensee shall be just, fair and reasonable."); ORS 757.285 ("Agreements regarding rates * * * [for] attachments shall be deemed to be just, fair and reasonable, unless the Public Utility Commission finds * * * that such rates * * * are adverse to the public interest and fail to comply with the provisions hereof."); ORS 757.495 (Commission must find certain contracts to be "fair and reasonable").

As the Court explained in *Hope*, the requirement that rates be fair, just, and reasonable does not define a method by which rates are to be calculated; instead, the fixing of fair, just, and reasonable rates involves a balancing of investor and consumer interests. *Fed. Power Comm'n v. Hope Natural Gas Co.*, 320 US 591, 603 (1944). Subsequently, the *Hope* Court's explanation of the standard was incorporated almost verbatim in ORS 756.040(1). *See Hope*, 320 US at 603-04. ORS 756.040(1) defines the term "fair and reasonable" as follows:

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

Thus, the text and context of SB 408 indicate that by using the term "fair, just and reasonable," the Oregon legislature intended to prohibit the Commission from adjusting rates in a manner that fails to provide adequate revenue for operating expenses, capital costs, and a return on investment commensurate with other similar enterprises and sufficient to maintain the utility's financial integrity.

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Given the plain, ordinary meaning of the term "fair, just and reasonable," which is apparent from the text and context of SB 408, under the *PGE* framework, the analysis would be at an end. *PGE*, 859 P2d at 1146. Nevertheless, even if this term was adjudged to be ambiguous, this same interpretation is also fully supported by the legislative record. On numerous occasions, the Department of Justice advised the legislature that the law must allow the Commission to set rates that are "fair"; otherwise, the law could result in an unconstitutional taking of private property under *Hope*. *See, e.g.*, Statement of Deputy Attorney General Peter Shepherd, Senate Bill 408 Public Hearing, House State and Federal Affairs Committee (June 30, 2005) ("[R]ate setters must allow investors in a regulated utility to recover their prudent expenses and earn a fair return on their investment. This is, you'll hear people refer to this as the *Hope* Test[.]"); Statement of Assistant Attorney General Paul Graham, SB 408 Work Session, House State and Federal Affairs Committee (July 15, 2005) ("[*Hope* is] the case that prohibits contriscatory [sic] rates and what the *Hope* case says is that a regulator can use any method it wants to set rates, but at the end of the day, the bottom line, has to be that the rates allow the utility * * * a reasonable opportunity to earn a fair return on the investment it's made to serve rate payers.").

Thus, as the Department of Justice explained, the inclusion of the "fair, just and reasonable" language in ORS 757.210 sets a "downward limitation" on the adjustment that the Commission can make under the Act. Statement of Peter Shepherd, SB 408 Work Session, House State and Federal Affairs Committee (July 15, 2005) ("[The] PUC cannot allow the adjustment if it would result in a rate which is not fair, just and reasonable, as the terms of the total rate. So, that there would be an upward limitation, as well as a downward limitation."). *See also* Statement of Rep. Tom Butler, SB 408 Work Session, House State and Federal Affairs Committee (July 15, 2005) ("fair, just and reasonable" language "attempts to make [the adjustment] both symmetrical, as well as nonconfiscatory and in that regard completely constitutional"); Statement of Rep. Tom Butler, House Chamber Session

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(July 30, 2005) ("The bill's current proponents contend that the trigger to stop the downward spiral was that the rates must be fair, just and equitable—fair, just and reasonable."); Statement of Rep. Robert Ackerman, House Chamber Session (July 30, 2005) ("I conclude that the 'fair, just and reasonable' standard and the limited use of the automatic adjustment clause satisfies constitutional requirements. Now that is from our Legislative Counsel."). *See also* written Testimony of Deputy Attorney General Pete Shepherd, Work Session on SB 408, House State and Federal Affairs Committee (June 30, 2005) (describing "fair, just and reasonable" language as providing protection against *Hope* violation).

In any event, SB 408 must be interpreted in a way that is consistent with its constitutionality. *Vorm*, 609 P2d at 195 (courts are required to interpret statutes in a manner consistent with their constitutionality); *see also Welch*, 364 P2d at 1012 (the court is "bound to uphold the constitutionality of legislation when it is possible to do so"); *Easton v. Hurita*, 625 P2d 1290, 1292 (Or 1981) (statutes that are "somewhat ambiguous" must be interpreted so as to avoid "any serious constitutional problems"). Given that *Hope* is a constitutional standard, it is necessary for the Commission to interpret SB 408 in a manner that provides a downward limit on rate adjustments. Consequently, the Commission must terminate any automatic adjustment clause that causes rates to be so low as to materially adversely affect the utility — *i.e.*, rates that fail to provide adequate revenue for operating expenses, capital costs, and a return on investment commensurate with other similar enterprises and sufficient to maintain the utility's financial integrity.

2. "Material Adverse Effect" Provides an Upward Limit on Rate Adjustments.

The legislature did not define the term "material adverse effect" within SB 408, preferring instead to leave the determination to the Commission's discretion. *See* Colloquy between Dexter Johnson, Chair Sen. Rick Metsger, and Sen. Vicki Walker, Senate Business and Economic Development Committee, Senate Bill 408 Work Session (May 31, 2005)

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("There was concern that that definition was too inflexible and so that definition has been omitted and in its place is a restriction on the [Committee] that they may not make the material adverse effect finding and therefore not impose an automatic adjustment clause unless they conduct a hearing as part of that determination that would allow rate payer advocates and utilities to in an adversarial context argue whether or not there is in fact a material adverse effect."); Sen. Vicki Walker (proponent of bill), Senate Chamber Debate On Senate Bill 408 (June 8, 2005) ("Colleagues, then the material adverse affect clause will be defined in a public hearing process so that everyone has input on what that actually means."). It is clear from the legislative record, however, that an extreme upward rate adjustment would constitute a material adverse effect on customers. *See* Sen. Roger Beyer, Senate Chamber Debate on SB 408 (June 8, 2005) ("if the PUC determines that material adverse effect on customers would be too great, they may not require the utility to raise their rates."); Statement of Peter Shepherd, SB 408 Work Session, House State and Federal Affairs Committee (July 15, 2005) ("[The] PUC cannot allow the adjustment if it would result in a rate which is not fair, just and reasonable, as the terms of the total rate. So, that there would be an upward limitation, as well as a downward limitation.").

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D. Estimated Taxes — If a Utility Pays Quarterly Estimated Taxes, Must the Automatic Adjustment Clause be Applied Quarterly, or Does the Law Allow It to be Applied Yearly?[24]

> Response: SB 408 requires annual review and application of automatic adjustment clauses based on actual taxes paid. Consequently, regardless of whether a utility or its affiliated group files quarterly estimated taxes, the law does not permit the automatic adjustment clause to be applied quarterly.

1. The Text and Context of SB 408, and its Legislative History, Demonstrate That Adjustments Cannot Be Based on Quarterly Estimated Payments.

a. The Act Bases Adjustments on Actual Taxes, Not Estimates.

As posed, the question assumes, incorrectly, that the filing of quarterly estimated taxes constitutes "taxes paid" under SB 408. However, the Act requires rate adjustments to be based on actual taxes "incurred" (section 12(a)) and "paid to units of government" (section 12(b)). Taxes submitted with quarterly estimated tax filings are not taxes incurred and paid, but are indeed based on the taxpayer's estimated taxes, which may or may not reflect that taxpayer's ultimate tax liability. For example, a taxpayer may submit estimated taxes in a year in which it turns out not to have any taxes "incurred" and "paid."

Moreover, the concept of applying an automatic adjustment clause based on the amount of estimated quarterly taxes is inconsistent with the definition of "taxes paid" in

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[24] Stated in its entirety, the fourth issue that Administrative Law Judge Logan designated for early resolution is:

> "Section 3 of SB 408 requires the Commission to establish an automatic adjustment clause within 30 days (or later date, established by rule, not to exceed 60 days) once a determination is made regarding the $100,000 trigger amount. Section 4 states that if an automatic adjustment clause is established, it applies only to taxes paid to units of government and collected from ratepayers on or after January 1, 2006. If a utility pays quarterly estimated taxes, must the automatic adjustment clause be applied quarterly, or does the law allow it to be applied yearly?"

ALJ Logan Memorandum at 1.

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SB 408, which adjusts the amount received by government to account for deferred taxes, charitable contributions, and utility investments not included in rates. Until this information is reported in the October 15 tax report, the Commission lacks sufficient information to determine "taxes paid." The Commission simply cannot know the amount of taxes "incurred" and "paid" until after the annual tax reports are filed. SB 408 § 3(1).

b. The Act Requires Annual, Not Quarterly, Reporting and Adjustments.

Nothing in SB 408 refers to or supports the use of a quarterly adjustment. The first step of the *PGE* analysis, looking at the text and context of the statute, provides the answer to the Commission's question: a quarterly review of taxes paid is not allowed. The Act does not contain *any* mention of a quarterly review. On the other hand, annual reporting is expressly required. SB 408 § 3(1). The annual report must contain data for the previous fiscal "year," not "quarter." *Id.* Moreover, the Act expressly provides for the continuation of automatic adjustment clauses on an annual basis:

> "If an adjustment to rates is made under an automatic adjustment clause established under this section, the automatic adjustment clause shall remain in effect for each successive *year* after an adjustment is made and until an order terminating the automatic adjustment clause is made under subsection (9) of this section."

SB 408 § 3(5) (emphasis added). If the legislature had intended to allow quarterly reviews, it could have easily done so, instead of requiring that the automatic adjustment clause remain in effect on an annual basis after an adjustment is made. The Commission should follow the cardinal rule and "presume that a legislature says in a statute what it means and means in a statute what is says there." *Connecticut Nat'l Bank*, 503 US at 253-54. Consideration of taxes on a quarterly basis would be inconsistent with this provision of the Act, which supports only an annual review and application of automatic adjustment clauses.

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2. As a Practical Matter, Quarterly Adjustments Would Be Onerous and Could Result in Unnecessary Rate Volatility.

Quarterly adjustments could result in rate volatility even when, on an annual basis, little or no adjustment is warranted. Commitment of the Commission's, utilities' and other parties' resources to such an unnecessary, time-consuming, and costly exercise is unwarranted. Thus, even if the Commission were to determine that it could utilize quarterly reviews, notwithstanding the express provisions and legislative history to the contrary, the Commission, as a matter of policy, should decline to adopt such an approach.

Moreover, the participants in this docket have agreed that, whether or not the Act allows the Commission to use forecasted data, as a policy matter the Commission should base SB 408 adjustments on historic data only. *See* Letter from Paul Graham, Assistant Attorney General, to Participants in Docket AR 499 at 1-2 (Oct. 7, 2005) (summarizing agreements of participants). The use of estimated quarterly taxes would give the Commission an incomplete and inaccurate picture of the taxes actually paid to units of government.

IV. CONCLUSION

PacifiCorp and Avista urge adoption of the statutory interpretation of SB 408 outlined above.[25] These interpretations give effect to the legislature's intent, as expressed in the text of the statute and in the legislative history.

[25] As explained at footnote 13, *supra*, PacifiCorp and Avista reserve their right under *England v. Louisiana Bd. of Med. Examiners*, 312 US 411, 84 S Ct 461, 11 L Ed 2d 440 (1964), to bring challenges to the legality of the statute itself, including constitutional challenges, in an appropriate federal court.

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DATED: October 28, 2005.

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AVISTA CORPORATION

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October 28, 2005

ELECTRONIC FILING

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Re: Docket No. AR 499

Enclosed for filing is one copy of the Joint Comments of Avista Corporation and PacifiCorp in this matter. A hard copy was served on all parties of record as indicated on the attached certificate of service.

Very truly yours,

Sarah J. Adams Lien

SJL:jlf
Enclosure
cc: Service List

BEFORE THE PUBLIC UTILITY COMMISSION OF OREGON

AR 499

In the Matter of the Adoption of Permanent Rules to Implement SB 408, Relating to Matching Utility Taxes Paid with Taxes Collected.	**JOINT OPENING COMMENTS OF AVISTA CORPORATION AND PACIFICORP**

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BEFORE THE PUBLIC UTILITY COMMISSION OF OREGON

AR 499

In the Matter of the Adoption of Permanent Rules to Implement SB 408, Relating to Matching Utility Taxes Paid with Taxes Collected.	**JOINT OPENING COMMENTS OF AVISTA CORPORATION AND PACIFICORP**

PacifiCorp and Avista Corporation ("Avista") submit these comments jointly. The scope and meaning of SB 408 are now critical issues for Oregon, given the profoundly negative impacts this legislation could have on the financial integrity of the energy utilities that operate in this state. The proper statutory interpretation of SB 408 hinges on the definition and meaning of the term "properly attributed." This issue has particularly significant implications for Oregon's multi-state utilities PacifiCorp and Avista, and for utilities such as PacifiCorp and Avista that file taxes on a consolidated basis with an affiliated group.

I. INTRODUCTION

On September 2, 2005, Governor Theodore Kulongoski signed into law Senate Bill 408 ("SB 408" or the "Act"), noting that "the final version of the bill defers many of the difficult questions about the impact and implementation of SB 408 to the Oregon Public Utility Commission (OPUC)." *See* September 2, 2005 letter from Governor Kulongoski to Secretary of State Bill Bradbury. The Oregon Public Utility Commission ("Commission") initiated this rulemaking docket to answer, among other things, those "difficult questions about the impact and implementation of SB 408."

Recognizing that technical implementation issues cannot be resolved until overarching policy and legal issues are addressed, Administrative Law Judge Kathryn A. Logan designated four issues for early resolution by the Commission in this rulemaking docket. Those four issues are:

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1. How should the Commission apply the "properly attributed" standard as it appears in the individual sections of the bill?

2. What did the legislature intend in adoption of section 3(13)(f)(B)?

3. May the Commission terminate the automatic adjustment clause upon [a] showing by a utility that the automatic adjustment clause has a material adverse effect on the utility?

4. Section 3 of SB 408 requires the Commission to establish an automatic adjustment clause within 30 days (or later date, established by rule, not to exceed 60 days) once a determination is made regarding the $100,000 trigger amount. Section 4 states that if an automatic adjustment clause is established, it applies only to taxes paid to units of government and collected from ratepayers on or after January 1, 2006. If a utility pays quarterly estimated taxes, must the automatic adjustment clause be applied quarterly, or does the law allow it to be applied yearly?

ALJ Logan Memorandum at 1 (Oct. 5, 2005).

The Act leaves a number of its key terms undefined, including the terms "properly attributed" and "material adverse effect." These terms are not defined in other Oregon statutes or tax law. Nor are these terms unambiguously defined in the legislative history of SB 408. However, the legislative history and the Act itself make clear certain directives and policy goals, which must guide the interpretation of these terms. *State v. Bandon*, 582 P2d 52, 53 (Or App 1978) (statutes must be construed "with a view to effecting the overall policy which the statutes are intended to promote"). Although the Act is ambiguous in some respects, the following directives are clear:

- Rates are to be adjusted downward when a utility that is part of an affiliated group collected more taxes in rates than: (A) it incurred (net of certain adjustments specified in SB 408) as a result of its utility operations (*i.e.,* the utility's separate-return or stand-alone tax expense) or (B) its affiliated group paid in taxes to units of government (*i.e.,* the affiliated group's consolidated tax expense).

- Tax liabilities of affiliates may not be used to adjust rates upward or downward, except that affiliate tax benefits may be used to adjust rates downward when an affiliated group paid less tax to units of government than the utility collected in rates.

- Rates may not be adjusted under the Act if doing so would cause rates to be so high that customers would suffer material adverse effects or so low that utilities have no opportunity to recover their costs plus a reasonable return on their investments.

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- Calculations of "taxes paid" under the Act must be done in such a way as to protect incentives for utilities to be good corporate citizens and to invest in utility infrastructure.

- The first rate adjustment under the Act may not occur until some time after 2006, when the Commission can review the difference between taxes collected in rates and taxes actually paid to units of government in 2006.

It is clear from these statutory directives that the legislature intended SB 408 to address the so-called "Enron" problem (*i.e.,* when an affiliated group paid little or no taxes to government) while protecting against unintended consequences, such as penalizing affiliated groups that pay more tax in total than the utility collected in rates, creating disincentives for Oregon utility investment in unregulated businesses, including renewable energy, and discouraging financially attractive, positive tax-paying companies from making investments in Oregon utilities.[1]

In the context of these directives and policy goals, the participants in this docket were able to reach agreement at the first public workshop on the following important principles:[2]

- SB 408 may result in rate increases as well as rate decreases.

- The October 2005 and 2006 tax reports are for the sole purpose of determining whether there is a trigger for the automatic adjustment clause, not to support a rate change.

- The Commission may use historic data for the automatic adjustment clause.

- Whether or not the Act allows the Commission to use forecasted data, as a policy matter the Commission should base SB 408 adjustments on historic data only.

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[1] Although PacifiCorp and Avista find objectionable any allocation of affiliate losses to a utility because such allocations violate cost-causation principles and are likely unconstitutional, PacifiCorp and Avista nevertheless acknowledge that SB 408 clearly provides for the allocation of certain affiliated group losses to utilities when the consolidated group paid less tax to government than the utility collected in rates. However, a loss-allocation approach like that adopted in the temporary rule goes even further by guaranteeing a rate reduction whenever *any single affiliate* suffered a loss – that is, even when the consolidated group paid taxes far in excess of those collected in rates. This extreme overreaching was not the legislature's intent and it is not the premise of SB 408.

[2] *See* Letter from Paul Graham, Assistant Attorney General, to Participants in Docket AR 499 at 1-2 (Oct. 7, 2005) (summarizing agreements of participants) (attached hereto as Exhibit A).

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With the above directives, policy goals, and agreements in mind, PacifiCorp and Avista respectfully submit the following joint opening comments in response to the issues designated by ALJ Logan.

II. STANDARDS OF STATUTORY INTERPRETATION

The ultimate goal in interpreting a statute is to determine the intent of the legislature. *See, e.g., State ex rel. Click v. Brownhill*, 15 P3d 990, 992 (Or 2000); *see also* ORS 174.020(1)(a) ("In the construction of a statute, a court shall pursue the intention of the legislature if possible."); *PGE v. Bureau of Labor and Industries*, 859 P2d 1143, 1145-46 (Or 1993). The Oregon Supreme Court has set out the following three-step analytical framework to use in interpreting a statute:[3]

1. In the first step of the *PGE* analysis, the court looks to the text and context of the statute. *PGE*, 859 P2d at 1146. The text of the statute is considered the best evidence of the legislature's intent. *Id.* In interpreting the text, the court considers rules of construction that bear directly on how to read the text. *Id.* The cardinal rule of construction in this context is that "courts must presume that a legislature says in a statute what it means and means in a statute what it says there." *Connecticut Nat'l Bank v. Germain,* 503 US 249, 253-54. Consequently, courts must give the words of a statute their plain, natural, and ordinary meanings. *See, e.g.,* 859 P2d at 611; *Click*, 15 P3d 990, 992. Also at the first level of the *PGE* analysis, the court examines the context of the statutory provision, which includes other provisions of the same statute, as well as other related statutes. 859 P2d at 1146. Only when the intent of the legislature is not clear from this analysis does the court move to the second step of the analysis.

2. In the second step of the *PGE* analysis, the court examines the legislative history to inform the court's inquiry into legislative intent. *Id.* The court considers the legislative history along with the text and context of the statute to determine if all of these together make the legislative intent clear. *Id.* Again, only if this analysis does not yield an unambiguous result does the court move to the next step of the analysis.

3. In the third step of the *PGE* analysis, the court may resort to general maxims of statutory construction (either looking to Oregon's statutory interpretation statute or to case law) to determine legislative intent.

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[3] All three steps of the *PGE* analysis permit for the use of general rules of construction, some of which are mandated by statute, *e.g.,* ORS 174.010-.090, and others of which are found in case law.

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The *PGE* framework for statutory interpretation informs the responses to ALJ Logan's four issues designated for early resolution by the Commission in this rulemaking docket.

III. RESPONSES

A. "Properly Attributed" — How Should the Commission Apply the "Properly Attributed" Standard as It Appears in the Individual Sections of the Bill?

> Response: In applying SB 408, the Commission should recognize as "properly attributed" the tax liability that results from the economic activities of an entity, without consideration of the tax effects of other affiliated business entities. This stand-alone approach to attribution, combined with recognition of the "lesser of" standard in section 3(12), achieves the legislature's stated intent of decreasing rates when a utility's affiliated group paid less tax to government than the utility collected in rates, while otherwise complying with the legislative prohibition against attribution of affiliate tax liabilities to utilities.

1. It Is Clear from the Text and Context of SB 408, and Its Legislative History, That Taxes "Properly Attributed" Means Tax Payments Incurred as a Result of the Economic Activities of an Entity.

The text and context of SB 408 demonstrate that taxes "properly attributed" means tax payments incurred as a result of the economic activities of an entity without regard to the tax liabilities of other entities. SB 408 leaves the term "properly attributed" undefined, suggesting that the legislature intended the term to be given its common meaning. *See PGE*, 859 P2d at 611; *Click*, 15 P3d at 992. The common meaning of "attribute" is "belonging to, produced by, resulting from or originating in." *Webster's New World Dictionary* 92 (4th ed 2001).

This common meaning is consistent with the use of the term throughout the Act, including section 3(12), which is the only provision of the Act that provides any description of the meaning of the term "properly attributed." There, the Act describes an attribution to the utility of "taxes paid" based on the utility's operations only, stating:

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> "[T]axes paid that are properly attributed to the regulated operations of the public utility may not exceed the lesser of:
>
> "(a) That portion of the total taxes paid that is incurred as a result of income generated by the regulated operations of the utility[.]"

SB 408, 73d Or Legislative Assembly, Reg Sess § 3(12) (2005).

The phrase "portion of the total taxes paid that is incurred as a result of income generated by the regulated operations of the utility" describes an attribution to the utility of "taxes paid" based solely on the tax payments for the regulated operations, or otherwise stated, the tax obligations "produced by or resulting from" receipt of income from regulated operations.[4]

Some may argue that section 3(12)(a) does not require this stand-alone approach to attribution because that section says "taxes paid that is incurred" and "taxes paid" is defined, in part, as "amounts received by units of government." SB 408 § 3(13)(f). However, an interpretation of section 3(12)(a) that limits the amount "incurred as a result of income generated by the regulated operations of the utility" by the "amounts received by units of government" would render the "lesser of" language superfluous. Under such an interpretation, the section 3(12)(a) amount would always be the same or less than the section 3(12)(b) amount. It is also worthy to note that the only time "taxes paid" appears in the operative provisions of the Act without the words "to units of government" is in section 3(12)(a). The omission of "to units of government" and the "lesser of" language are given full effect only if section 3(12)(a) is interpreted to mean taxes incurred as a result of income generated by the regulated operations of the utility.

This interpretation also comports with other related statutes and the Commission's historic practice of computing taxes for ratemaking purposes based on the regulated

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[4] Of course, the "lesser of" qualifier reduces the "taxes paid" if the affiliated group's consolidated taxes are lower than the utility's stand-alone taxes.

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operations of the utility only. Through its use of the term "properly attributed," SB 408 preserves the stand-alone approach to the calculation of tax liability. Moreover, section 3(7) reinforces this approach by expressly precluding consideration of affiliate tax liabilities in calculating the automatic adjustment clause except when the affiliated group paid less tax to units of government than the utility collected in rates.[5]

In particular, the "properly attributed" language and the description of attribution in section 3(7) are consistent with the Commission's statutory obligation to prevent cross-subsidization by maintaining the separation of regulated and unregulated utility operations. *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 whether or not utility is part of an affiliated group for federal and state tax filing purposes); *Re Affiliated Transactions for Energy Utils.*, AR 459, Order No. 03-691, 2003 WL 23305011 at *1 (Or Pub Util Comm'n Dec. 1, 2003) (Commission promulgated stand-alone rule to prevent cross-subsidization); *Re Affiliated Transactions for Energy Utils.*, AR 459, Staff Report at 4 (Or Pub Util Comm'n Aug. 7, 2003) (recommending that Commission initiate rulemaking proceeding to promulgate rules to prevent cross-subsidization); *In re PacifiCorp*, Order No. 03-726, App at 5 (stand-alone method prevents "cross-subsidization").

The legislative history confirms that the legislature intended the taxes attributed to the utility to be the taxes incurred as a result of income generated by regulated operations only, without regard to the tax liabilities of affiliates. In the following colloquy between Senator Rick Metsger, a proponent of SB 408, and Pamela Lesh, Portland General Electric

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[5] Section 3(7) expressly prohibits "adjustments to rates for taxes paid that are properly attributed to any unregulated affiliate of the public utility or to the parent of the utility."

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Company's Vice President for Regulatory Affairs, Senator Metsger explains that the amount attributable to utilities is the amount resulting from regulated operations:

> "Chair [Metsger]: [W]hen they file the report with the commission, it will be those taxes which are attributable only to the operations of that utility, even if you have multiple other affiliates. That's going to have to be figured in the tax report that in this case PacifiCorp would have to file, is to then break that down.
>
> "Lesh: Mr. Chairman, if I could ask a question. Would that work for the losses then as well if the other corporations had had losses and those are offset, would this tax report...
>
> "Chair: It has nothing to do with other corporations, it's only the utility itself. No other affiliations are affected by this. It would be your responsibility to delineate the utility in filing the report with the PUC, what their actual costs were, what their taxes are. It has nothing to do with any other affiliates you have. And that would be your responsibility is to have to extract that cost just like you did in your scenarios, but to actually be able to do that. * * *
>
> * * * * *
>
> "Chair: You can consolidate all you want, but you're not going to be allowed to collect other than the taxes that you owe on this particular, in this case, in the rates that you are collecting for the operation of actually that utility. File anywhere you want."

Work Session on SB 408 before the Senate Business and Economic Development Committee (May 26, 2005). Other portions of the legislative history similarly make clear that any rate adjustment clause should "not apply to the activities of other entities however they are related to the utility, but only to the utility itself." Work Session on SB 408 before the Senate Business and Economic Development Committee (May 31, 2005) (statement of Dexter Johnson, Legislative Counsel).

Moreover, a stand-alone attribution method makes sense in the context of SB 408's treatment of affiliate tax liabilities *in total*. SB 408 refers repeatedly to the taxes paid to units of government by the affiliated group in total, not just affiliates with positive or negative tax liabilities. "Affiliated group" is defined in SB 408 as "an affiliated group of corporations of

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which the public utility is a member and that files a consolidated federal income tax return." SB 408 § 3(13)(a). Rather than permitting (or requiring) examination of individual members of the affiliated group, this definition permits examination of the whole entity only – that is, the group of corporations that files a consolidated return. By looking at the total group, the Commission is able to consider the ultimate issue: whether taxes paid to units of government by the utility or group in total are less than the taxes incurred as a result of income generated by the regulated operations of the utility. *See* SB 408 § 3(12).

Indeed, the legislative history also demonstrates that SB 408 does not require an automatic adjustment whenever *any* affiliate suffers a loss, but instead only when a utility's affiliated group paid less tax than the utility collected in rates. Representative Brian Boquist explained this point when he carried the bill on the House floor. *See* House Floor Session (July 30, 2005) (statement of Rep. Brian Boquist). Representative Boquist's statement was consistent with the analysis by Deputy Attorney General Peter Shepherd, which was distributed to each member of the House during the floor debate. *See* House Floor Letter (memorandum from Dep. Att'y Gen. Peter Shepherd to Rep. Tom Butler, July 30, 2005). There, Deputy Attorney General Shepherd analyzed the impact of SB 408 and provided an outline of the various scenarios that would cause rates to "rise," "stay the same," or "go down" under the Act. He concluded that rates would "stay the same" if the affiliated group paid more tax to government than the utility collected in rates. *Id.* at 1. He did not conclude that rates would "go down" if any member of the group suffered a loss. *Id.* Rather, he concluded that two things could cause rates to "go down" for a utility that is part of an affiliated group: (1) the utility had less tax expense on a stand-alone basis than it collected in rates,[6] or (2) "losses incurred by affiliated companies offset the tax liability in the return so

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[6] Deputy Attorney General Shepherd's analysis does not address the circumstances that would cause a utility's tax expense to decrease on a stand-alone basis nor the potential for mitigating the harmful effects of a rate reduction when a utility is already under-earning. As further reducing an under-earning utility's revenues raises clear constitutional and equity

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that the amount of tax received by the government is less than the amount allowed as estimated taxes [*i.e.,* in rates]." *Id.* at 2.

As demonstrated by Deputy Attorney General Shepherd's analysis, a stand-alone approach to attribution does not perpetuate the status quo. Instead, SB 408 requires rate adjustments when the taxes in rates exceed the lesser of the two measures of taxes paid defined in section 3(12). In this way, SB 408 creates an exception to the stand-alone attribution approach when affiliate losses *in total* result in the affiliated group's tax liability being less than the utility's stand-alone tax liability, such that the affiliated group's tax liability replaces the stand-alone tax liability as the utility's tax expense under the "lesser of" test. *See* SB 408 § 3(12).[7] Thus, when a utility collected more taxes in rates than its affiliated group paid to units of government,[8] SB 408 requires the Commission to direct the utility to establish an automatic adjustment clause to account for the difference. *See* SB 408 §§ 3(6), (12).

2. Stand-Alone Attribution Effectuates the Act's Stated Purpose of Aligning Amounts of Income Tax Collected in Rates with Taxes Actually Incurred and Paid by Utilities to Government Taxing Authorities.

Section 3(12) states that the attribution of "taxes paid" to the utility "may not exceed" the lesser of consolidated or stand-alone tax payments, demonstrating the legislature's intention that customers receive a rate adjustment when a utility collected tax in excess of the lesser of (a) its stand-alone tax expense or (b) the amount paid to government by the utility or

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issues, the Commission should carefully consider during this rulemaking proceeding whether the legislature actually intended for a utility with unexpectedly high costs or other events that cause the utility to under-earn (due to for example weather conditions or energy markets) to suffer further reductions in revenues through an SB 408 adjustment, and, if so, whether the Commission can or must put in place a regulatory mechanism to recover the extra costs.

[7] This approach to allocation of affiliate losses is sometimes referred to as a "*United Gas Pipe Line*" or "pour-over" approach to allocation of consolidated tax benefits. *See* discussion of *United Gas Pipe Line* at Section III.A.4.b, *infra.*

[8] "Taxes paid" is net of adjustments specified in SB 408, including deferred taxes, charitable contributions and non-recognized utility investments. SB 408 § 3(13)(f)(A)-(C).

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its affiliated group. In other words, SB 408 allows the utility to retain recovery in Oregon retail rates only for the lesser of these two amounts. In this way SB 408 effectuates the underlying policy of addressing the so-called "Enron problem" — by insuring that the affiliated group *in total* pays at least as much in tax as is embedded in Oregon rates.

a. The Stand-Alone Attribution Approach Solves the So-Called "Enron Problem" — That Is, It Results in a Rate Decrease When a Utility Collected More for Taxes Than Its Affiliated Group Paid to Units of Government.

To illustrate, take the examples provided in Staff's August 12, 2005 letter to Oregon utilities:[9]

	Utility A	Utility B	Utility C
Regulated Utility Operations (tax liability)	130	130	130
Affiliate X (tax liability)	130	65	-20
Affiliate Y (tax liability)	-60	-95	-60
Taxes Paid to Government	200	100	50

Pursuant to section 3(12)(a), the Commission would first ask what is the tax liability incurred as a result of income from regulated operations. For Utilities A, B, and C, that amount is $130. Then, pursuant to section 3(12)(b), the Commission would ask what is the amount of tax paid to units of government by the utility or its affiliated group. For Utility A, that amount is $200; for Utility B, it is $100; and for Utility C, it is $50. Thus, because the "taxes paid that are properly attributed to the regulated operations of the public utility may not exceed the lesser of" the section 3(12)(a) or (b) amounts, the taxes paid and properly attributed to each utility are as follows: for Utility A $130 (the lesser of (a) $130 and (b) $200); for Utility B $100 (the lesser of (a) $130 and (b) $100); and for Utility C $50 (the

[9] This example does not appear to address situations in which affiliates are regulated utilities or situations in which the Oregon regulated utility has a negative tax liability, both of which raise added layers of complexity. *See, e.g.,* discussion regarding regulated affiliates and normalization violations *supra* at 20-21.

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lesser of (a) $130 and (b) $50). Thus, Utility B would be subject to an automatic adjustment clause to refund to customers $30 and Utility C would be subject to an automatic adjustment clause to refund to customers $80.[10]

b. Loss-Allocation Approaches Base Tax Adjustments Solely on the Tax Liabilities of Individual Affiliates and the Corporate Organization of the Affiliated Group, Without Regard to the Taxes Incurred as a Result of Regulated Operations.

Consistent with the plain directives of SB 408, the stand-alone approach bases tax adjustments on whether taxes were incurred as a result of the regulated operations of the utility and paid to units of government. In contrast, whether a rate adjustment occurs under a loss-allocation approach such as the one adopted in the temporary rule, OAR 860-022-0039, may depend entirely on the tax liability of an individual affiliate or the corporate organization of the affiliated group. The arbitrary results produced by a loss-allocation approach can be illustrated by looking again to the examples provided by Staff.

Most notably, under a loss-allocation approach, the amount deemed to be paid and properly attributed to Utility A would not be $130 (the lesser of its stand-alone tax liability and the amount paid to government by its affiliated group); rather, the amount deemed to be paid and properly attributed to Utility A would be $100, because a loss-allocation approach requires the Commission to disregard Affiliate Y's negative tax liability and distribute the amount paid to units of government by the affiliated group among the members of the group with a positive tax liability (Utility A and Affiliate X). Thus, Utility A would be subject to an automatic adjustment clause to refund to customers $30.[11] This is despite the fact that the

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[10] This analysis assumes the amount of "tax authorized to be collected in rates" is the same as the utilities' stand-alone tax liability ($130 for all three utilities) and that the "taxes paid" figures are net of the adjustments required by SB 408.

[11] This analysis assumes the amount of "tax authorized to be collected in rates" is the same as the utility's stand-alone tax liability ($130) and that the "taxes paid" figures are net of the adjustments required by SB 408.

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amount of tax incurred by the utility as a result of income generated by its regulated operations was $130 and this amount was in fact paid by the affiliated group to units of government.

This result is particularly egregious and arbitrary in light of the fact that the utility incurred the full cost of its stand-alone tax liability. In other words, the utility generated tax income that "caused" this expense and this expense "caused" the affiliated group's payment to be higher by a corresponding amount. If the utility's tax liability had been less, the affiliated group's actual payment would have decreased by a corresponding amount. For example, if Utility A's stand-alone tax liability had been $120 ($10 less), the affiliated group would have paid to units of government $190 ($10 less). Likewise, if Utility A's stand-alone tax liability had been $0 ($130 less), the affiliated group would have paid to units of government $70 ($130 less). An approach that denies Utility A the opportunity to recover an incurred expense, which was actually paid to units of government, is contrary to SB 408 and a violation of Utility A's constitutional right to fair and symmetrical ratemaking and to rates that permit an opportunity to recover costs and earn a fair rate of return. *See FPV v. Hope Natural Gas Co.*, 320 US 591 (1944); ORS 756.040(1) (codifying *Hope* standard). Thus, adoption of a loss-allocation approach would reduce rates by allocating affiliate losses to the utility even when the utility incurred its full tax expense *and* the utility's consolidated group paid more taxes to government than the utility collected in rates. In this way, a loss-allocation approach would inevitably violate *Hope* and ORS 756.040.

When a statute is susceptible to more than one interpretation, and one is more consistent with the statute's constitutionality, the constitutional interpretation prevails. *Vorm v. David Douglas School Dist. No. 40*, 609 P2d 193, 195 (Or App 1980); *City of Portland v. Welch*, 364 P2d 1009, 1012 (Or 1961). Accordingly, the Commission is constrained by its statutory obligation under ORS 756.040 and the constitutional limits

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expressed in *Hope* from adopting a loss-allocation approach to the term "properly attributed."[12]

As further evidence of the arbitrary nature of this approach, a loss-allocation approach would also produce different results simply depending on the corporate organization of the utility's affiliated group. That is, whether a rate adjustment is required when a utility's affiliated group paid taxes in excess of the utility's stand-alone tax expense could depend entirely on whether the utility's affiliates were organized as separate companies or merged companies.

Taking the example of Utility A again, if Affiliate X and Affiliate Y were merged into one corporate entity, the amount of taxes paid and properly attributed to Utility A would be $130. However, if Affiliate X and Affiliate Y remain separate corporate entities, the amount of taxes paid and properly attributed to Utility A would be $100.

Thus, whether or not an adjustment occurs could depend entirely on whether the utility's affiliates were separate or merged companies, despite the fact that, under either scenario:

- Government units received the same amount in tax payments from the affiliated group;
- Utility A's cost-of-service, including its stand-alone tax expense, remained the same; and;
- The Affiliates' total tax expense remained the same.

[12] Although SB 408 *on its face* raises serious constitutional concerns, PacifiCorp and Avista do not intend to assert challenges to the statute's legality in this proceeding. Instead, PacifiCorp and Avista reserve their right under *England v. Louisiana Bd. of Med. Examiners*, 312 US 411, 84 S Ct 461, 11 L Ed 2d 440 (1964), to bring such challenges in an appropriate federal court.

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To illustrate:

			Effect if Affiliate X and Y Are Merged	
	Stand-Alone Tax Liability	Loss-Allocation "Properly Attributed" Amount	Stand-Alone Tax Liability	Loss-Allocation "Properly Attributed" Amount
Utility A	$130	$100	$130	$130
Aff. X	$130	$100	$70	$70
Aff. Y	($60)	$0		
Consolidated Tax Payment	$200	$200	$200	$200

Thus, if Affiliate X and Affiliate Y were merged into one corporate entity, Utility A would be allowed to retain recovery of $130. In contrast, if Affiliate X and Affiliate Y remain separate corporate entities, Utility A would be subject to an automatic adjustment clause to refund to customers $30.[13] This irrational outcome demonstrates the problematic nature of loss-allocation approaches.

3. A Stand-Alone Approach to the Term "Properly Attributed" Appropriately Limits the Commission's Review Function to the Taxes Paid by the Utility and Its Affiliated Group, Not Each of the Group's Members.

Additionally, unlike a loss-allocation approach, a stand-alone attribution approach would not require the Commission to review the tax returns of individual non-utility affiliates, but rather would require only that the Commission determine (a) the taxes paid and incurred by the stand-alone utility as a result of income generated by its regulated operations and (b) the total taxes paid to units of government by the utility's affiliated group. In contrast, a loss-allocation approach would require the Commission to review not only the

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[13] This analysis assumes the amount of "tax authorized to be collected in rates" is the same as the utility's stand-alone tax liability ($130) and that the "taxes paid" figures are net of the adjustments required by SB 408.

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consolidated tax liability of the entire affiliated group but also the individual stand-alone tax liabilities of each non-utility affiliate. The Commission also might be required to audit the tax information of each affiliate to determine whether the reported tax liabilities were accurate.[14] The tax information of nonregulated affiliates is highly sensitive business information that is protected from disclosure by federal law. *See* IRC § 6103(a) (no officer or employee of any state may disclose any tax return or return information provided to the IRS). Thus, a loss-allocation approach to properly attributed would place the Commission in the inappropriate position of reviewing non-jurisdictional entities' confidential and highly sensitive business information.

4. Had the Legislature Intended the Term "Properly Attributed" to be Code for a Specific Allocation Formula, It Would Have Said So.

"Properly attributed" is not defined in other Oregon statutes or tax law. Nor does anything in the Act or legislative history indicate a legislative intent that the "properly attributed" language in SB 408 be code for a specific allocation formula. To interpret the words "properly attributed" as code for a formula that required the Commission to disregard certain losses and base an allocation on the taxable income of individual affiliates with positive taxable income would run afoul of the "cardinal" rule of construction, which requires courts to construe statutes according to their terms. *See PGE*, 317 Or at 611; *see also Connecticut Nat'l Bank*, 503 US at 253-54.

Proponents of a loss-allocation approach such as the one adopted in the temporary rule may point to the models employed in other states, such as Pennsylvania, as a basis for interpreting "properly attributed" in this way. However, the mere fact that other jurisdictions adopt a particular approach does not change the fact that Oregon has not adopted that approach. Nothing in the Act or legislative history indicates that the Oregon legislature

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[14] As explained in Section III.A.5, *infra*, such a result would place the Commission outside of its regulatory jurisdiction.

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modeled SB 408 after existing law in another jurisdiction. Instead, the legislative history demonstrates that the Act's proponents believed that consolidated taxes are being considered in a number of states, but does not indicate any attempt to model SB 408 after the law of any particular state. *See* Statement by Sen. Rick Metsger, Senate Floor Debate on SB 408 (June 8, 2005) (listing seven jurisdictions that he believes use a consolidated approach).[15]

a. SB 408 Is Not Modeled After Pennsylvania.

The Pennsylvania approach was cited only twice in the entire legislative record relating to SB 171 and SB 408, and then only as a reference to one of several states that do not follow a stand-alone tax approach. *See id.*; Statement by Chair Sen. Ryan Deckert, Public Hearing on SB 171 before the Senate Revenue Committee (Apr. 14, 2005).[16] Indeed, when the Oregon legislators drafted, debated, and ultimately passed SB 408, they were aware that the Commission and the Oregon Department of Justice believed that the approach used in Pennsylvania was flawed. *See* Letter to Sen. Ryan Deckert, Chair Senate Revenue Committee, and Sen. Rick Metsger, Chair Senate Business and Economic Development Committee, from the Commission at p. 1 (attaching legal memorandum from Department of

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[15] Senator Metsger stated:

> "A couple of issues were brought about other states, and I wanted to talk a little bit about that. There are other states that take into account the taxes. Connecticut, this is from the Public Utility Commission in their white paper and their investigation. The study that was done. Connecticut, Florida, Indiana, Pennsylvania, Tennessee, Virginia and West Virginia, report that they do consider the savings from the consolidated returns and recognize those for the rate making purposes. Additionally, the Pennsylvania PUC, consistent with the state supreme court decisions, applies this same actual taxes paid standard by including a utility's share of federal taxes benefits when they do set the rates. Now, in Oregon, why do we have a situation in Oregon that's a little more difficult? Well, one of the major reasons is we're an income tax state."

[16] Chair Deckert stated: "Well, other states do, I mean, we've heard a lot about Pennsylvania, who does a true-up. We can get that, I mean, there are other states. I want to say 41 states have the consolidated form on their regulated utilities."

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Justice and noting that Commission had previously provided the committees with a copy of the Commission Staff's White Paper on the Treatment of Income Taxes in Utility Ratemaking (the "White Paper")). In that legal opinion, which the Commission brought to the legislature's attention, the Department of Justice analyzed Pennsylvania's approach, concluding:

> "The flaw with the Pennsylvania approach is not that it follows the actual taxes paid doctrine but that it patently fails to consider aligning the benefits and burdens of the consolidated tax structure. While I have concluded that this Commission could adopt an actual taxes paid doctrine to calculate tax expenses, it must do so in a rational, symmetrical way. This is why the Pennsylvania cases are incorrect – they do not even attempt to align the benefits and burdens of the tax treatment. In fact, the Pennsylvania approach does not look at all the consolidated companies in the parent's corporate family. It looks only at those who lost money in recent years. It ignores those that were profitable, except for the purpose of calculating the utility's share of tax savings from the losing companies."

Legal Memorandum to the Commission from Assistant Attorney General Jason Jones at 5 (Feb. 18, 2005) (footnote omitted); s*ee also* White Paper at 11-12 (Feb. 2005) (criticizing the Pennsylvania approach, stating that "[t]he Commission's counsel advises that those making a legal challenge to this approach will likely point to the lack of an economic rationale in attacking it"). Nowhere in the legislative history does anyone question or contradict the advice contained in these records.

The fact that Pennsylvania was not the Oregon legislature's model for SB 408 is also demonstrated by the many differences between the two states' approaches. Unlike SB 408, Pennsylvania's rule (a) is applied in general rate proceedings during which the parties and the Pennsylvania public utility commission have the opportunity to approve of an overall rate of return that is reasonable for both the customers and the utility; (b) is not based on statutory prescriptions; (c) does not apply to stand-alone utilities; (d) does not use an automatic adjustment clause; (e) does not true-up past taxes paid with past over- or under-collections;

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and (f) does not include statutory offsets for deferred taxes, unrecovered utility investments, and charitable deductions.

b. Nor Is SB 408 Modeled After Any Other Existing Law.

Nothing in the Act or legislative history indicates a legislative intent to model SB 408 after any other existing law. There is no uniformity in the approaches applied by the states that Senator Metsger identified. Some evaluate only the utility and its corporate parent's tax liabilities; others use methods that are not well explained in the applicable orders; Pennsylvania and West Virginia appear to allocate affiliate losses to utilities in the manner adopted in the temporary rule; and Connecticut appears to use the net-loss or stand-alone attribution approach described in SB 408. *See Re United Illuminating Co.*, 2002 WL 31720159 (Conn DPUC 2002). However, none of these states has a scheme that is entirely consistent with SB 408.

As in Connecticut, the Federal Energy Regulatory Commission's predecessor, the Federal Power Commission (the "FPC") used a net-loss allocation approach until 1972 that was similar to SB 408; this approach is often referred to as the *United Gas Pipe Line* approach. *See FPC v. United Gas Pipe Line*, 386 US 237, 87 S Ct 1003, 18 L Ed 2d 18 (1967) (FPC's approach was within FPC's statutory authority); *see also Florida Gas Transmission Company*, 47 FPC 341, 93 PUR 3d 477 (1972) (rejecting *United Gas Pipe Line* approach in favor of stand-alone approach).

The plain language of SB 408 is consistent with the allocation approach approved of in *United Gas Pipe Line*. There, affiliate losses were applied to reduce a utility's stand-alone tax expense only if such losses were not fully offset by affiliate gains. 386 US at 241; *see also Cities Service Gas Co.*, 30 FPC 158, 49 PUR 3d 229 (1963) (using approach). Under this approach, as intended by SB 408, affiliate losses are taken into account only if the consolidated tax liability is less than the utility's stand-alone tax liability. *See El Paso Natural Gas Co.*, 46 FPC 454, 90 PUR 3d 462 (1971) (applying *United Gas Pipe Line*

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approach, but making no consolidated tax adjustment, because there was no net loss to be applied to the regulated company's income).

c. Thus, an Approach That Allocates Affiliate Tax Losses to a Utility When the Affiliated Group Pays More Tax Than the Utility's Stand-Alone Tax Liability Is Not Within the Legislative Delegation of Authority.

Rules implementing a statute must be within the legislative delegation of authority and reasonably calculated to accomplish the legislative purpose. *Pacific Northwest Bell Telephone Co. v. Davis*, 43 Or App 999, 1005, 608 P2d 547 (1979) (citing *Crouse v. Workmen's Comp. Bd.*, 26 Or App 849, 852, 554 P2d 568 (1976)). Here, except when the section 3(12) cap is implicated, the Act does not authorize the Commission to allocate affiliate tax losses to the utility. Thus, the loss-allocation approach adopted in the temporary rule is wrong in its treatment of affiliate tax losses and is not in conformance with SB 408.

5. A Stand-Alone Approach to the Term "Properly Attributed" Limits Unintended Consequences.

Approaches that allocate affiliate losses to utilities, even when the affiliated group paid more tax than the utility collected in rates, implicate significant, negative unintended consequences. For example, under a loss-allocation approach, the Commission would be required to audit the stand-alone tax liability of each affiliate of the utility, ultimately expanding the purview of the Commission's regulatory oversight to non-jurisdictional entities. Thus a loss-allocation approach would place the Commission in the business of investigating affiliate and parent tax issues and the reasonableness of their business decisions, an area outside of its regulatory jurisdiction.[17]

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[17] Information that is solely within the control of a utility's unregulated parent, subsidiary, or affiliate is outside the scope of the Commission's investigative powers, which are limited to regulated utilities within the Commission's jurisdiction. *See* ORS 756.070-.125 (Commission has authority to investigate management of "public utilities"); ORS § 757.005 (defining "public utility"). SB 408 does not expand these powers.

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This is especially problematic with respect to *utility* operations in other jurisdictions. SB 408 did not intend to capture tax benefits or losses of utility operations in other jurisdictions and assign those tax benefits to Oregon regulated utility operations. There is no mention in SB 408 of utility operations in jurisdictions other than Oregon. Indeed, if SB 408 treats utility operations in another jurisdiction the same as non-utility affiliates by apportioning a tax benefit from a utility operation in another jurisdiction to determine tax payment amounts attributed to Oregon utility operations, the result will likely be a violation of the normalization rules of the Internal Revenue Code (the "IRC").[18] A violation of the normalization rules would cause potentially extreme rate increases.[19] Indeed, the legislature recognized expressly the need to protect customers from such an outcome. *See* SB 408 §§ 3(8), 3(13)(f)(C).

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[18] Under the normalization rules, the investment tax credit and accelerated depreciation are available to companies that operate utilities only if they follow the normalization method of accounting. In order to use a normalization method of accounting, the utility must treat assets consistently in ratemaking and tax accounting. IRC § 168(i)(9); *see* Priv Ltr Rul 2004-18-001 (Apr. 30, 2004) (utility's maintenance of an accumulated deferred federal income tax reserve associated with property that was excluded from the utility's regulated books of account would violate the consistency requirement of section 168(i)(9)(B) and the normalization rules, because the utility's rate base, tax expense, and depreciation expense for ratemaking purposes would be determined without the cost of the excluded property). If SB 408 causes the deferred taxes of an out-of-state utility to be flowed through to ratepayers in Oregon, that utility property will be treated inconsistently in ratemaking and tax accounting — thereby violating the normalization rules.

[19] The consequence of violating the IRC normalization requirements is severe: the utility (or filing entity) would lose the right to claim accelerated depreciation on its federal tax returns. IRC § 168(f) (depreciation deduction determined under section 168 shall not apply to any public utility property if the taxpayer does not use a normalization method of accounting). This consequence may be permanent with respect to any utility property existing at the time of the violation. *See id.* The loss of accelerated depreciation would probably cause decreased investment in utilities and their affiliates, decreased diversification of utilities, and increased rates and prices in all jurisdictions in which the affected utilities and affiliates do business. *See* White Paper at 9 (identifying annual rate impact of the loss of normalization on Oregon customers of Portland General Electric and PacifiCorp as between $20 and $30 million).

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B. Investments/Credits – What Did the Legislature Intend in Adoption of Section 3(13)(f)(B)?

Response: In adopting Section 3(13)(f)(B), the legislature intended to avoid confiscation of tax savings associated with unrecognized utility investments by providing for an adjustment to "taxes paid" for tax savings arising from expenditures in regulated operations of the utility that were not taken into account in ratemaking.

1. Section 3(13)(f)(B) Provides for an Adjustment to "Taxes Paid" for Tax Savings Arising from Unrecognized Expenditures in the Regulated Operations of the Utility.

According to the relevant sections of SB 408:

> "(f) 'Taxes paid' means amounts received by units of government from the utility or from the affiliated group of which the utility is a member, whichever is applicable, adjusted as follows:
>
> * * * * *
>
> "(B) Increased by the amount of tax savings realized as a result of tax credits associated with investment by the utility in the regulated operations of the utility, to the extent the expenditures giving rise to the tax credits and tax savings resulting from the tax credits have not been taken into account by the commission in the utility's last general ratemaking proceeding[.]"

On its face, section 3(13)(f)(B) lacks a plain meaning with respect to utility expenditures and investments.[20] It is only in the context of the Act's underlying policies and traditional ratemaking principles that the section's meaning becomes clear.[21] In that context, section 3(13)(f)(B) provides for an adjustment to "taxes paid" for tax savings arising from

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[20] The statute is clear that tax savings incurred as a result of affiliate activities do not serve to increase the amount of taxes paid.

[21] In determining legislative intent, it is proper for a court to consider the policy and purpose of a statute, and to consider in that connection whether or not such policy will be attained by a literal interpretation of the language used. *State v. Buck*, 262 P2d 495, 497 (Or 1953) (citing *Swift & Co. v. Peterson*, 233 P2d 216, 223 (Or 1951)).

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any expenditure in the regulated operations of a utility that was not taken into account in ratemaking. Thus, SB 408 allows utility investors to retain the tax benefits of, for example, Business Energy Tax Credits ("BETCs") that utilities purchase when the cost of such purchases are not included in rates. Likewise, SB 408 allows utility investors to retain tax benefits of other expenditures in regulated utility operations that were not taken into account in ratemaking. Such an interpretation is consistent with traditional cost-causation principles and the requirement to match "benefits and burdens," which the Department of Justice has advised is a legal standard for ratemaking in this context.

2. This Interpretation Is Supported by the Text of SB 408.

Although at first glance the text of section 3(13)(f)(B) is confusing, upon a close reading of the section, it appears that the legislature intended "tax credits" to mean any tax item that gives rise to a tax savings.[22] The Act provides that "taxes paid" are "[i]ncreased by the amount of tax savings realized as a result of tax credits" to the extent that "tax savings resulting from the tax credits have not been taken into account" for ratemaking purposes. SB 408 § 3(13)(f)(B). To give meaning to this provision, the Commission should reject any interpretation of "tax credits" that fails to give effect to both phrases. *See Murphy v. Nilsen*, 527 P2d 736, 739 (Or App 1974) (citing *Blyth & Co. v. City of Portland*, 282 P2d 363 (Or 1955) (statutes should be interpreted to give effect to every section, clause, phrase or word). The only interpretation that gives effect to both phrases is one that recognizes that the drafters intended "tax credits" to mean anything that gives rise to tax savings. In other words, the term "tax credits" includes not only items that are themselves tax savings, but also items that, when applied, produce tax savings (*i.e.,* deductions).

[22] The legislative record does not explain the intent of this provision. Although the record contains a number of references to "tax credit" and "investments," none of these references address these terms as they are used in section 3(13)(f)(B).

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3. This Interpretation Is Consistent with State of Oregon and Commission Policies Encouraging Energy Conservation and Investment in Utility Infrastructure.

This interpretation is consistent with state of Oregon and Commission policies encouraging energy conservation and investment in utility infrastructure. Indeed, any other interpretation of section 3(13)(f)(B) would eliminate the economic incentive for utility investors to make such investments. Lawmakers frequently use tax credits *and other tax benefits* to encourage investment in activities such as development of renewable resources. *See, e.g.,* ORS 469.190 (BETCs encourage use of renewable resources); Oregon Department of Energy, Oregon Renewable Energy Action Plan at 1 (2004) (*available at* http://egov.oregon.gov/ ENERGY/RENEW/docs/FinalREAP.pdf) ("We can make Oregon the national leader in renewable energy and renewable product manufacturing. .... Development of renewable energy will lessen our reliance on fossil fuels, protect Oregon's clean air and create jobs.") *quoting* Governor Kulongoski (2003)); Energy Policy Act of 2005, Title XV, "Energy Policy Tax Incentives Act," HR 6, 109th Cong (2005) (enacted) (encouraging investment in utility infrastructure).[23] Any approach that limits the effectiveness of these tax benefits or otherwise discourages investment in renewable energy and utility infrastructure would be contrary to state and federal energy policy. *See Re Nat'l Rates for Natural Gas*, 4 PUR 4th 401 (Fed. Power Comm'n 1974) ("'[T]o reduce the rates of a regulated pipeline because of . . . [tax losses resulting from] affiliated exploration and

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[23] *See also* White House Press Release (*available at* www.whitehouse.gov/news/releases/2005/08/print/20050808-4.html), which states:

> "The energy bill will help modernize our aging energy infrastructure to help reduce the risk of large-scale blackouts and minimize transmission bottlenecks. This will be accomplished by repealing outdated rules that discourage investment in new infrastructure, offering tax incentives for new transmission construction, and by encouraging the development of new technologies, such as superconducting power lines, to make the grid more efficient."

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development activities would be discouraging to the very enterprise we now want to encourage.'" (citation omitted)).

Allocating the tax benefits of participation in these ventures to entities that do not take the risk of investment would decrease or eliminate the economic value of these tax incentives. Thus, if "tax credits" in section 3(13)(f)(B) is interpreted narrowly to mean tax credits as defined by the IRC, SB 408 will discourage utility investors from investing in renewable energy and utility infrastructure and would therefore be contrary to state and federal energy policy. When utility investors bear the risk of such investments (*i.e.,* the costs are not included in rates), state and federal policy directs that they should receive the benefit.

Consistent with the interpretation of section 3(13)(f)(B) outlined above, in advocating for SB 408's passage, the Citizens' Utility Board of Oregon and Industrial Customers of Northwest Utilities assured legislators that section 3(13)(f)(B) broadly preserved tax benefits associated with renewable energy investment:

> "*The utilities say, 'The bill undermines Oregon's renewable energy industry.'*
>
> "**RESPONSE: Tax credits and tax incentives that exist today will exist after the bill's passage.**
>
> "Again, the bill changes nothing in utility ratemaking or tax policy. If a utility wishes to avail themselves of tax credits and incentives, customers can support that. The bill discourages nothing. In fact, Section 3[13](f)(B) allows the amount of taxes paid to be '**(i)ncreased by the amount of tax savings realized as a result of tax credits associated with investment by the utility in the regulated operations of the utility, to the extent the expenditures giving rise to the tax credits and tax savings resulting from the tax credits have not been taken into account by the commission in the utility's last general ratemaking proceeding.**' This means that the utility can take into account any tax credits or incentives when reporting its taxes paid, as long as those credits were not already accounted for in a previous rate case."

See Utility Customers Ask for Fairness and Equity: Taxes Collected Must Align with Taxes Paid; Vote Yes on SB 408-C (emphases in original), attached hereto as Exhibit B.

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C. "Material Adverse Effect" — May the Commission Terminate the Automatic Adjustment Clause upon [a] Showing by a Utility that the Automatic Adjustment Clause Has a Material Adverse Effect on the Utility?

Response: Pursuant to its duty to set rates that are fair, just and reasonable, the Commission must terminate any automatic adjustment clause that causes rates to be so low as to materially adversely affect the utility.

Section 5(1)(a) contains a downward limit on rate adjustments in that it prohibits the Commission from authorizing a rate or schedule of rates that is not "fair, just and reasonable." SB 408 § 5(1)(a). Conversely, section 3(9) contains an upward limit in that it requires the Commission to terminate any automatic adjustment clause that the Commission determines "would have a material adverse effect on customers of the public utility." SB 408 § 3(9). Accordingly, the Commission must terminate any automatic adjustment clause that would result in unreasonably high or low rates.

1. "Fair, Just and Reasonable" Provides a Downward Limit on Rate Adjustments.

SB 408 does not define the term "fair, just and reasonable." The terms "fair" and "just" are commonly defined as having interchangeable meanings; *e.g.,* "fair" is defined in part as "just," and "just" is defined in part as "fair." *See Webster's New World Dictionary* (4th ed 2001) (defining the term "fair" as "just and honest; impartial; unprejudiced; according to the rules;" defining the term "just" as "right or fair; equitable; impartial; well-founded; reasonable;" defining the term "reasonable" as "using or showing reason, or sound judgment, sensible; not extreme, immoderate, or excessive.").

This interchangeable meaning is consistent with usage of the terms in related statutes. As with ORS 757.210, as amended by SB 408, these statutes declare that the Commission must set fair, just, and reasonable utility rates — using the terms "fair" and "just" interchangeably. *See, e.g.,* ORS 756.040(1) (codifying the *Hope* standard by requiring the Commission to "balance the interests of the utility investor and consumer in establishing fair

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and reasonable rates"); ORS 757.273 ("All rates * * * by any public utility or telecommunications utility for any attachment by a licensee shall be just, fair and reasonable."); ORS 757.285 ("Agreements regarding rates * * * [for] attachments shall be deemed to be just, fair and reasonable, unless the Public Utility Commission finds * * * that such rates * * * are adverse to the public interest and fail to comply with the provisions hereof."); ORS 757.495 (Commission must find certain contracts to be "fair and reasonable").

As the Court explained in *Hope*, the requirement that rates be fair, just, and reasonable does not define a method by which rates are to be calculated; instead, the fixing of fair, just, and reasonable rates involves a balancing of investor and consumer interests. *Fed. Power Comm'n v. Hope Natural Gas Co.*, 320 US 591, 603 (1944). Subsequently, the *Hope* Court's explanation of the standard was incorporated almost verbatim in ORS 756.040(1). *See Hope*, 320 US at 603-04. ORS 756.040(1) defines the term "fair and reasonable" as follows:

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

Thus, the text and context of SB 408 indicate that by using the term "fair, just and reasonable," the Oregon legislature intended to prohibit the Commission from adjusting rates in a manner that fails to provide adequate revenue for operating expenses, capital costs, and a return on investment commensurate with other similar enterprises and sufficient to maintain the utility's financial integrity.

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Given the plain, ordinary meaning of the term "fair, just and reasonable," which is apparent from the text and context of SB 408, under the *PGE* framework, the analysis would be at an end. *PGE*, 859 P2d at 1146. Nevertheless, even if this term was adjudged to be ambiguous, this same interpretation is also fully supported by the legislative record. On numerous occasions, the Department of Justice advised the legislature that the law must allow the Commission to set rates that are "fair"; otherwise, the law could result in an unconstitutional taking of private property under *Hope*. *See, e.g.,* Statement of Deputy Attorney General Peter Shepherd, Senate Bill 408 Public Hearing, House State and Federal Affairs Committee (June 30, 2005) ("[R]ate setters must allow investors in a regulated utility to recover their prudent expenses and earn a fair return on their investment. This is, you'll hear people refer to this as the *Hope* Test[.]"); Statement of Assistant Attorney General Paul Graham, SB 408 Work Session, House State and Federal Affairs Committee (July 15, 2005) ("[*Hope* is] the case that prohibits contriscatory [sic] rates and what the *Hope* case says is that a regulator can use any method it wants to set rates, but at the end of the day, the bottom line, has to be that the rates allow the utility * * * a reasonable opportunity to earn a fair return on the investment it's made to serve rate payers.").

Thus, as the Department of Justice explained, the inclusion of the "fair, just and reasonable" language in ORS 757.210 sets a "downward limitation" on the adjustment that the Commission can make under the Act. Statement of Peter Shepherd, SB 408 Work Session, House State and Federal Affairs Committee (July 15, 2005) ("[The] PUC cannot allow the adjustment if it would result in a rate which is not fair, just and reasonable, as the terms of the total rate. So, that there would be an upward limitation, as well as a downward limitation."). *See also* Statement of Rep. Tom Butler, SB 408 Work Session, House State and Federal Affairs Committee (July 15, 2005) ("fair, just and reasonable" language "attempts to make [the adjustment] both symmetrical, as well as nonconfiscatory and in that regard completely constitutional"); Statement of Rep. Tom Butler, House Chamber Session

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(July 30, 2005) ("The bill's current proponents contend that the trigger to stop the downward spiral was that the rates must be fair, just and equitable—fair, just and reasonable."); Statement of Rep. Robert Ackerman, House Chamber Session (July 30, 2005) ("I conclude that the 'fair, just and reasonable' standard and the limited use of the automatic adjustment clause satisfies constitutional requirements. Now that is from our Legislative Counsel."). *See also* written Testimony of Deputy Attorney General Pete Shepherd, Work Session on SB 408, House State and Federal Affairs Committee (June 30, 2005) (describing "fair, just and reasonable" language as providing protection against *Hope* violation).

In any event, SB 408 must be interpreted in a way that is consistent with its constitutionality. *Vorm*, 609 P2d at 195 (courts are required to interpret statutes in a manner consistent with their constitutionality); *see also Welch*, 364 P2d at 1012 (the court is "bound to uphold the constitutionality of legislation when it is possible to do so"); *Easton v. Hurita*, 625 P2d 1290, 1292 (Or 1981) (statutes that are "somewhat ambiguous" must be interpreted so as to avoid "any serious constitutional problems"). Given that *Hope* is a constitutional standard, it is necessary for the Commission to interpret SB 408 in a manner that provides a downward limit on rate adjustments. Consequently, the Commission must terminate any automatic adjustment clause that causes rates to be so low as to materially adversely affect the utility — *i.e.,* rates that fail to provide adequate revenue for operating expenses, capital costs, and a return on investment commensurate with other similar enterprises and sufficient to maintain the utility's financial integrity.

2. "Material Adverse Effect" Provides an Upward Limit on Rate Adjustments.

The legislature did not define the term "material adverse effect" within SB 408, preferring instead to leave the determination to the Commission's discretion. *See* Colloquy between Dexter Johnson, Chair Sen. Rick Metsger, and Sen. Vicki Walker, Senate Business and Economic Development Committee, Senate Bill 408 Work Session (May 31, 2005)

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("There was concern that that definition was too inflexible and so that definition has been omitted and in its place is a restriction on the [Committee] that they may not make the material adverse effect finding and therefore not impose an automatic adjustment clause unless they conduct a hearing as part of that determination that would allow rate payer advocates and utilities to in an adversarial context argue whether or not there is in fact a material adverse effect."); Sen. Vicki Walker (proponent of bill), Senate Chamber Debate On Senate Bill 408 (June 8, 2005) ("Colleagues, then the material adverse affect clause will be defined in a public hearing process so that everyone has input on what that actually means."). It is clear from the legislative record, however, that an extreme upward rate adjustment would constitute a material adverse effect on customers. *See* Sen. Roger Beyer, Senate Chamber Debate on SB 408 (June 8, 2005) ("if the PUC determines that material adverse effect on customers would be too great, they may not require the utility to raise their rates."); Statement of Peter Shepherd, SB 408 Work Session, House State and Federal Affairs Committee (July 15, 2005) ("[The] PUC cannot allow the adjustment if it would result in a rate which is not fair, just and reasonable, as the terms of the total rate. So, that there would be an upward limitation, as well as a downward limitation.").

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D. Estimated Taxes — If a Utility Pays Quarterly Estimated Taxes, Must the Automatic Adjustment Clause be Applied Quarterly, or Does the Law Allow It to be Applied Yearly?[24]

> Response: SB 408 requires annual review and application of automatic adjustment clauses based on actual taxes paid. Consequently, regardless of whether a utility or its affiliated group files quarterly estimated taxes, the law does not permit the automatic adjustment clause to be applied quarterly.

1. The Text and Context of SB 408, and its Legislative History, Demonstrate That Adjustments Cannot Be Based on Quarterly Estimated Payments.

a. The Act Bases Adjustments on Actual Taxes, Not Estimates.

As posed, the question assumes, incorrectly, that the filing of quarterly estimated taxes constitutes "taxes paid" under SB 408. However, the Act requires rate adjustments to be based on actual taxes "incurred" (section 12(a)) and "paid to units of government" (section 12(b)). Taxes submitted with quarterly estimated tax filings are not taxes incurred and paid, but are indeed based on the taxpayer's estimated taxes, which may or may not reflect that taxpayer's ultimate tax liability. For example, a taxpayer may submit estimated taxes in a year in which it turns out not to have any taxes "incurred" and "paid."

Moreover, the concept of applying an automatic adjustment clause based on the amount of estimated quarterly taxes is inconsistent with the definition of "taxes paid" in

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[24] Stated in its entirety, the fourth issue that Administrative Law Judge Logan designated for early resolution is:

> "Section 3 of SB 408 requires the Commission to establish an automatic adjustment clause within 30 days (or later date, established by rule, not to exceed 60 days) once a determination is made regarding the $100,000 trigger amount. Section 4 states that if an automatic adjustment clause is established, it applies only to taxes paid to units of government and collected from ratepayers on or after January 1, 2006. If a utility pays quarterly estimated taxes, must the automatic adjustment clause be applied quarterly, or does the law allow it to be applied yearly?"

ALJ Logan Memorandum at 1.

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SB 408, which adjusts the amount received by government to account for deferred taxes, charitable contributions, and utility investments not included in rates. Until this information is reported in the October 15 tax report, the Commission lacks sufficient information to determine "taxes paid." The Commission simply cannot know the amount of taxes "incurred" and "paid" until after the annual tax reports are filed. SB 408 § 3(1).

b. The Act Requires Annual, Not Quarterly, Reporting and Adjustments.

Nothing in SB 408 refers to or supports the use of a quarterly adjustment. The first step of the *PGE* analysis, looking at the text and context of the statute, provides the answer to the Commission's question: a quarterly review of taxes paid is not allowed. The Act does not contain *any* mention of a quarterly review. On the other hand, annual reporting is expressly required. SB 408 § 3(1). The annual report must contain data for the previous fiscal "year," not "quarter." *Id.* Moreover, the Act expressly provides for the continuation of automatic adjustment clauses on an annual basis:

> "If an adjustment to rates is made under an automatic adjustment clause established under this section, the automatic adjustment clause shall remain in effect for each successive *year* after an adjustment is made and until an order terminating the automatic adjustment clause is made under subsection (9) of this section."

SB 408 § 3(5) (emphasis added). If the legislature had intended to allow quarterly reviews, it could have easily done so, instead of requiring that the automatic adjustment clause remain in effect on an annual basis after an adjustment is made. The Commission should follow the cardinal rule and "presume that a legislature says in a statute what it means and means in a statute what is says there." *Connecticut Nat'l Bank*, 503 US at 253-54. Consideration of taxes on a quarterly basis would be inconsistent with this provision of the Act, which supports only an annual review and application of automatic adjustment clauses.

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2. As a Practical Matter, Quarterly Adjustments Would Be Onerous and Could Result in Unnecessary Rate Volatility.

Quarterly adjustments could result in rate volatility even when, on an annual basis, little or no adjustment is warranted. Commitment of the Commission's, utilities' and other parties' resources to such an unnecessary, time-consuming, and costly exercise is unwarranted. Thus, even if the Commission were to determine that it could utilize quarterly reviews, notwithstanding the express provisions and legislative history to the contrary, the Commission, as a matter of policy, should decline to adopt such an approach.

Moreover, the participants in this docket have agreed that, whether or not the Act allows the Commission to use forecasted data, as a policy matter the Commission should base SB 408 adjustments on historic data only. *See* Letter from Paul Graham, Assistant Attorney General, to Participants in Docket AR 499 at 1-2 (Oct. 7, 2005) (summarizing agreements of participants). The use of estimated quarterly taxes would give the Commission an incomplete and inaccurate picture of the taxes actually paid to units of government.

IV. CONCLUSION

PacifiCorp and Avista urge adoption of the statutory interpretation of SB 408 outlined above.[25] These interpretations give effect to the legislature's intent, as expressed in the text of the statute and in the legislative history.

[25] As explained at footnote 13, *supra*, PacifiCorp and Avista reserve their right under *England v. Louisiana Bd. of Med. Examiners*, 312 US 411, 84 S Ct 461, 11 L Ed 2d 440 (1964), to bring challenges to the legality of the statute itself, including constitutional challenges, in an appropriate federal court.

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DATED: October 28, 2005.

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AVISTA CORPORATION

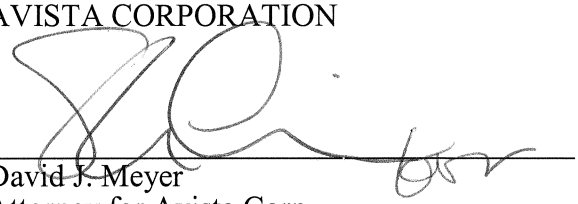

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EXHIBIT A

HARDY MYERS
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PETER D. SHEPHERD
Deputy Attorney General

DEPARTMENT OF JUSTICE
GENERAL COUNSEL DIVISION

October 7, 2005

Dear participants to AR 499:

I am in receipt of the AR 499 order, and I have two sets of comments about it.

My **first comment** is about two legal questions that we discussed that are not covered by the order. ALJ Kathryn Logan did not include these questions because, at this point, there is no dispute about them. The two questions are:

1. May the Commission use forecast data for the automatic adjustment clause?; and

2. Can the tax adjustment result in either a rate increase or decrease?

With respect to the first question, I do not recall an agreement as to whether the Commission has legal authority to use forecast data. Some may say it can; others may disagree. I thought the agreement among those who attended the September 28 workshop was that, whether or not the PUC has authority to use forecast data, it should use only historic data. In other words, the agreement was not about the law; it was about the policy the Commission should follow.

As for the second question, it is possible that we may have different ideas as to how SB 408 may result in either a rate increase or decrease, but I recall that we all agreed that it could. In other words, unlike the first question, we based our agreement on the law.

If my recollections are correct, then ALJ Logan's order covers all of the necessary legal issues. I believe her order is correct, but I would like to know if anyone disagrees.

My **second comment** is about the areas of agreement we reached at the September 28 workshop. There were two that I think we should memorialize:

1. The October 2005 and 2006 reports are for the sole purpose of determining whether there is a trigger for the automatic adjustment clause, not to support a rate change; and

2. The Commission may use historic data for the automatic adjustment clause.

If my first comment regarding the two legal questions is correct, then I suggest we can add two more statements to the areas of agreement, which I am numbering as 3 and 4:

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EXHIBIT A

3. Even if the Commission may use forecast data for the automatic adjustment clause, it should, as a matter of policy, use only historic data; and

4. A tax adjustment may result in either a rate increase or rate decrease.

Because these areas of agreement indicate which SB 408 issues need to be briefed and which do not, it is important that the record be clear as to the agreements.

Please let me know whether you agree with me that the three legal issues in ALJ Logan's order are all we need to brief. Also, please provide any comments you may have about the way I have characterized our agreements. If we concur on the areas of agreements, I will file them on behalf of the participants.

I request your responses on or before October 19.

Sincerely,

/s/Paul A. Graham
Paul A. Graham
Attorney-in-Charge
Regulated Utility & Business Section

cc: ALJ Kathryn Logan

PAG:nal/GENO0392

EXHIBIT B

INDUSTRIAL CUSTOMERS OF NORTHWEST UTILITIES

UTILITY CUSTOMERS ASK FOR FAIRNESS AND EQUITY: TAXES COLLECTED MUST ALIGN WITH TAXES PAID VOTE YES ON SB 408-C

Customers have crafted a bill that ensures that taxes collected through our rates are actually paid. However, there have been serious misrepresentations about SB 408-C. Yet the effect of the bill is very straightforward: utilities will have to report how much they collected in taxes and they will have to report how much they paid in taxes. If there's a difference between the two amounts of more than $100,000, there will have to be a true up. That's it. Nothing in utility ratemaking is changed. Nothing in tax policy is changed.

Let's look at the misrepresentations one by one.

The utilities say, "The bill is 'constitutionally unsound.' "
RESPONSE: SB 408-C does not violate either the state or the US Constitution.

The bill does not switch between methodologies. In fact, it picks a method and applies it consistently. Regulators have tremendous discretion in determining rates and how to calculate charges, including taxes, within those rates. All that is required is a rational explanation. "Taxes collected equals taxes paid" is a rational explanation. Is it a change from the current practice? Yes. But that's the point.

Neither would the bill result in confiscatory rates. This would mean that somehow the utility would be prevented from making its regulated rate of return. This is patently absurd. Having a utility report how much they collect in taxes, having them report how much they paid in taxes and making sure those two amounts are closely aligned does not result in confiscatory rates. It results in better accountability.

The utilities are fond of quoting *Hope Natural Gas v. Federal Power Commission*, saying that utility investors must have an opportunity to earn a fair and reasonable return on their investment. Customers have no quarrel with that premise. But making sure that taxes collected in rates are actually paid does not prevent that opportunity in any way. Investors should not be able to increase their profit margins by simply keeping taxes collected in rates.

The utilities say, "The bill undermines Oregon's renewable energy industry."
RESPONSE: Tax credits and tax incentives that exist today will exist after the bill's passage.

Again, the bill changes nothing in utility ratemaking or tax policy. If a utility wishes to avail themselves of tax credits and incentives, customers can support that. The bill discourages nothing. In fact, Section 3(f)(B) allows the amount of taxes paid to be "**(i)ncreased by the amount of tax savings realized as a result of tax credits associated with investment by the utility in the regulated operations of the utility, to the extent the expenditures giving rise to the tax credits and tax savings resulting from the tax credits have not been taken into account by the commission in the utility's last general ratemaking proceeding.**" This means that the utility can take into account any tax credits or incentives when reporting its taxes paid, as long as those credits were not already accounted for in a previous rate case.

-over-

EXHIBIT B

The utilities say, "The bill discourages charitable contributions and economic development."
RESPONSE: Even the utilities admit utility charitable contributions are exempt from adjustment in SB 408-C. And they don't explain how their dire predictions will come to pass.

But the utilities keep bringing up contributions and business activities of affiliates. If a utilities is part of a larger corporate structure or has other subsidiaries, it can still file consolidated tax returns if that is the wish of the utility or its corporate parent. However, for taxes collected in rates, SB 408-C asks only that the utility report the amount it collected for taxes in its rates, based on activities "properly attributed to the utility," and how much was actually paid to governmental entities. If there is a difference – either up or down – then there needs to be a true up. There is nothing in the bill that prevents a utility's corporate parent from investing in job creation, business development or making charitable contributions. But ratepayers should no longer pay for those activities by allowing unpaid taxes to be a slush fund for either utility investors or a utility's corporate parent.

The utilities say, "The bill is an extreme reaction to the Enron bankruptcy."
RESPONSE: The bill is a moderate approach to addressing a serious ratepayer concern.

The bill could have attempted to have the utilities to repay the hundreds of millions of dollars in collected taxes that were never paid to government entities to customers. The bill could have fundamentally changed tax policy or ratemaking. The bill could have done many things that could be labeled extreme. But SB 408-C is very moderate in its approach and is not a reaction to the Enron bankruptcy, although customers do not want that situation to occur again. The Enron bankruptcy simply brought the problem to light. It is fundamentally unfair for utilities – any utility – to keep money that customers paid as part of their rates, understanding that money will be paid to government. Rather than undertake a radical approach to the problem, all customers want is to know how much is collected for taxes in rates, how much is actually paid and to make sure those numbers are closely aligned. And that's all SB 408-C does.

SB 408-C is fair.
SB 408-C is moderate.
SB 408-C is straightforward.
SB 408-C is what customers are requesting.

Please Vote Yes on SB 408-C.

For more information, please contact: *Mark Nelson, ICNU: 503-363-7084*
Jeff Bissonnette, CUB: 503-516-1636

CERTIFICATE OF SERVICE

I hereby certify that I served a true and correct copy of the foregoing document in Docket AR 499 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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