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**Inara K. Scott**  
Assistant General Counsel

April 24, 2006

***Via Electronic Filing and U.S. Mail***

Oregon Public Utility Commission  
Attention: Filing Center  
PO Box 2148  
Salem OR 97308-2148

Re: In the Matter of the Adoption of Permanent Rules to Implement SB 408,  
Relating to Matching Utility Taxes Paid with Taxes Collected  
OPUC Docket No. AR 499  
**Revised Straw Proposals of PGE**

Attention Filing Center:

Enclosed for filing in the above-captioned docket is a letter to Administrative Law Judge Logan with Portland General Electric's Revised Straw Proposals. This document is being filed by electronic mail with the Filing Center.

An extra copy of this cover letter is enclosed. Please date stamp the extra copy and return it to me in the envelope provided.

Thank you in advance for your assistance.

Sincerely,

/s/ INARA K. SCOTT  
Inara K. Scott

cc: AR 499 Service List

Enclosure

## **CERTIFICATE OF SERVICE**

I hereby certify that I have this day caused the foregoing LETTER TO ALJ LOGAN AND REVISED STRAW PROPOSALS OF PORTLAND GENERAL ELECTRIC COMPANY to be served by First Class US Mail, postage prepaid and properly addressed, and by electronic mail, upon each party on the attached service list.

Dated at Portland, Oregon, this 24<sup>th</sup> day of April, 2006.

/s/ INARA K. SCOTT

Inara K. Scott

AR 499  
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Kathryn A. Logan  
Administrative Law Judge  
Oregon Public Utility Commission  
PO Box 2148  
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Re: In the Matter of the Adoption of Permanent Rules to Implement SB 408,  
Relating to Matching Utility Taxes Paid with Taxes Collected  
OPUC Docket No. AR 499  
**Revised Straw Proposals of Portland General Electric Company**

Dear Judge Logan:

Enclosed are PGE's revised straw proposals addressing the topics of expenses between rate cases and the earnings test. The first proposal provides a means for considering the utility's actual financial results while calculating an adjustment under the automatic adjustment clause. This proposal is simple and verifiable, and addresses the unintended consequences of an increased volatility in rates that will otherwise follow from the implementation of SB 408. This proposal is also necessary to minimize the significant impact SB 408 will have on a stand-alone utility such as PGE, an impact legislators did not consider or intend when they passed SB 408.

PGE's second proposal addresses another area of serious concern – the proper treatment of disallowed expenses, non-utility expenses, and expenses that have not been included in rates. Even if PGE's first proposal is adopted, this second proposal is necessary to capture these expenses, which clearly were not included in the utility's last rate case. The tax impact of these expenses cannot fairly be considered to have been included in a forecast of taxes derived from the utility's last rate case, and the Commission is well within its authority to use a mechanism such as a deferral to ensure that SB 408 does not impute the tax consequences of these expenses to customers.

PGE's third proposal is an earnings test to be included in the automatic adjustment clause. Once again, PGE believes this proposal is necessary even if the Commission approves the other two proposals. The Commission has a responsibility and statutory mandate to only set

ALJ Kathryn A. Logan

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rates that are fair, just and reasonable. ORS 756.040; 757.210. Without an earnings review at the time a rate adjustment is calculated, the Commission cannot be assured that the rate that will go into effect comports with these basic statutory standards.

Sincerely,

/s/ INARA K. SCOTT

Inara K. Scott

IKS:am

cc: AR 499 Service List



**PUBLIC UTILITY COMMISSION OF OREGON**

**Docket No. AR 499**

**REVISED STRAW PROPOSALS OF PORTLAND GENERAL ELECTRIC  
April 24, 2006**

**1. Calculating the amount of taxes charged to customers by actual net to gross ratios.**

**a. Proposed rule language:**

Taxes Charged for a given period is the product of multiplying the following three factors:

1. The revenues the utility collects from customers in Oregon, excluding any revenues from supplemental adjustments or other revenue amounts the Commission finds inappropriate for the calculation of Taxes Charged.

2. The utility's actual ratio of the net revenues from regulated operation of the utility to gross revenues from regulated operations of the utility, calculated by reference to the Company's FERC Form 1 data for that period.

3. The utility's actual effective tax rate, calculated by reference to the utility's FERC Form 1 data for that period.

**b. Related sections of bill:** 3(6) (automatic adjustment clause)

**c. Brief description:** This proposal would calculate an amount for "taxes charged" to customers that incorporates both the amount of "taxes authorized to be collected" per Commission rate setting and variances from that amount caused by tax effect of utility's actual financial results.

**d. Brief rationale:** Under the plain language of the statute, the automatic adjustment clause "shall account for all taxes paid to units of government...and all taxes that are authorized to be collected through rates, so that *ratepayers are not charged* for more tax than...the utility pays to units of government." 3(6) (emphasis added). The bill does not define the calculation of taxes charged to ratepayers. This proposal works within the language of the bill to reach a fair result that calculates the amount of *taxes charged* by the utility by reference to actual utility results. This proposal would not have an effect on the calculation of "taxes paid and properly attributed" – it simply acknowledges that amounts calculated solely by reference to the utility's test year are not representative of the utility's actual results.

**e. Consequences:** This proposal would eliminate surcharges and collections from customers that result solely from variances from the utility's actual net to gross ratio and forecasted net to gross ratio. This proposal does not alter the impact of the "properly attributed" calculation. The primary impact of the proposal would be to mitigate the wide variances in rates that would otherwise result from the interpretation of "taxes authorized to be collected," which appear to be an unintended consequence of SB 408's definition of "taxes authorized to be collected."

**2. Use of deferred accounting to capture tax effects of expenses that have not been included in rates:**

- a. Proposed rule language:** A deferral account would be set up each year and would account for tax benefits related to disallowed expenses and investments, or investments that have not been included in rates. If an adjustment under SB 408 credits utility customers for these tax benefits, the deferral would operate in the opposite manner to return that credit to the utility.
- b. Related sections of the bill:** 3(6); 3(13)(e), (f).
- c. Brief description:** This proposal would return to the utility the tax effect of certain cost variances that should not trigger a rate action under the bill because the costs were not included in rates. These cost variances can be divided into three categories: 1) disallowed utility investments; 2) disallowed expenditures; and 3) investments not included in rates.
- d. Brief rationale:** When a cost item is disallowed or never included in rates, customers do not pay the cost of the item. It would be inappropriate to then give customers a benefit related to the disallowed item or item not in rates. This proposal addresses a significant unintended consequence of the bill – utility customers receive a benefit from costs that they do not bear and that are not included in rates, and utilities are required to credit amounts to customers related to an item for which the utility has received no cost recovery.
- e. Consequences and Example:** Imagine a utility purchases an asset for \$10,000,000. The investment is not included in rates. Sometime after purchase the asset is deemed worthless or inoperable, and the utility is required to write off its value on its books. Because the asset has not been sold, a tax deduction may not be claimed on its tax return, but the book-tax difference causes the utility to establish a deferred tax asset of (assuming 40% tax rate) \$4,000,000. In a subsequent year the utility disposes of the asset. The utility's tax payments to governmental units are reduced by \$4,000,000 at date of disposal. If this asset had been related to the regulated operations of the utility, the deferred tax adjustment under 3(13)(f)(C) would offset the reduction in "taxes paid" by a corresponding increase in "taxes authorized to be collected," and there would be no net adjustment to customers under SB 408. However, because the deferred tax adjustment was not included in rates and therefore appears unrelated to the utility's regulated operations, it would not offset the \$4,000,000 reduction in "taxes paid." Therefore, utility customers would receive a refund of this amount despite the fact that they have borne none the cost of the investment and that neither the cost of the item or the tax benefit was included in the utility's last general rate case.

This situation can be remedied simply by using a deferral to track deferred tax adjustments related to non-regulated subsidiaries and return those tax adjustment to the utility if credited to customers through the operation of an automatic adjustment clause under SB 408.

### 3. Earnings Test

a. **Proposed Rule Language:** In applying the automatic adjustment clause, the Commission will administer an earnings test to determine if any resulting surcharge or refund is reasonable. The earnings test will generally conform to standards required of utilities for filing their Results of Operations reports with the Commission. However, actual stand-alone utility financial results for the regulated operations of Oregon will be adjusted by replacing the utility's stand-alone Oregon regulated income tax expense with "taxes paid that are properly attributable to the regulated Oregon operations of the utility." Surcharges or refunds will be limited by the earnings test as follows:

1. Surcharges are limited to those amounts that result in the utility earning no greater than its authorized return on equity as determined by the Commission in the last general rate case proceeding.
2. Refunds are limited to those amounts that result in the utility earning no less than its authorized return on equity as determined by the Commission in the last general rate case proceeding.

b. **Related sections of bill:** 3(6) (automatic adjustment clause)

c. **Brief description:** An earnings test would be used to evaluate the reasonableness of adjustments calculated under the automatic adjustment clause. The earnings test would replace the utility's actual stand-alone Oregon income tax expense with the amount of "taxes paid that are properly attributable to the regulated Oregon operations of the utility" calculated as part of the automatic adjustment clause. All other aspects of the earnings test would generally conform to the approach used by utilities to develop their Results of Operations reports, including the application of previous rate making decisions from the last applicable general rate case Order of the Commission.

Surcharges resulting from the application of SB 408 will be limited to those collections that result in the utility earning no more than its authorized return on equity from the last applicable general rate case Order of the Commission.

Refunds resulting from the application of SB 408 will be limited to those refunds that result in the utility earning no less than its authorized return on equity from the last applicable general rate case Order of the Commission.

d. **Brief Rationale:** While an earnings test is not explicitly prescribed by SB 408, the Commission has a responsibility to produce rates that are fair, just and reasonable (ORS 756.040; 757.210). In fact, amendments to ORS 757.210 included in Senate Bill 408 prohibit the Commission from setting a rate that is not just and reasonable. An earnings test would ensure that the operation of the automatic adjustment clause neither unreasonably harms the utility nor

unreasonably harms customers. By requiring that the utility replace its stand-alone Oregon regulated income tax expense with the “taxes paid” amount, the application of the earnings test is consistent with the intent of SB 408 to only credit the utility when actual tax payments are made to the appropriate entities.

- e. **Consequences:** The Commission must consider the impact of surcharges or refunds calculated under an SB 408 automatic adjustment clause on the utility prior to allowing rates to go into effect. The earnings test would provide a simple, verifiable, and easy to administer test for making this calculation. The earnings test would ensure that rates remain fair, just, and reasonable.