BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

UE 177(4)

In the Matter of OREGON PUBLIC UTILITY STAFF Requesting the Commission Direct PACIFICORP (dba PACIFIC POWER & LIGHT COMPANY) To File Tariffs Establishing Automatic Adjustment Clauses Under the Terms of SB 408.	)))))))))))))	OPENING BRIEF OF THE INDUSTRIAL CUSTOMERS OF NORTHWEST UTILITIES

I. INTRODUCTION

Pursuant to the February 15, 2011 Prehearing Conference Report, the Industrial Customers of Northwest Utilities ("ICNU") submits the following opening brief regarding PacifiCorp's (or the "Company") proposed tax surcharge and the proposed stipulation ("Stipulation") of PacifiCorp, the Oregon Public Utility Commission ("OPUC" or the "Commission") Staff, and the Citizens' Utility Board ("CUB") (jointly, the "Settling Parties"). The Commission should reject the Settling Parties' proposed $13.5 million tax surcharge because it inappropriately allows PacifiCorp to recover a total of $77.4 million in total income taxes from customers for 2009, even though the Company did not paid <u>any</u> federal income taxes in 2009. The $13.5 million surcharge on customers is unjust and unreasonable, because it ignores that PacifiCorp experienced negative taxable income in 2009, it is not based on an accurate calculation of what PacifiCorp's stand-alone tax liability would be if it were a separate utility,

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and it fails to give ratepayers the benefit of PacifiCorp's tax losses. The Commission should instead recognize that PacifiCorp has negative stand-alone tax liability and account for these losses in a manner similar to how they are treated in Portland General Electric Company's ("PGE") 2009 tax report. Ratepayers can be provided a surcredit in a manner that complies with the Internal Revenue Service ("IRS") normalization requirements, Senate Bill ("SB") 408, and the Commission's SB 408 rules.

II. SUMMARY BACKGROUND

PacifiCorp submitted its SB 408 compliance tax report on October 15, 2010. The purpose of the tax filing is to determine for the 2009 tax year the difference between the state, federal and local taxes paid to taxing authorities and properly attributed to the Company's regulated operations with those collected in rates. The tax report allegedly calculated the amount of taxes paid to the taxing authorities using the "stand-alone method" in the recently amended OAR § 860-022-0041, which estimated that PacifiCorp paid $29.4 million more in taxes than were collected in rates. Joint Testimony/100, Bird-Fuller-Feighner/2. With interest, this would have resulted in a 3.1% surcharge. PacifiCorp filing at 1. Any surcharge amount is in addition to the almost $64 million that PacifiCorp collected from customers in rates for its 2009 income taxes. ICNU/100, Blumenthal/2. Although PacifiCorp proposed a large 2009 tax surcharge, the Company actually experienced negative taxable income and paid no taxes to the federal taxing authorities in 2009. ICNU/106 (Excerpt of PacifiCorp's SEC 2009 10-K); ICNU/107 (Excerpt of PacifiCorp's FERC Income Statement).

Administrative Law Judge ("ALJ") Hardie initially set a schedule in this proceeding, but prior to the filing of testimony by Staff and intervenors, the Settling Parties

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entered into the Stipulation. The schedule was revised, and the focus of this proceeding has shifted from a review of PacifiCorp's original filing to a review of the reasonableness of the proposed Stipulation. The ALJ adopted a new schedule that allowed for the Settling Parties to file supporting testimony, ICNU to file testimony in opposition to the Stipulation, and a full evidentiary hearing and briefing schedule.

The Settling Parties filed the Stipulation and supporting testimony by Ryan Fuller, Carla Bird, Gordon Feighner, and Bob Jenks. The Stipulation proposed four changes to PacifiCorp's tax report. First, the parties agreed to certain adjustments that initially reduced the Company's surcharge to $27.3 million. Stipulation at 3. Next, the Settling Parties agreed to resolve three additional issues regarding the tax report, including PacifiCorp's: 1) exclusion of certain supplemental schedules in the calculation of the taxes authorized to be collected in rates; 2) inclusion of the impact of depreciation flow-through in the calculation of the deferred tax floor in to OAR § 860-022-0041(4)(d) ("(4)(d) limitation"); and 3) methodology for allocating to Oregon the total-Company book-tax difference for book and tax depreciation. Id. The Stipulation made changes to these three issues, which resulted in a $12.24 million adjustment, including a $5.06 million adjustment related to the calculation of taxes collected, and a $7.18 million adjustment related to the calculation of the deferred tax floor. Id.

At the time it was filed, the Stipulation was inconsistent with OAR § 860-022-0041(4)(d). As a result, the Settling Parties agreed to request a rule change, so that the deferred tax floor does not apply to taxes paid determined under the stand-alone method. Hearing Transcript ("Tr.") at 83-84. The Settling Parties claim that PacifiCorp's taxes paid calculation is consistent with the stand-alone method, but they do not include PacifiCorp's stand-alone tax

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losses and instead allow those losses to be passed through to the Company's parent company. Tr. at 31, 57-58, 63-64. The Settling Parties ignore that PacifiCorp had negative taxable income in 2009, and instead they assume the Company had no tax liability. Id.

The Stipulation ultimately recommends a surcharge of $13.47 million for federal and state taxes and a refund of $86,932 for local taxes. Stipulation at 5. The interest on the surcharge and refund amounts will reflect the Blended Treasury Rate. During the deferral and amortization periods, the estimated amount of surcharge plus interest is $15.77 million for federal and state taxes and the estimated refund plus interest is $101,739 for local taxes. Id. at 5.

PacifiCorp and Staff, but not CUB, joined in the second part of the Stipulation, which provides that PacifiCorp will seek a Private Letter Ruling ("PLR") from the IRS regarding whether the revision to OAR § 860-022-0041(4)(d) will cause a normalization violation. Pending the rulemaking and a favorable PLR from the IRS, PacifiCorp will file an application for deferral of the difference between the surcharge produced by the deferred tax floor ($27.3 million) and the surcharge calculated assuming the rule change ($13.47 million). Id. at 7.

On February 7, 2011, ICNU submitted Written Objections and the Testimony of Ellen Blumenthal in opposition to the Stipulation. Ms. Blumenthal was required to review PacifiCorp's tax report in the Portland safe room, while Staff was provided a complete copy of the filing in their offices. Ms. Blumenthal traveled to Portland and spent approximately two days reviewing the Company's tax report in the safe room. Ms. Blumenthal was only allowed to take limited notes and was constantly monitored by a PacifiCorp employee. Tr. at 21-22. Even if Ms. Blumenthal had been allowed to take comprehensive notes, PacifiCorp's workpapers are

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extensive, and it would have been impossible to take sufficient notes for Ms. Blumenthal to recalculate all aspects of PacifiCorp's tax filing back at her offices.

Ms. Blumenthal's testimony proposes an alternative method of calculating PacifiCorp's tax report; however, since she did not have access to the Company's highly confidential workpapers while drafting her testimony, she did not propose a complete calculation. Ms. Blumenthal first agreed with the Settling Parties that the (4)(d) limitation in the current rule is not necessary to comply with the normalization requirements. ICNU/100, Blumenthal/7-8. Ms. Blumenthal then calculated an alternative tax calculation that includes PacifiCorp's stand-alone tax losses and results in a larger adjustment to PacifiCorp's proposed tax surcharge. Id. at Blumenthal/11-13; Highly Confidential ICNU/104. Ms. Blumenthal's alternative calculation results in a small surcredit if other deferred taxes are included, and a large surcredit if other deferred taxes are excluded. Id.

Ms. Blumenthal also explained that Part 2 of the Stipulation is not necessary, because the normalization provisions of the IRC are clear and straightforward. ICNU/100, Blumenthal/10. Ms. Blumenthal explained that the proposed rule change will not result in a normalization violation, and it is unnecessary for PacifiCorp to obtain a PLR or file a request for deferral. Id. Ms. Blumenthal did not address ICNU's previously raised concerns with how PacifiCorp's tax report and the rules violate SB 408.

On February 15, 2011, Staff submitted a request to modify OAR § 860-022-0041(4)(d), on the grounds that the deferred tax floor would unnecessarily harm Oregon ratepayers and violates SB 408. In the Matter of the Adoption of a Temporary Amendment to OAR 860-022-0041, Docket No. AR 547, Order No. 11-064 at 2 (Feb. 22, 2011). Specifically,

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the deferred tax floor would result in imposing "a surcharge of millions of dollars greater than is required under ORS 757.268." Id. at 3. The Commission adopted a new temporary rule within seven days without accepting comments from interested parties. Id. The new rule removes "the deferred tax balance floor for both the stand-alone and consolidated methodologies for calculating 'taxes paid.'" Id. at 2.

III. ARGUMENT

The fundamental issue in this proceeding is how to account for PacifiCorp's negative taxable income when calculating the Company's stand-alone tax liability. The Settling Parties assume that PacifiCorp did not actually experience any tax losses, which is inconsistent with the fact that the Company actually did not pay any taxes in 2009. The Settling Parties decision to ignore PacifiCorp's negative taxable income is not necessary to account for or normalize PacifiCorp's deferred taxes, and it artificially inflates the amount of taxes that are calculated under the stand-alone methodology. The Commission should adopt Ms. Blumenthal's alternative approach of accounting for PacifiCorp's losses because it reduces or eliminates PacifiCorp's surcharge in a manner that is consistent with SB 408, the SB 408 rules and the IRC normalization requirements.

The Settling Parties raise a number of inaccurate and/or unpersuasive arguments against Ms. Blumenthal's recommendations. Ms. Blumenthal did not have the ability to utilize PacifiCorp's tax report when she drafted her testimony, and she acknowledges that the final PacifiCorp tax amount will need to be recalculated to include those small amounts she intentionally omitted in order to simplify her calculation, including state and local taxes and charitable contributions. Ms. Blumenthal did not propose a specific tax calculation, but instead

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recommended an overall approach that will require PacifiCorp to file a revised tax report that includes all the appropriate adjustments. In addition, contrary to the Settling Parties complaints, Ms. Blumenthal's recommendations will not result in any normalization violations, and she appropriately included all of the Company's regulated operations. The Settling Parties concerns on these issues are based on inaccurate factual grounds and unsupported interpretations of the IRC's normalization requirements.

Finally, all parties agree that ratepayers should not benefit from accelerated tax depreciation as required by the normalization requirements, and that the (4)(d) limitation improperly imposed a deferred tax floor that exceeded the IRC normalization requirements and artificially inflated the Company's surcharge. While the accelerated depreciation issue is no longer in dispute, it reflects that the Commission can make common sense changes to ensure that the SB 408 rules comply with SB 408 and ratepayers do not pay unnecessarily high surcharges, particularly in a year in which the utility paid no taxes.

1. The Commission Should Recognize that PacifiCorp's Tax Return Shows that the Company Experienced Negative Taxable Income

The Settling Parties decision to ignore PacifiCorp's negative taxable income is inconsistent with the requirement that the stand-alone method should be the most accurate estimate of what the Company's taxes would be if PacifiCorp was not included in a consolidated tax return. The practical impact of the Settling Parties' approach is that the tax losses that PacifiCorp actually experienced (and would experience if it operated as a stand-alone utility) are passed on to the Company's owner, Berkshire Hathaway. The Settling Parties inappropriately recognize that PacifiCorp's tax losses offset the taxable income of other Berkshire Hathaway affiliates lowering Berkshire Hathaway's tax liability. The Settling Parties' tax report violates

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the Commission's previous conclusion that PacifiCorp's stand-alone tax liability should be estimated without accounting for tax differences caused by inclusion of the utility in the corporate operations of the utility's parent or affiliates. Re PacifiCorp SB 408 Tax Report for Calendar Year 2006, Docket No. UE 177, Order No. 09-177 at 14 (May 20, 2009).

This is the first year under SB 408 in which PacifiCorp and PGE did not pay any income taxes and reported negative taxable income. Tr. at 22. The Settling Parties propose that PacifiCorp's negative taxable income be ignored and that the Commission assume that PacifiCorp did not report losses. Tr. at 31-32, 57-58, 63-64. ICNU proposes that the starting point for PacifiCorp's tax report is to recognize that the Company reported losses, in a manner similar to how Staff and PGE account for PGE's tax losses. Tr. at 22, 31-32. ICNU's approach does not improperly allow ratepayers to benefit from accelerated depreciation or violate any normalization requirements, but simply accounts for the Company's losses in a manner that better reflects the fact that PacifiCorp did not actually pay taxes in 2009. Tr. at 31-32. Oregon ratepayers should not be required to pay any additional surcharges.

When calculating PacifiCorp's taxes that are properly attributed to regulated operations, the Settling Parties assume that PacifiCorp did not experience negative taxable income. Tr. at 31-32, 57-58, 63-64. In contrast, when Staff and PGE calculate that utility's tax report, they recognize that PGE experienced losses and received refunds of taxes paid in prior periods because of 2009 negative taxable income. Tr. at 22, 31-32, 57-58. Ms. Blumenthal's recommendation is that the Commission direct PacifiCorp to account for its losses in a similar manner as PGE, which will result in a significant reduction or elimination of the surcharge. Tr. at 22, 31-32, 57-58; ICNU/100, Blumenthal/11-13. The Settling Parties' approach "makes no

sense in a year in which we have a huge negative tax loss for ratepayers to pay even more in income taxes than they've already paid to the utility through rates." Tr. at 58.

Ms. Blumenthal recalculated PacifiCorp's tax report by "starting with a negative taxable income" attributable to Oregon regulated operations. Tr. at 31-32. The calculation of the Company's actual tax liability on a stand-alone basis begins with PacifiCorp's negative taxable income per its tax return. Ms. Blumenthal then added back the tax depreciation deduction included in the negative taxable income related to its Oregon regulated operations and deducted the straight line depreciation. Tr. at 31-32. The tax depreciation was added back in order to ensure that Oregon ratepayers do not benefit from the accelerated tax depreciation.

The Oregon tax rule does not clearly address how to account for negative taxable income, which is reflected in Staff's different treatment of the losses for PGE and PacifiCorp. Tr. at 63-64. Although the Settling Parties never explain why they start with no tax liability instead of the Company's negative tax liability, ICNU assumes that it is because PacifiCorp is a member of a consolidated tax group that files a single tax return. Tr. at 31-32, 57-58, 63-64. The Stipulation is based on the loss reported by PacifiCorp being "subsumed in the consolidated income of its parent." Tr. at 31. The Settling Parties essentially recognize that PacifiCorp's actual negative tax liability is used to offset taxable income in its shareholder's positive tax liability, resulting in significant tax savings for Berkshire Hathaway. Tr. at 31-32, 57-58, 63-64.

Since PacifiCorp's tax report in this proceeding is based on the stand-alone method, PacifiCorp's actual tax losses should be accounted for and should not be used to lower Berkshire Hathaway's tax liability. The Settling Parties' approach is inconsistent with the Commission's rulings in the Company's previous tax proceedings concluding that the stand-

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alone method should not account for the tax gains and losses of parent companies or affiliates. The Commission's rules allow PacifiCorp's tax filing to be based on a stand-alone method, which has the goal of providing "the most accurate information available on what taxes the regulated operations of the utility would pay if it were to pay taxes as a separate fully regulated company . . . ." Docket No. UE 177, Order No. 09-177 at 14. The Commission rejected ICNU's argument in that proceeding that the stand-alone method should recognize that PacifiCorp's tax liability is offset with the losses of Berkshire Hathaway affiliates. Id. at 15-16. The Commission reasoned that the statute does not mandate "that the stand-alone cap reflect tax savings caused by losses in the corporate operations of the utility's parent or affiliates." Id. at 15-16.

The Settling Parties' decision to assume that PacifiCorp's tax liability is not negative essentially recognizes that PacifiCorp's owner uses the Company's tax losses to offset the tax liability of other affiliates and reduce its overall tax liability. If the stand-alone method should not recognize that PacifiCorp's tax liability is offset with affiliate losses, then the stand-alone method should similarly not recognize that PacifiCorp's tax losses are offset with affiliate gains. The current situation results in Berkshire Hathaway winning whether PacifiCorp experiences tax gains or losses.

2. Recognizing PacifiCorp's Standalone Losses Does Not Violate SB 408

The Settling Parties complain that Ms. Blumenthal violates SB 408 because her tax calculation did not include all of the minor adjustments related to state income taxes and charitable contributions and the operations of the Pacific Minerals, but notably do not argue that using PacifiCorp's tax losses violates the law. Ms. Blumenthal did not prepare a complete tax report pinpointing an exact surcredit amount, because she did not have sufficient access to

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PacifiCorp's highly confidential documents. Instead of calculating every component of the Company's tax report, Ms. Blumenthal recommended an overall approach of recognizing, rather than ignoring, PacifiCorp's negative taxable income. Ms. Blumenthal recognizes that further adjustments related to charitable contributions and state and local taxes will need to be made; however, these items do not significantly alter the fact that a large surcharge is not warranted. ICNU/100, Blumenthal/3; Tr. at 38-41, 61. Separately, the Settling Parties' argument that Ms. Blumenthal's tax report excluded certain regulated operations related to Pacific Minerals is factually incorrect. Tr. at 34-35, 46-47; ICNU/105 at 47.

The Settling Parties argue that Ms. Blumenthal's tax calculation violates SB 408 because it does not include state income taxes and charitable contributions. Joint Testimony/200, Jenks-Bird-Fuller/4-5. The Settling Parties are correct that ICNU did not include these amounts and that they should be included in the final tax report, but these are not flaws in ICNU's approach. Ms. Blumenthal did not include these amounts because they were "de minimus in this case" and she did not have access to the documents to accurately calculate them. ICNU/100, Blumenthal/3; Tr. at 20-22, 38-41, 61. The inclusion or lack of inclusion of these amounts has nothing to do with whether PacifiCorp's tax losses are recognized, and Ms. Blumenthal's tax calculation can be updated easily by PacifiCorp to include state taxes and charitable contributions.

The Settling Parties incorrectly argue that Ms. Blumenthal's tax calculation is not based on PacifiCorp's regulated operations. Joint Testimony/200, Jenks-Bird-Fuller/4. Specifically, they allege that Ms. Blumenthal excluded Pacific Minerals, a portion of which falls under the jurisdiction of the Commission. Id. ICNU agrees that Pacific Minerals should be

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included in the tax report and, as Ms. Blumenthal explained at the hearing, she included the company in her tax calculation. Tr. at 46-47. Ms. Blumenthal used PacifiCorp's own workpapers, which include Pacific Minerals, to calculate her adjustment. Tr. at 46-47; ICNU/105 at 47 (excerpt of PacifiCorp workpapers).

The Settling Parties also criticize Ms. Blumenthal's tax calculation because she did not use the Revised Protocol to allocate total Company activity to Oregon regulated operations. Joint Testimony/200, Jenks-Bird-Fuller/4. Ms. Blumenthal did not use the Revised Protocol because its allocation factors are not designed to allocate income as a single amount. For example, none of the Revised Protocol allocation factors used by PacifiCorp include operating revenues. The Settling Parties could not even identify which allocation factors were used to allocate book depreciation. Tr. at 87. The results of operations used by Ms. Blumenthal should reflect the allocation factors from the Revised Protocol, as long as PacifiCorp used the Revised Protocol to prepare the results of operations report that it filed with the Commission.

3. ICNU's Recommendations Will Not Result in an IRS Normalization Violation

The Settling Parties argue that Ms. Blumenthal's tax calculation violates the IRS normalization rules. Once again, the Settling Parties do not argue that including losses in the Company's tax filing violates the IRC normalization requirements, rather that Ms. Blumenthal's alternative calculation is inconsistent with the normalization requirements of the IRC because: 1) ICNU's adjustments for tax and book depreciation are allegedly allocated at different ratios than the amounts included in pre-tax book-income and taxable income; and 2) Ms. Blumenthal

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allegedly believes that basis differences are not required to be normalized by the IRC.[1/] These arguments are groundless and mere distractions from the essential issue of how to account for PacifiCorp's negative taxable income. In addition, even if these claims were correct, they would reduce but not fundamentally alter Ms. Blumenthal's adjustment. Confidential Exhibit Joint Testimony/202.

The Settling Parties argue that Ms. Blumenthal's adjustments for tax and book depreciation are allocated improperly at a different ratio than the amounts included in the pre-tax book-income and taxable income, and that ICNU's surcredit is overstated because Ms. Blumenthal did not match book and tax depreciation with PacifiCorp's taxable income (or losses). Joint Testimony/200, Jenks-Bird-Fuller/6. ICNU agrees that Ms. Blumenthal did not match these items, but matching is not necessary and the Settling Parties fail to explain or provide any citations for their argument that matching is required by the IRC. First, book depreciation (line 3 of ICNU/104) is not actually included in the tax return, so there is no need to carefully match it with PacifiCorp's taxable income on Exhibit ICNU/104. More importantly, the Settling Parties fail to inform the Commission that their tax calculation similarly uses different percentages and does not match. Tr. at 35-39. Ms. Blumenthal's calculations used the amounts and percentages provided in the Company's workpapers, which PacifiCorp itself used to calculate its normalization of the difference between book and tax depreciation. Tr. at 34-35.

The Settling Parties also argue that Ms. Blumenthal "erroneously testifies that basis differences are not required to be normalized by the IRC." Joint Testimony/200, Jenks-Bird-Fuller/6. The Settling Parties then claim that Ms. Blumenthal did not normalize the basis

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[1/] The Settling Parties also argue that Ms. Blumenthal allegedly excluded Pacific Minerals. This is incorrect, as explained in the preceding section.

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difference for Contributions in Aid of Construction. Id. Notably, the Settling Parties fail to identify any specific aspect of Ms. Blumenthal's calculation in which she allegedly did not normalize basis differences. Ms. Blumenthal's statement that basis differences are not required to be normalized is a generic and generally accurate statement, but it does not mean that Ms. Blumenthal failed to normalize any basis differences. Ms. Blumenthal used PacifiCorp's workpapers for her tax calculation and did not change any normalized basis differences that might be included in their original filing. Tr. at 46. In other words, her adjustment includes any basis differences already normalized by PacifiCorp. The Settling Parties' claims are a disingenuous attempt to distort and mischaracterize Ms. Blumenthal's tax calculation.

4. ICNU's Recommendations Are Not Inconsistent with Normalized Taxes in Rates

The Settling Parties argue that Ms. Blumenthal's approach is inconsistent with how the amounts authorized to be collected in rates should be calculated. Joint Testimony/200, Jenks-Bird-Fuller/6-8. The Settling Parties state that the Commission uses fully normalized income taxes in setting rates and that Ms. Blumenthal's exclusion of non-depreciation deferred taxes constitutes improper flow-through accounting which results in "a significant mismatch when compared against taxes authorized to be collected in rates." Id. at 7. ICNU is not advocating flow-through accounting but instead recommends that these deferred taxes be excluded, because PacifiCorp has not met its burden of proof to establish that they are related to regulated operations. Tr. at 51-52. Exclusion of the deferred taxes increases Ms. Blumenthal's proposed small surcredit to a large surcredit. ICNU/100, Blumenthal/12.

PacifiCorp has not demonstrated that all of its deferred taxes are related to costs that are or should be included in rates. Id. The Settling Parties are correct that taxes in the

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Company's rate cases are intended to be fully normalized, but they have not submitted any evidence that demonstrates what is included in PacifiCorp's present rates. Tr. at 51-52. The Settling Parties' testimony does not make this claim, and at the hearing Staff admitted that it has not verified whether the total non-depreciation related deferred taxes were actually included in rates in the last general rate case. Tr. at 82-83. PacifiCorp's deferred taxes have not been reviewed fully in a general rate case or this proceeding, and they should be excluded until the Company has met its burden of proof to establish that they do not include any improper amounts. Tr. at 82-83; ICNU/100, Blumenthal/12.

IV. CONCLUSION

A $13.5 million surcharge is unwarranted and unreasonable because PacifiCorp did not pay any federal income taxes in 2009, and the Settling Parties ignore the Company's negative taxable income when calculating their proposed surcharge. The Settling Parties' tax calculation is not representative of what PacifiCorp's stand-alone tax liability would be if it were not owned by Berkshire Hathaway, but instead allows PacifiCorp's parent company to reap the benefits of its losses. The Commission should recognize that PacifiCorp has negative stand-alone tax liability and calculate its tax report in a manner similar to PGE's 2009 tax report.

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Dated this 11th day of March, 2011.

Respectfully submitted,

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losses and instead allow those losses to be passed through to the Company's parent company. Tr. at 31, 57-58, 63-64. The Settling Parties ignore that PacifiCorp had negative taxable income in 2009, and instead they assume the Company had no tax liability. Id.

The Stipulation ultimately recommends a surcharge of $13.47 million for federal and state taxes and a refund of $86,932 for local taxes. Stipulation at 5. The interest on the surcharge and refund amounts will reflect the Blended Treasury Rate. During the deferral and amortization periods, the estimated amount of surcharge plus interest is $15.77 million for federal and state taxes and the estimated refund plus interest is $101,739 for local taxes. Id. at 5.

PacifiCorp and Staff, but not CUB, joined in the second part of the Stipulation, which provides that PacifiCorp will seek a Private Letter Ruling ("PLR") from the IRS regarding whether the revision to OAR § 860-022-0041(4)(d) will cause a normalization violation. Pending the rulemaking and a favorable PLR from the IRS, PacifiCorp will file an application for deferral of the difference between the surcharge produced by the deferred tax floor ($27.3 million) and the surcharge calculated assuming the rule change ($13.47 million). Id. at 7.

On February 7, 2011, ICNU submitted Written Objections and the Testimony of Ellen Blumenthal in opposition to the Stipulation. Ms. Blumenthal was required to review PacifiCorp's tax report in the Portland safe room, while Staff was provided a complete copy of the filing in their offices. Ms. Blumenthal traveled to Portland and spent approximately two days reviewing the Company's tax report in the safe room. Ms. Blumenthal was only allowed to take limited notes and was constantly monitored by a PacifiCorp employee. Tr. at 21-22. Even if Ms. Blumenthal had been allowed to take comprehensive notes, PacifiCorp's workpapers are

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extensive, and it would have been impossible to take sufficient notes for Ms. Blumenthal to recalculate all aspects of PacifiCorp's tax filing back at her offices.

Ms. Blumenthal's testimony proposes an alternative method of calculating PacifiCorp's tax report; however, since she did not have access to the Company's highly confidential workpapers while drafting her testimony, she did not propose a complete calculation. Ms. Blumenthal first agreed with the Settling Parties that the (4)(d) limitation in the current rule is not necessary to comply with the normalization requirements. ICNU/100, Blumenthal/7-8. Ms. Blumenthal then calculated an alternative tax calculation that includes PacifiCorp's stand-alone tax losses and results in a larger adjustment to PacifiCorp's proposed tax surcharge. Id. at Blumenthal/11-13; Highly Confidential ICNU/104. Ms. Blumenthal's alternative calculation results in a small surcredit if other deferred taxes are included, and a large surcredit if other deferred taxes are excluded. Id.

Ms. Blumenthal also explained that Part 2 of the Stipulation is not necessary, because the normalization provisions of the IRC are clear and straightforward. ICNU/100, Blumenthal/10. Ms. Blumenthal explained that the proposed rule change will not result in a normalization violation, and it is unnecessary for PacifiCorp to obtain a PLR or file a request for deferral. Id. Ms. Blumenthal did not address ICNU's previously raised concerns with how PacifiCorp's tax report and the rules violate SB 408.

On February 15, 2011, Staff submitted a request to modify OAR § 860-022-0041(4)(d), on the grounds that the deferred tax floor would unnecessarily harm Oregon ratepayers and violates SB 408. In the Matter of the Adoption of a Temporary Amendment to OAR 860-022-0041, Docket No. AR 547, Order No. 11-064 at 2 (Feb. 22, 2011). Specifically,

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the deferred tax floor would result in imposing "a surcharge of millions of dollars greater than is required under ORS 757.268." Id. at 3. The Commission adopted a new temporary rule within seven days without accepting comments from interested parties. Id. The new rule removes "the deferred tax balance floor for both the stand-alone and consolidated methodologies for calculating 'taxes paid.'" Id. at 2.

III. ARGUMENT

The fundamental issue in this proceeding is how to account for PacifiCorp's negative taxable income when calculating the Company's stand-alone tax liability. The Settling Parties assume that PacifiCorp did not actually experience any tax losses, which is inconsistent with the fact that the Company actually did not pay any taxes in 2009. The Settling Parties decision to ignore PacifiCorp's negative taxable income is not necessary to account for or normalize PacifiCorp's deferred taxes, and it artificially inflates the amount of taxes that are calculated under the stand-alone methodology. The Commission should adopt Ms. Blumenthal's alternative approach of accounting for PacifiCorp's losses because it reduces or eliminates PacifiCorp's surcharge in a manner that is consistent with SB 408, the SB 408 rules and the IRC normalization requirements.

The Settling Parties raise a number of inaccurate and/or unpersuasive arguments against Ms. Blumenthal's recommendations. Ms. Blumenthal did not have the ability to utilize PacifiCorp's tax report when she drafted her testimony, and she acknowledges that the final PacifiCorp tax amount will need to be recalculated to include those small amounts she intentionally omitted in order to simplify her calculation, including state and local taxes and charitable contributions. Ms. Blumenthal did not propose a specific tax calculation, but instead

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recommended an overall approach that will require PacifiCorp to file a revised tax report that includes all the appropriate adjustments. In addition, contrary to the Settling Parties complaints, Ms. Blumenthal's recommendations will not result in any normalization violations, and she appropriately included all of the Company's regulated operations. The Settling Parties concerns on these issues are based on inaccurate factual grounds and unsupported interpretations of the IRC's normalization requirements.

Finally, all parties agree that ratepayers should not benefit from accelerated tax depreciation as required by the normalization requirements, and that the (4)(d) limitation improperly imposed a deferred tax floor that exceeded the IRC normalization requirements and artificially inflated the Company's surcharge. While the accelerated depreciation issue is no longer in dispute, it reflects that the Commission can make common sense changes to ensure that the SB 408 rules comply with SB 408 and ratepayers do not pay unnecessarily high surcharges, particularly in a year in which the utility paid no taxes.

1. The Commission Should Recognize that PacifiCorp's Tax Return Shows that the Company Experienced Negative Taxable Income

The Settling Parties decision to ignore PacifiCorp's negative taxable income is inconsistent with the requirement that the stand-alone method should be the most accurate estimate of what the Company's taxes would be if PacifiCorp was not included in a consolidated tax return. The practical impact of the Settling Parties' approach is that the tax losses that PacifiCorp actually experienced (and would experience if it operated as a stand-alone utility) are passed on to the Company's owner, Berkshire Hathaway. The Settling Parties inappropriately recognize that PacifiCorp's tax losses offset the taxable income of other Berkshire Hathaway affiliates lowering Berkshire Hathaway's tax liability. The Settling Parties' tax report violates

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the Commission's previous conclusion that PacifiCorp's stand-alone tax liability should be estimated without accounting for tax differences caused by inclusion of the utility in the corporate operations of the utility's parent or affiliates. Re PacifiCorp SB 408 Tax Report for Calendar Year 2006, Docket No. UE 177, Order No. 09-177 at 14 (May 20, 2009).

This is the first year under SB 408 in which PacifiCorp and PGE did not pay any income taxes and reported negative taxable income. Tr. at 22. The Settling Parties propose that PacifiCorp's negative taxable income be ignored and that the Commission assume that PacifiCorp did not report losses. Tr. at 31-32, 57-58, 63-64. ICNU proposes that the starting point for PacifiCorp's tax report is to recognize that the Company reported losses, in a manner similar to how Staff and PGE account for PGE's tax losses. Tr. at 22, 31-32. ICNU's approach does not improperly allow ratepayers to benefit from accelerated depreciation or violate any normalization requirements, but simply accounts for the Company's losses in a manner that better reflects the fact that PacifiCorp did not actually pay taxes in 2009. Tr. at 31-32. Oregon ratepayers should not be required to pay any additional surcharges.

When calculating PacifiCorp's taxes that are properly attributed to regulated operations, the Settling Parties assume that PacifiCorp did not experience negative taxable income. Tr. at 31-32, 57-58, 63-64. In contrast, when Staff and PGE calculate that utility's tax report, they recognize that PGE experienced losses and received refunds of taxes paid in prior periods because of 2009 negative taxable income. Tr. at 22, 31-32, 57-58. Ms. Blumenthal's recommendation is that the Commission direct PacifiCorp to account for its losses in a similar manner as PGE, which will result in a significant reduction or elimination of the surcharge. Tr. at 22, 31-32, 57-58; ICNU/100, Blumenthal/11-13. The Settling Parties' approach "makes no

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sense in a year in which we have a huge negative tax loss for ratepayers to pay even more in income taxes than they've already paid to the utility through rates." Tr. at 58.

Ms. Blumenthal recalculated PacifiCorp's tax report by "starting with a negative taxable income" attributable to Oregon regulated operations. Tr. at 31-32. The calculation of the Company's actual tax liability on a stand-alone basis begins with PacifiCorp's negative taxable income per its tax return. Ms. Blumenthal then added back the tax depreciation deduction included in the negative taxable income related to its Oregon regulated operations and deducted the straight line depreciation. Tr. at 31-32. The tax depreciation was added back in order to ensure that Oregon ratepayers do not benefit from the accelerated tax depreciation.

The Oregon tax rule does not clearly address how to account for negative taxable income, which is reflected in Staff's different treatment of the losses for PGE and PacifiCorp. Tr. at 63-64. Although the Settling Parties never explain why they start with no tax liability instead of the Company's negative tax liability, ICNU assumes that it is because PacifiCorp is a member of a consolidated tax group that files a single tax return. Tr. at 31-32, 57-58, 63-64. The Stipulation is based on the loss reported by PacifiCorp being "subsumed in the consolidated income of its parent." Tr. at 31. The Settling Parties essentially recognize that PacifiCorp's actual negative tax liability is used to offset taxable income in its shareholder's positive tax liability, resulting in significant tax savings for Berkshire Hathaway. Tr. at 31-32, 57-58, 63-64.

Since PacifiCorp's tax report in this proceeding is based on the stand-alone method, PacifiCorp's actual tax losses should be accounted for and should not be used to lower Berkshire Hathaway's tax liability. The Settling Parties' approach is inconsistent with the Commission's rulings in the Company's previous tax proceedings concluding that the stand-

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alone method should not account for the tax gains and losses of parent companies or affiliates. The Commission's rules allow PacifiCorp's tax filing to be based on a stand-alone method, which has the goal of providing "the most accurate information available on what taxes the regulated operations of the utility would pay if it were to pay taxes as a separate fully regulated company . . . ." Docket No. UE 177, Order No. 09-177 at 14. The Commission rejected ICNU's argument in that proceeding that the stand-alone method should recognize that PacifiCorp's tax liability is offset with the losses of Berkshire Hathaway affiliates. Id. at 15-16. The Commission reasoned that the statute does not mandate "that the stand-alone cap reflect tax savings caused by losses in the corporate operations of the utility's parent or affiliates." Id. at 15-16.

The Settling Parties' decision to assume that PacifiCorp's tax liability is not negative essentially recognizes that PacifiCorp's owner uses the Company's tax losses to offset the tax liability of other affiliates and reduce its overall tax liability. If the stand-alone method should not recognize that PacifiCorp's tax liability is offset with affiliate losses, then the stand-alone method should similarly not recognize that PacifiCorp's tax losses are offset with affiliate gains. The current situation results in Berkshire Hathaway winning whether PacifiCorp experiences tax gains or losses.

2. Recognizing PacifiCorp's Standalone Losses Does Not Violate SB 408

The Settling Parties complain that Ms. Blumenthal violates SB 408 because her tax calculation did not include all of the minor adjustments related to state income taxes and charitable contributions and the operations of the Pacific Minerals, but notably do not argue that using PacifiCorp's tax losses violates the law. Ms. Blumenthal did not prepare a complete tax report pinpointing an exact surcredit amount, because she did not have sufficient access to

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PacifiCorp's highly confidential documents. Instead of calculating every component of the Company's tax report, Ms. Blumenthal recommended an overall approach of recognizing, rather than ignoring, PacifiCorp's negative taxable income. Ms. Blumenthal recognizes that further adjustments related to charitable contributions and state and local taxes will need to be made; however, these items do not significantly alter the fact that a large surcharge is not warranted. ICNU/100, Blumenthal/3; Tr. at 38-41, 61. Separately, the Settling Parties' argument that Ms. Blumenthal's tax report excluded certain regulated operations related to Pacific Minerals is factually incorrect. Tr. at 34-35, 46-47; ICNU/105 at 47.

The Settling Parties argue that Ms. Blumenthal's tax calculation violates SB 408 because it does not include state income taxes and charitable contributions. Joint Testimony/200, Jenks-Bird-Fuller/4-5. The Settling Parties are correct that ICNU did not include these amounts and that they should be included in the final tax report, but these are not flaws in ICNU's approach. Ms. Blumenthal did not include these amounts because they were "de minimus in this case" and she did not have access to the documents to accurately calculate them. ICNU/100, Blumenthal/3; Tr. at 20-22, 38-41, 61. The inclusion or lack of inclusion of these amounts has nothing to do with whether PacifiCorp's tax losses are recognized, and Ms. Blumenthal's tax calculation can be updated easily by PacifiCorp to include state taxes and charitable contributions.

The Settling Parties incorrectly argue that Ms. Blumenthal's tax calculation is not based on PacifiCorp's regulated operations. Joint Testimony/200, Jenks-Bird-Fuller/4. Specifically, they allege that Ms. Blumenthal excluded Pacific Minerals, a portion of which falls under the jurisdiction of the Commission. Id. ICNU agrees that Pacific Minerals should be

included in the tax report and, as Ms. Blumenthal explained at the hearing, she included the company in her tax calculation. Tr. at 46-47. Ms. Blumenthal used PacifiCorp's own workpapers, which include Pacific Minerals, to calculate her adjustment. Tr. at 46-47; ICNU/105 at 47 (excerpt of PacifiCorp workpapers).

The Settling Parties also criticize Ms. Blumenthal's tax calculation because she did not use the Revised Protocol to allocate total Company activity to Oregon regulated operations. Joint Testimony/200, Jenks-Bird-Fuller/4. Ms. Blumenthal did not use the Revised Protocol because its allocation factors are not designed to allocate income as a single amount. For example, none of the Revised Protocol allocation factors used by PacifiCorp include operating revenues. The Settling Parties could not even identify which allocation factors were used to allocate book depreciation. Tr. at 87. The results of operations used by Ms. Blumenthal should reflect the allocation factors from the Revised Protocol, as long as PacifiCorp used the Revised Protocol to prepare the results of operations report that it filed with the Commission.

3. ICNU's Recommendations Will Not Result in an IRS Normalization Violation

The Settling Parties argue that Ms. Blumenthal's tax calculation violates the IRS normalization rules. Once again, the Settling Parties do not argue that including losses in the Company's tax filing violates the IRC normalization requirements, rather that Ms. Blumenthal's alternative calculation is inconsistent with the normalization requirements of the IRC because: 1) ICNU's adjustments for tax and book depreciation are allegedly allocated at different ratios than the amounts included in pre-tax book-income and taxable income; and 2) Ms. Blumenthal

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allegedly believes that basis differences are not required to be normalized by the IRC.[1/] These arguments are groundless and mere distractions from the essential issue of how to account for PacifiCorp's negative taxable income. In addition, even if these claims were correct, they would reduce but not fundamentally alter Ms. Blumenthal's adjustment. Confidential Exhibit Joint Testimony/202.

The Settling Parties argue that Ms. Blumenthal's adjustments for tax and book depreciation are allocated improperly at a different ratio than the amounts included in the pre-tax book-income and taxable income, and that ICNU's surcredit is overstated because Ms. Blumenthal did not match book and tax depreciation with PacifiCorp's taxable income (or losses). Joint Testimony/200, Jenks-Bird-Fuller/6. ICNU agrees that Ms. Blumenthal did not match these items, but matching is not necessary and the Settling Parties fail to explain or provide any citations for their argument that matching is required by the IRC. First, book depreciation (line 3 of ICNU/104) is not actually included in the tax return, so there is no need to carefully match it with PacifiCorp's taxable income on Exhibit ICNU/104. More importantly, the Settling Parties fail to inform the Commission that their tax calculation similarly uses different percentages and does not match. Tr. at 35-39. Ms. Blumenthal's calculations used the amounts and percentages provided in the Company's workpapers, which PacifiCorp itself used to calculate its normalization of the difference between book and tax depreciation. Tr. at 34-35.

The Settling Parties also argue that Ms. Blumenthal "erroneously testifies that basis differences are not required to be normalized by the IRC." Joint Testimony/200, Jenks-Bird-Fuller/6. The Settling Parties then claim that Ms. Blumenthal did not normalize the basis

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[1/] The Settling Parties also argue that Ms. Blumenthal allegedly excluded Pacific Minerals. This is incorrect, as explained in the preceding section.

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difference for Contributions in Aid of Construction. Id. Notably, the Settling Parties fail to identify any specific aspect of Ms. Blumenthal's calculation in which she allegedly did not normalize basis differences. Ms. Blumenthal's statement that basis differences are not required to be normalized is a generic and generally accurate statement, but it does not mean that Ms. Blumenthal failed to normalize any basis differences. Ms. Blumenthal used PacifiCorp's workpapers for her tax calculation and did not change any normalized basis differences that might be included in their original filing. Tr. at 46. In other words, her adjustment includes any basis differences already normalized by PacifiCorp. The Settling Parties' claims are a disingenuous attempt to distort and mischaracterize Ms. Blumenthal's tax calculation.

4. ICNU's Recommendations Are Not Inconsistent with Normalized Taxes in Rates

The Settling Parties argue that Ms. Blumenthal's approach is inconsistent with how the amounts authorized to be collected in rates should be calculated. Joint Testimony/200, Jenks-Bird-Fuller/6-8. The Settling Parties state that the Commission uses fully normalized income taxes in setting rates and that Ms. Blumenthal's exclusion of non-depreciation deferred taxes constitutes improper flow-through accounting which results in "a significant mismatch when compared against taxes authorized to be collected in rates." Id. at 7. ICNU is not advocating flow-through accounting but instead recommends that these deferred taxes be excluded, because PacifiCorp has not met its burden of proof to establish that they are related to regulated operations. Tr. at 51-52. Exclusion of the deferred taxes increases Ms. Blumenthal's proposed small surcredit to a large surcredit. ICNU/100, Blumenthal/12.

PacifiCorp has not demonstrated that all of its deferred taxes are related to costs that are or should be included in rates. Id. The Settling Parties are correct that taxes in the

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Company's rate cases are intended to be fully normalized, but they have not submitted any evidence that demonstrates what is included in PacifiCorp's present rates. Tr. at 51-52. The Settling Parties' testimony does not make this claim, and at the hearing Staff admitted that it has not verified whether the total non-depreciation related deferred taxes were actually included in rates in the last general rate case. Tr. at 82-83. PacifiCorp's deferred taxes have not been reviewed fully in a general rate case or this proceeding, and they should be excluded until the Company has met its burden of proof to establish that they do not include any improper amounts. Tr. at 82-83; ICNU/100, Blumenthal/12.

IV. CONCLUSION

A $13.5 million surcharge is unwarranted and unreasonable because PacifiCorp did not pay any federal income taxes in 2009, and the Settling Parties ignore the Company's negative taxable income when calculating their proposed surcharge. The Settling Parties' tax calculation is not representative of what PacifiCorp's stand-alone tax liability would be if it were not owned by Berkshire Hathaway, but instead allows PacifiCorp's parent company to reap the benefits of its losses. The Commission should recognize that PacifiCorp has negative stand-alone tax liability and calculate its tax report in a manner similar to PGE's 2009 tax report.

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Dated this 11th day of March, 2011.

Respectfully submitted,

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March 11, 2011

Via FedEx and Electronic

Public Utility Commission
Attn: Filing Center
550 Capitol St. NE #215
P.O. Box 2148
Salem OR 97308-2148

Re: In the Matter of OREGON PUBLIC UTILITY STAFF Requesting the Commission direct PACIFICORP, dba PACIFIC POWER & LIGHT COMPANY, to file tariffs establishing automatic adjustment clauses under the terms of SB 408.
Docket No. UE 177

Dear Filing Center:

Enclosed please find an original and six (6) copies of the Opening Brief of the Industrial Customers of Northwest Utilities ("ICNU") in the above-referenced docket.

Please return one file-stamped copy of the Highly Confidential Direct Testimony in the self-addressed, stamped envelope provided.

Thank you for your assistance, and please do not hesitate to contact our office if you have any questions.

Sincerely yours,

/s/ Sarah A. Kohler
Sarah A. Kohler

Enclosure

cc: Service List

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that I have this day served the foregoing Opening Brief on behalf of the Industrial Customers of Northwest Utilities upon the parties, on the service list, by causing the same to be deposited in the U.S. Mail, postage-prepaid, where paper service has not been waived.

Dated at Portland, Oregon, this 11th day of March, 2011.

/s/ Sarah A. Kohler
Sarah A. Kohler

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