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April 13, 2009

Via Electronic and U.S. Mail

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 the original and five (5) copies of the Opening Brief on Reconsideration on behalf of the Industrial Customers of Northwest Utilities in the above-referenced matter.

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

Sincerely yours,

/s/ Allison M. Wils
Allison M. Wils

Enclosures

cc: Service List

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that I have this day served the foregoing Opening Brief on Reconsideration on behalf of the Industrial Customers of Northwest Utilities upon all parties identified on the service list via electronic mail, as agreed upon by all parties on April 2, 2009.

Dated at Portland, Oregon, this 13th day of April, 2009.

/s/ Allison M. Wils
Allison M. Wils

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BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

UE 177

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 ON RECONSIDERATION OF THE INDUSTRIAL CUSTOMERS OF NORTHWEST UTILITIES

April 13, 2009

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I. INTRODUCTION

Pursuant to the schedule set by Judge Grant on April 2, 2009, the Industrial Customers of Northwest Utilities ("ICNU") submits this Opening Brief to the Public Utility Commission of Oregon ("OPUC" or the "Commission"). The Commission is reconsidering whether ICNU properly challenged the validity of OAR § 860-022-0041, the rule implementing Senate Bill ("SB") 408, in this Docket. According to statute and precedent, ICNU not only could but had to challenge OAR § 860-022-0041 in UE 177.

Further, upon reconsideration, the Commission should determine that OAR § 860-022-0041 does not result in the calculation of a utility's *actual* tax expense, as required by SB 408. Rather, the methodology required by OAR § 860-022-0041 produces only hypothetical numbers that do not accurately reflect taxes paid to units of government. Thus, the Commission may not rely on OAR § 860-022-0041 to impose a SB 408 surcharge given that the rule produces a result that is inconsistent with the statute. Accordingly, the Commission must reject PacifiCorp's requested surcharge in this Docket, which has been approved in reliance upon OAR § 860-022-0041.

II. BACKGROUND

Pursuant to ORS § 757.268(1), on October 15, 2007, PacifiCorp filed its tax report for the 2006 tax year with the Commission. On January 22, 2008, Staff and ICNU filed direct testimony concerning the tax report. Staff's testimony focused on whether PacifiCorp's tax report complied with OAR § 860-022-0041. ICNU filed testimony by witness Ellen Blumenthal, primarily focusing on whether

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OAR § 860-022-0041 produced a result that was consistent with SB 408. PacifiCorp filed rebuttal testimony on February 12, 2008.

On February 19, 2008, PacifiCorp submitted a Motion in Limine objecting to Ms. Blumenthal's testimony and requesting that certain portions be stricken. ICNU submitted its response to PacifiCorp's Motion in Limine on February 22, 2008.

On March 3, 2008, ALJ Arlow granted PacifiCorp's Motion in Limine striking a majority of Ms. Blumenthal's Testimony. At the hearing on March 4, 2008, ICNU objected to ALJ Arlow's ruling. ICNU's objection was noted, and Ms. Blumenthal's Testimony (ICNU/100–101) was received and marked and designated as evidence offered, excluded, and to which exception has been taken. Transcript at 30–31. ICNU also offered ICNU/102 into evidence, which detailed exactly which portions of Ms. Blumenthal's Testimony had been stricken. ALJ Arlow excluded ICNU/102. Id. at 34, lines 16–19. ICNU's Counsel made an offer of proof regarding the excluded exhibit, ICNU/102. Id. at 34, lines 24–25, 35, lines 1–2.

On March 20, 2008, the Commission affirmed, in its entirety, the ALJ's decision to strike portions of Ms. Blumenthal's testimony as "irrelevant to this proceeding." Order No. 08-176 at 1. In its final order, the OPUC once more stated that Ms. Blumenthal's testimony was "inappropriate in this proceeding" and resolved to "disregard ICNU's arguments with respect to this issue." Order No. 08-201 at 4–5 (Apr. 11, 2008).

ICNU filed a petition for judicial review of the final order in UE 177 on May 12, 2008. On December 12, 2008, ICNU filed its Opening Brief before the Oregon

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Court of Appeals. However, on March 24, 2009, just three days before Answering Briefs were due, the OPUC made a highly unusual decision and filed a notice of withdrawal of the final order for purposes of reconsideration. Judge Grant held a telephone conference on April 2, 2009, in which the present procedural briefing schedule was established to address ICNU's Assignment of Error No. 2 and, by implication, Assignment of Error No. 1. In sum, the Commission is reconsidering: 1) the propriety of ICNU raising arguments in UE 177 challenging the validity of OAR § 860-022-0041; and 2) whether OAR § 860-022-0041 properly implements the legislative mandates of SB 408.

Moreover, the ALJ determined that relevant portions of Ms. Blumenthal's stricken testimony would be accepted by the Commission in briefing as commentary.[1/] Likewise, responsive portions of PacifiCorp's rebuttal testimony that were not previously admitted are also acceptable in briefing, as commentary.[2/]

III. STANDARD OF REVIEW

Subsequent to the filing of a petition for judicial review and anytime prior to a hearing, ORS § 183.482(6) permits an agency to withdraw an "order for purposes of reconsideration." As explained by the Oregon Court of Appeals, "[t]o reconsider means . . . 'to think over, discuss or debate, * * * especially with a view to changing or

---

1/ That testimony includes: ICNU/100, Blumenthal/3, lines 3–13; Blumenthal/5, lines 1–16; Blumenthal/6, line 23 through Blumenthal/7, line 2; Blumenthal/9, line 3 through Blumenthal/12, line 4; Blumenthal/14, line 19 through Blumenthal/15, line 9.

2/ This testimony includes: PPL/100, Larson/7, lines 1–13; Larson/7, line 17 through Larson/9, line 12; Exhibit PPL/103; Exhibit PPL/104; PPL/200, Fuller/5, line 10 through Fuller/7, line 14; Fuller/8, line 15 through Fuller/9, line 10; Exhibit PPL/204; Exhibit PPL/205.

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reversing.'" Gritter v. Adult & Family Servs. Div., 182 Or App 249, 254 (2002) (quoting Webster's Third New Int'l Dictionary, 1897 (unabridged ed 1993)).[3/]

PacifiCorp has the burden of proof to establish that its proposed rates are fair, just and reasonable. ORS § 757.210(1). The fact that this Docket involves an automatic adjustment clause does not absolve PacifiCorp of its burden of proof, as the Commission may only authorize a rate that is shown to be fair, just and reasonable. Id. In order to meet its burden of proof, PacifiCorp must establish that its rates will "reflect the taxes that are paid to units of government . . . ." ORS § 757.267(f). The burden of proof is borne by PacifiCorp "throughout the proceeding and does not shift to any other party." Re PacifiCorp, OPUC Docket No. UE 116, Order No. 01-787 at 6 (Sept. 7, 2001). When other parties dispute the proposed rates, PacifiCorp retains the burden to show that all its suggested changes are just and reasonable. Id.

After the record has been closed in a proceeding before the Commission, "no additional evidence shall be received except upon the order of the commission and a reasonable opportunity of the parties to examine any witnesses with reference to the additional evidence and otherwise rebut and meet such additional evidence." ORS § 756.558(1). The Commission can delegate any of its duties or powers except, *inter alia*, the authority to "[e]nter orders on reconsideration." ORS § 756.055(2)(d).

[3/] Gritter was later vacated for mootness, but the reasons for vacating did not concern the Court's treatment of reconsideration. See Gritter, 183 Or App 578 (2002).

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IV. ARGUMENT

A. ICNU Properly Challenged the Validity of OAR § 860-022-0041 through Ms. Blumenthal's Testimony, which Should not Have Been Stricken by the Commission

In certain circumstances, agency rules must first be challenged in agency proceedings before the Court of Appeals will review the validity of a rule. ORS § 183.400(1). This is the statutory mandate for parties to an order or contested agency case. This mandate is directly applicable to ICNU, as a party to contested OPUC Case No. UE 177. By repeatedly refusing to even consider ICNU's challenge to OAR § 860-022-0041, the OPUC erred.

1. An Agency Rule Must First be Challenged in Agency Proceedings in Circumstances such as those Affecting ICNU

UE 177 was the first contested case in which OAR § 860-022-0041 was applied.[4/] ORS § 183.400 requires that, in certain circumstances, an agency rule *must first* be challenged in agency proceedings before the Court of Appeals will review a rule's validity. ORS § 183.400 provides, in part:

> (1) The validity of any rule may be determined upon a petition by any person to the Court of Appeals in the manner provided for review of orders in contested cases. The court shall have jurisdiction to review the validity of the rule whether or not the petitioner has first requested the

[4/] PacifiCorp's 2005 tax report filing in October 2006 was not a contested case. In fact, Staff filed a letter on January 18, 2007, informing the Commission that there were no contested issues with respect to PacifiCorp's 2005 tax report. ICNU even filed a letter of its own on January 23, 2007, supporting Staff's position but expressly reserving all arguments when a rate adjustment based on SB 408 actually would be in contest. PacifiCorp witness D. Douglas Larson had to admit, despite his apparent belief that ICNU should have raised its challenges sooner, that "the 2005 tax reports did not produce a rate change." PPL/100, Larson/8, lines 14–15. Notwithstanding Mr. Larson's opinions, ICNU properly complied with Oregon law in first raising its challenges to PacifiCorp's 2006 tax report when OAR § 860-022-0041 was first applied in a contested case.

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> agency to pass upon the validity of the rule in question, *but not when the petitioner is a party to an order or a contested case in which the validity of the rule may be determined by a court*."
>
> (2) The validity of any applicable rule may also be determined by a court, upon review of an order in any manner provided by law or pursuant to ORS 183.480 or upon enforcement of such rule or order in the manner provided by law.

(Emphasis added). Under a plain reading of ORS § 183.400, the validity of an administrative rule may be challenged by either: 1) a petition for review; or 2) a judicial review of any order.

The requirement of an initial agency challenge is not novel. The rules of preservation apply just as equally to judicial review of agency orders as to review of court judgments. To this effect, ORAP § 5.45(1) provides in part: "No matter claimed as error will be considered on appeal unless the claim of error was preserved in the lower court . . . ." This rule was applied to agency review in Lake County v. Teamsters Local Union #223, 208 Or App 271, 277, 145 (2006). See also Baker v. Driver and Motor Vehicle Servs. Div., 201 Or App 310, 313, 118 (2005) (holding that established "rules of preservation apply on judicial review of administrative agency orders").

In sum, ICNU is compelled by ORS § 183.400 to challenge the validity of a rule in OPUC proceedings in order to preserve appellate review. The Oregon Court of Appeals has affirmed such a requirement in Lake County and in Baker. Therefore, far from inappropriately raising a challenge to OAR § 860-022-0041 before the OPUC,

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ICNU was conforming to the mandate of law by challenging the rule in the first contested case in which it was applied: UE 177.

2. The OPUC Contravened Precedent by Refusing to Address ICNU's Repeated Challenges to the Validity of OAR § 860-022-0041

According to the Oregon Court of Appeals, an agency's "contested cases are appropriate proceedings in which to raise even purely legal challenges" to rules. Wheaton v. Kulongoski, 209 Or App 355, 364 n 3 (2006). Thus, in agency proceedings, a party need not ground a rule challenge on a factual or as-applied basis. A facial challenge is both lawful and proper.

The Oregon Supreme Court has ruled that an agency errs by simply assuming, rather than actually considering, the propriety of challenged rules. England v. Thunderbird, 315 Or 633 (1993). In England, a party challenged the validity of three rules in a contested agency proceeding, arguing that the rules were "outside the Director's delegated authority and contrary to" statute. Id. at 636 (internal quotation and citation omitted). The agency ultimately denied the challenge. Id. at 636–37.

The Court, however, held that the agency merely "*assumed* the validity of and relied on" the challenged rules. Id. at 639 (emphasis added). By only assuming the validity of the challenged rules, the agency had effectively refused to *actually* consider the rules as the challenging party had requested. Consequently, the Court held that the agency decision was "erroneous," and reversed and remanded. Id. at 639–40.

The holding in England is directly applicable to UE 177. By merely assuming the validity of OAR § 860-022-0041—and not actually considering the rule,

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despite ICNU's repeated challenges—the OPUC erred in the same manner as the agency in England.

The record contains three separate examples of the OPUC (including the ALJ acting pursuant to delegation from the Commission) refusing to consider ICNU's challenges to the validity of OAR § 860-022-0041. First, on March 3, 2008, ALJ Arlow issued a ruling granting PacifiCorp's motion in limine objecting to the testimony of ICNU witness Ellen Blumenthal. The ALJ expressly adopted PacifiCorp's argument that the OPUC strike Ms. Blumenthal's testimony "on the grounds that they consist of irrelevant arguments that attack the validity of OAR 860-022-0041." Ruling at 5. Testimony that the ALJ refused to consider included a claim by Ms. Blumenthal that tax calculations required by the Rule "do not meet the goal of SB 408." Id. (citing ICNU/100, Blumenthal/3). The ALJ also refused to admit testimony "that the Commission's rules do not operate as intended and as required by SB 408." Id. (citing ICNU/100, Blumenthal/12).

Next, the Commission itself, upon review of ALJ Arlow's ruling, similarly refused to consider ICNU's arguments challenging the validity of OAR § 860-022-0041. Specifically, the Commission affirmed the ALJ's ruling that challenges to the rule were "irrelevant." Order 08-176 at 1. Moreover, the OPUC affirmed the ALJ's ruling "in its entirety"—the ALJ's ruling itself being a grant of PacifiCorp's motion "in its entirety." Id. Thus, the OPUC expressly adopted all of the very same rationales advanced by the ALJ and PacifiCorp in refusing to consider ICNU's rule challenges.

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Furthermore, the OPUC held that Ms. Blumenthal's testimony "constitutes a collateral attack" upon OAR § 860-022-0041, and that such a challenge to the rule's validity was "not appropriate." Id. at 3. According to the Commission, "public interest" was not served by ICNU presenting testimony concerning "failings of a rule's interpretation of a statute." Id. The OPUC maintained that the failings of a rule could only be "properly offered in support of a petition to amend [an] existing rule in a *separate* rulemaking proceeding." Id. (emphasis added). By so holding, the OPUC utterly rejected ICNU's contention that the stricken testimony "gives the Commission the factual evidence necessary to make a reasoned explanation as to why OAR § 860-022-0041 is inconsistent with SB 408." Motion for Expedited Consideration of ICNU at 10 (Mar. 13, 2008). In sum, the OPUC refused to consider the validity of OAR § 860-022-0041 in the light of failings *only apparent through actual application involving individualized facts*.

Finally, beyond just the testimony of Ms. Blumenthal, in its final order the Commission refused to consider *any* manner of challenge to OAR § 860-022-0041. The OPUC acknowledged that ICNU challenged the rule on the basis of the rule's non-compliance with SB 408. Order No. 08-201 at 4. Indeed, the OPUC explicitly acknowledged the findings of Staff who "agree[] with ICNU regarding *the rule's infirmity*." Id. at 6 (emphasis added). Nevertheless, the Commission refused to actually consider ICNU's challenge, merely assuming the validity of OAR § 860-022-0041—the exact error proscribed by England. Id. at 4–5. Ultimately and erroneously, the OPUC simply concluded: "We disregard ICNU's arguments." Id. at 5.

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According to Wheaton and England, OPUC cases are appropriate proceedings in which to raise all manner of rule challenges. In refusing to consider Ms. Blumenthal's testimony and ICNU's challenge to the validity of OAR § 860-022-0041, the OPUC ignored Oregon precedent. More importantly, the Commission has denied ICNU its federal due process rights in refusing to hear legitimate challenges, which were made in both the proper forum and at the proper time. US Const, Amend XIV, § 1.[5/] ICNU urges the OPUC to find that OAR § 860-022-0041 may be properly challenged in this Docket.

B. OAR § 860-022-0041 does not comply with SB 408

Whether PacifiCorp's tax report complies with OAR § 860-022-0041 is not the key issue in this case. Rather, if the rule does not comply with SB 408, then the Commission has no basis on which to order a rate change based on PacifiCorp's tax report. As stated in ICNU's Direct Testimony, it has become apparent that the application of OAR § 860-022-0041 to PacifiCorp's tax report produces a result that does not comply with SB 408. Moreover, in a broader sense, it should be concerning to the Commission that PacifiCorp has been awarded surcharges of over $20 million through the 2006 and 2007 Tax Report true-up processes, all the while maintaining that it is *under-earning* well below its Return on Equity rate. That OAR § 860-022-0041 provides a means for PacifiCorp to claim that it is under-earning *and* to still collect surcharges for

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[5/] The Commission has apparently reversed its earlier decision granting PacifiCorp's Motion in Limine; Judge Grant orally informed the parties that the Commission was procedurally changing its position on the Motion in Limine and the earlier stricken evidence will now be admitted. Nevertheless, no written order has yet been issued, raising serious procedural propriety issues. See Part IV.D, infra.

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under-collection from ratepayers evinces an absolute and fundamental disconnect between operation of SB 408 and the Commission's rule.

The provisions in ORS §§ 757.267 and 757.268 are simple and straight forward. "Utility rates that include amounts for taxes should reflect the taxes that are paid to units of government to be considered fair, just, and reasonable." ORS § 757.267 (1)(f). The automatic adjustment clause under SB 408, by its terms, applies only to the difference between: 1) actual taxes paid to governmental authorities that are properly attributed to regulated operations of the utility; and 2) taxes collected in rates. ORS § 757.268(6).

A correct understanding of both the text and context of ORS § 757.268(6) is critical to assessing the validity of OAR § 860-022-0041. The section provides, in its entirety:

> The automatic adjustment clause shall account for all taxes paid to units of government by the public utility that are properly attributed to the regulated operations of the utility, or by the affiliated group that are properly attributed to the regulated operations of the utility, and all taxes that are authorized to be collected through rates, so that ratepayers are not charged for more tax than:
>
> (a) The utility pays to units of government *and* that is properly attributed to the regulated operations of the utility; or
>
> (b) In the case of an affiliated group, the affiliated group pays to units of government *and* that is properly attributed to the regulated operations of the utility.

(Emphasis added).

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First, it is plain that the legislature created conjunctive requirements within subsections (a) and (b). The second conjunctive clauses are identical, providing that ratepayers are not to be charged for more tax than a utility or its affiliated group actually pays to units of government "and that is properly attributed to the regulated operations of the utility." On a fair reading of the text, the second conjunctive clause *acts to modify or limit* the first clause. That is, ratepayers cannot be simply charged for all tax amounts paid by utilities. Rather, ratepayers can only be charged for those amounts of taxes that are actually paid *and* that are properly attributed to the regulated operation of the utility. The "proper attributed" clause limits the amount of actual taxes paid in the first clauses by excluding taxes paid on non-regulated utility operations and/or taxes paid by utility affiliates.

To read the "properly attributed" clause in any other fashion—i.e., as expansive and not limiting, permitting ratepayers to be charged *for more tax* than the utility actually paid—would negate the first clause altogether and make nonsense of the legislature's chosen wording. If the legislature meant for properly attributed taxes to mean hypothetical taxes, such that "proper" attribution could exceed actual tax payments and make them irrelevant, it would not have included a conjunctive requirement in ORS § 757.268(6)(a) and (b). Merely stating the proper attribution clause would have been sufficient. Therefore, the expansive construction of what the legislature *intended* by "properly attributed" can only be maintained if the legislature's chosen *text* in ORS § 757.268(6) is willfully ignored.

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An expansive reading of the "properly attributed" clause also ignores the entire context of SB 408. ORS § 757.268(13)(f) defines "taxes paid" as "*amounts received* by units of government from the utility of the affiliated group of which the utility is a member." (Emphasis added). Since ORS § 757.268(6) does not allow ratepayers to be "charged for more *tax*" than a utility or its affiliated group "*pays* to units of government," the definition of "taxes paid" is plainly relevant. Based on the definition of taxes paid provided in statute, ORS § 757.268(6) must mean that ratepayers are not to be charged for more tax than is actually paid to units of government, that is, "amounts received by units of government." ORS § 757.268(13)(f). To construe the "properly attributed" clause as allowing ratepayers to be charged for hypothetical tax calculations that exceed amounts actually received by units of government makes a mockery of the defined terms of SB 408. Such a construction ignores the context of SB 408 and is invalid.

The only exceptions to actual taxes paid amounts are explicitly provided for in SB 408. In order to avoid a violation of the normalization provisions in the Internal Revenue Code, the tax depreciation deduction is replaced with straight line depreciation and investment tax credits are normalized. The tax benefit of any deduction taken by the utility for charitable contributions is to remain with the utility. These requirements of SB 408 are illustrated by the following flowchart:

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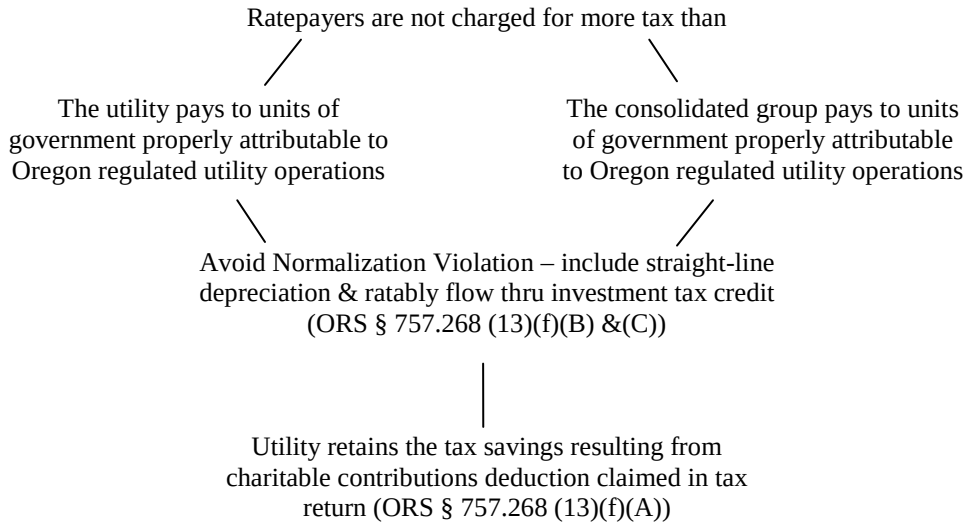
SB 408



OAR § 860-022-0041 not only unnecessarily complicates the calculation of the actual taxes paid by a utility on its regulated operations, but also does not comply with ORS §§ 757.267 and 757.268. The actual taxes paid calculations required by ORS §§ 757.267 and 757.268 in no way resemble the hypothetical OAR § 860-022-0041 income tax calculations currently used to calculate the income tax true-up required by SB 408. "The under collection of taxes reflected in PacifiCorp's tax report does not represent the difference between actual taxes paid . . . and the taxes PacifiCorp has collected through rates from its customers." ICNU/100, Blumenthal/3, lines 4–7; see also ICNU/100, Blumenthal/7, lines 1–2; ICNU/100, Blumenthal/14, lines 21–22. Indeed, "[n]one of the calculations required by [OAR § 860-022-0041] is an actual tax calculation." ICNU/100, Blumenthal/3, lines 9–10; see also ICNU/100, Blumenthal/6, line 23 and Blumenthal/7, line 1. Such results are an absolute violation of SB 408. "SB 408 requires this Commission to track the amount of taxes *actually paid* and

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determine what portion of those amounts are properly attributed to the regulated operations of the utility." Re Adoption of Permanent Rules to Implement SB 408 Relating to Utility Taxes, Docket No. AR 499, Order No. 06-532 at 1 (Sept. 14, 2006) (emphasis added) ("Order No. 06-532").

SB 408 is intended to ensure that if consolidated tax savings reduce the amount of taxes actually paid to governmental authorities, they are passed on to customers. See ORS § 757.267(b) (utility tax liability is "affected by the operations or tax attributes of the parent company"); ORS § 757.267(d) (consolidated tax return rules result in a difference between taxes paid and taxes collected). If OAR § 860-022-0041 does not produce an actual taxes paid result that includes consolidated tax savings, operation of the automatic adjustment clause would be illegal, and rates established will not be "fair, just and reasonable." ORS § 757.267(1)(f); see also, Re Adoption of Permanent Rules to Implement SB 408 Relating to Utility Taxes, Docket No. AR 499, Order No. 06-400 at 3 (July, 14, 2006) (Commission's method must ensure rates are fair and reasonable). The current methodologies prescribed by OAR § 860-022-0041 do not produce an actual taxes paid result and, therefore, do not ensure "fair, just, and reasonable" rates. ORS § 757.267(1)(f).

> ORS § 757.268(12) provides:
>
> For purposes of this section, taxes 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; or

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> (b) The total amount of *taxes paid to units of government* by the utility or by the affiliated group, whichever applies.

(Emphasis added.)

Thus, the actual taxes paid to units of government that are properly attributed to the regulated operations of the utility cannot be more than the taxes actually paid on the utility's regulated operations (subsection (a)), or the utility's share of the total taxes paid by the consolidated group that are attributable to regulated utility operations (subsection (b)). ORS § 757.268 plainly requires that reconciliation of taxes collected through rates and "taxes paid" *begin* with the actual taxes paid—not with a hypothetical calculation or liability.

None of the methodologies in OAR § 860-022-0041, however, calculate actual taxes paid, as required by the statute. See ICNU/100, Blumenthal/5, lines 15–16; ICNU/100, Blumenthal/3, lines 9–10; ICNU/100, Blumenthal/6, line 23 and Blumenthal/7, line 1; Transcript at 74, line 24 through 75, line 10. Rather, the Commission's rules involve hypothetical calculations that do not produce the actual taxes PacifiCorp paid to governmental authorities that are attributable to regulated utility operations. See ICNU/100, Blumenthal/7, lines 16–18 (stand alone method is a "hypothetical" calculation); ICNU/100, Blumenthal/6, line 23 (stand alone method is not an "actual tax" calculation).

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1. The Stand Alone Method does not Produce an Actual Taxes Paid Result

The definition of "stand alone tax liability" is unnecessarily complicated and does not produce an actual taxes paid calculation. See ICNU/100, Blumenthal/7, line 5, 13 (PacifiCorp's stand alone "calculation is not simple" and involves "unnecessary" calculations); ICNU/100, Blumenthal/6, line 23 (stand alone method does not produce "an 'actual tax' calculation").

OAR § 860-022-0041(2)(p) defines "stand-alone tax liability" as:

> [T]he amount of income tax liability calculated using a pro forma tax return and revenues and expenses in the utility's results of operations report for the year, except using zero depreciation expense for public utility property, excluding any tax effects from investment tax credits, and calculating interest expense in the manner used by the Commission in establishing rates.

ORS § 757.268(12)(a) already contains a definition for stand alone tax liability that requires an actual tax calculation: "[t]hat portion of the total taxes paid that is incurred *as a result of income generated* by the regulated operations of the utility[.]" (Emphasis added).

a. The Use of a Pro Forma Tax Return does not Produce an Actual Taxes Paid Result

Under the Commission's rules, the stand alone method utilizes a pro forma tax return. The use of a pro forma tax return is curious, as the 2006 tax year is a historical period for which an actual tax return already exists. ICNU/100, Blumenthal/6, lines 11–16. Even if taxes are filed on a consolidated basis, a tax return is prepared for

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each entity in the consolidated group. Id. at lines 15–16.[6/] The pro forma tax figures used by the Commission are based on book net income and is the same tax calculation used to set rates, which is then reconciled with the utility's reported taxable income using Schedule M-1. These are referred to as "Schedule M" adjustments. ICNU/100, Blumenthal/7, at lines 5–10. ORS §§ 757.267 and 757.268 make no provision for Schedule M adjustments.

PacifiCorp witness Ryan Fuller asserts that "Ms. Blumenthal's position is based on both an incorrect premise and a misreading of the Oregon statute and the Commission's rules." PPL/200, Fuller/8, lines 2–3. Mr. Fuller bases his assertion on the premise that the Commission's rules require the determination of taxes paid for "Oregon regulated operations." Id. at lines 3–5. ICNU does not dispute that only the regulated operations of PacifiCorp are to be considered. SB 408, however, plainly requires an actual tax calculation through the use of *taxable income* produced by Oregon regulated operations. While the use of pro-forma results of operations and Schedule M adjustments may be the most convenient method for PacifiCorp, convenience cannot overcome the plain language of the statute. Because OAR § 860-022-0041 uses the pro forma return to establish the cap of taxes paid and properly attributed under SB 408, using hypothetical figures to modify actual tax payment amounts, the rule is invalid.

[6/] Not only are individual tax returns necessarily prepared for each corporation included in a consolidated group (or else a consolidated return could never itself be created), but consolidated returns also contain schedules summarizing each affiliated corporation's individually prepared return. Any contention that pro forma returns are necessary to apportion properly attributed tax payments misunderstand how utilities file taxes.

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b. Use of the Interest Synchronization Method does not Produce a Figure for the Actual Interest Expense

Utilities do not use the interest synchronization method to calculate the interest deduction on their actual tax returns. ICNU/100, Blumenthal/6, lines 16–18. The use of the interest synchronization method veers the stand-alone method even farther from a determination of an actual taxes paid result. Mr. Fuller states that PacifiCorp originally used an actual interest calculation, but switched to the interest synchronization method at Staff's request and ICNU never objected. PPL/200, Fuller/9, lines 13–23; Fuller/10, lines 1–2. ICNU, however, objects to the Commission's rules regarding the stand-alone method as a whole. Even if PacifiCorp used an actual interest calculation, the Commission's rules would still fail to produce an actual tax calculation. Mr. Fuller's statements are thus immaterial to whether the Commission's rules comply with SB 408.

Staff acknowledges that the interest synchronization method does not produce an actual tax result. In its rebuttal testimony, Staff states that the Commission's rules should be changed "to more closely resemble the interest deduction available to the Company on a pro forma tax return." Staff/200, Owings-Ball/6, lines 17–20. Although Staff's recommendation is still based on a pro forma tax return, Staff concurs with Ms. Blumenthal that the Commission's rules need to be amended to more "accurately approximate the tax liability." Id. at line 17.

c. Customers Must be Given the Benefit of Depreciation

Although the removal of the accelerated tax depreciation expense for public utility property from the calculation is required to avoid a normalization violation,

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depreciation expense should be included on a straight line basis in order to produce an actual tax result. ICNU 100/Blumenthal 6, lines 18–23; ICNU 100/Blumenthal 15, lines 6–7. Mr. Fuller asserts that "a review of pages 2 and 6 of the tax report template demonstrates that depreciation expense is properly reflected in the stand alone calculation." PPL/200, Fuller/10, lines 11–13. OAR § 860-022-0041(2)(p), however, specifically states that zero depreciation expense shall be used for public utility property. In addition, it is unclear from the Staff tax report template that Mr. Fuller refers to whether depreciation is added back, as the template only specifically requires PacifiCorp to add back the tax benefit of tax depreciation on public utility property. PPL/201, page 5, lines 6, 15, and 24; Transcript at 71, lines 18–24. As stated by Ms. Blumenthal at the hearing, "The template is not clear. There is not a line item that says, Plus straight-line depreciation." Transcript at 72, lines 21–22.

In testimony, Staff simply asserted that there is no normalization violation from this treatment of depreciation. Staff/200, Owings-Ball/4, lines 21–22; Owings-Ball/5, lines 1–13.[7/] Ms. Blumenthal acknowledges that removal of accelerated tax depreciation expense is required to avoid a normalization violation, but is of the opinion that straight line depreciation on public utility property must be added back to produce an actual tax calculation. ICNU 100/Blumenthal 6, lines 18–23. It is simply not apparent

[7/] In its Response Brief, Staff only reiterated the contention of PacifiCorp that tax benefit depreciation is deducted from tax liability—not squarely addressing Ms. Blumenthal's concern that the template lacks the necessary addition of straight-line depreciation. Page 2, lines 15–20 (Mar. 19, 2008).

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that the Commission's rules require this step and there is no evidence in the record specifically showing that this step occurred.

d. Consolidated Tax Savings Must be Included

Use of the stand-alone tax methodology excludes any consolidated tax savings. ICNU/100, Blumenthal/6, lines 21–22; cf. Blumenthal/15, lines 5–6 (PacifiCorp's tax report "should include the utility's share of consolidated tax savings"). Without the inclusion of consolidated tax savings, the use of the stand-alone methodology fails to ensure that ratepayers will not pay more than the taxes paid by the affiliated group that is properly attributed to the regulated operations of the utility, as required by SB 408. ORS § 757.268(6). Staff agrees that customers do not benefit from consolidated tax savings through the stand-alone method. Staff, however, does not agree that SB 408 requires recognition of consolidated tax savings. Staff/200, Owings-Ball/3, lines 1–7. Consolidated tax savings is precisely the reason that such large amounts of taxes that are collected are never paid to governmental authorities, and was the primary reason why SB 408 was adopted. ORS § 757.267(b)–(d). Without the inclusion of consolidated tax savings, the Commission's rules simply maintain the "status quo," which is exactly what SB 408 was intended to correct. See Senate Committee Hearing at 23 (June 8, 2005) (Statement of Sen. Rick Metsger).

e. Publicly Available Information from PacifiCorp's 2006 10-K Illustrates that the Commission's Rules do not Comply with SB 408

In PacifiCorp's 10-K, filed with the Securities and Exchange Commission on March 1, 2007, PacifiCorp's financials for the nine-months ending December 31,

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2006 are listed. PacifiCorp 10-K at 55.[8/] PacifiCorp's 10-K reveals that 28.5% of PacifiCorp's retail electric revenues are attributable to Oregon. Id. at 12. As illustrated in the table below, this produces a stand-alone result of only $23 million for Oregon regulated operations, far less than the amount reached under the Commission's rules in this Docket.

Per 2006 10-K Page 55
(In Millions)

	Financials	Oregon Tax (28.5%) [(2)]
Revenues	$2,924	$833
Total Expenses	(2,509)	(715)
Energy Costs	(1,297)	(370)
O&M	(780)	(222)
Depreciation [(1)]	(355)	(101)
Other Taxes	(77)	(22)
Income From Operations	415	118
Interest Expense	(215)	(61)
Interest Income	6	2
AFUDC Equity	18	----
AFUDC Debt	17	----
Other	5	1
Income Before FIT	246	60
Income Tax	(86)	(23) [(3)]
Net Income	161	37

Notes:
(1) Depreciation is straight-line.
(2) Oregon 28.5% of retail electric revenues according to page 12 of 10-K for 9 months ended 12-31-2006.
(3) Computed at 38.5% based on information on page 76 of Form 10-K.

Therefore, use of the Commission's stand alone method produces a result that simply does not reflect the amount of taxes actually paid to governmental authorities. Use of actual income produces a result that complies with SB 408.

8/ PacifiCorp's 10-K is available electronically at: http:www.pacificorp.com/File/File73269.pdf.

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2. The Apportionment Method is Incorrectly based on Total Taxes Paid by the Consolidated Taxpayer and the Commission's Three-Factor Methodology

The Apportionment Method must ensure that ratepayers are not charged for more tax than the "affiliated group pays to units of government and that is properly attributed to the regulated operations of the utility." ORS § 757.268(6)(b). The actual amount of taxes paid and properly attributed to the regulated operations of the utility is a function of taxable income. Therefore, taxable income should be the basis for apportioning the total taxes paid to units of government that are properly attributable to the regulated operations of the utility, as required by SB 408. ICNU/100, Blumenthal/8, lines 10–12. The apportionment methodologies required by the Commission's rules do not produce an actual taxes paid result.

In short, the Apportionment Method violates SB 408 in at least two critical ways. First, the pro forma return is used as the starting point to calculate the Apportionment Method floor under OAR § 860-022-0041(3)(b) and (d). As already explained, the pro forma return by its nature produces hypothetical calculations, while SB 408 requires calculations from actual taxes paid. This fact alone invalidates the Apportionment Method. However, the invalidity of the Apportionment Method is compounded by OAR § 860-022-0041(4), which requires that the Apportionment Method calculation be compared to amounts calculated under the stand-alone liability. Since the stand-alone liability is itself a product of the pro forma tax return, and based on hypothetical calculations, this comparison violates SB 408.

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Further, using the amount of taxes paid by Berkshire Hathaway as the starting point and applying the Commission required three-factor methodology will allocate too much of the consolidated tax liability to PacifiCorp. INCU/100, Blumenthal 7, lines 25–26; Blumenthal/8, lines 6–9; Blumenthal/9, lines 6–10. The consolidated structure of Berkshire Hathaway consists of over 400 companies, most of which are significantly less capital intensive than PacifiCorp. Under the Apportionment Method, PacifiCorp's share of the total consolidated tax liability is allocated based on three factors: 1) gross plant; 2) wages and salaries; and 3) sales. OAR § 860-022-0041(3)(a)(B); Order No. 06-532 at 2–3. This is the same methodology used to determine the state income tax of multi-state corporations. However, it has nothing to do with determining the total federal income taxes paid by a taxpayer attributable to regulated utility operations.

Use of the three-factor methodology to determine the amount of taxes properly attributable to PacifiCorp, however, places too much emphasis on capital, wages and salaries, and sales. Regardless of how much taxable income PacifiCorp actually generates compared to the consolidated group (even if PacifiCorp produces a net loss), use of the three-factor methodology will not assign a reasonable amount of the consolidated taxes paid to PacifiCorp. INCU/100, Blumenthal 9, lines 3–15 and Table 1. Because PacifiCorp is one of, if not the most capital-intensive business in Berkshire Hathaway's consolidated group (including companies such as fast-food restaurants and other retail stores), this method will never reflect the actual amount of taxes that PacifiCorp actually paid to governmental authorities on its regulated operations.

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ICNU/100, Blumenthal/8, lines 1–9. Staff seems to agree with Ms. Blumenthal's analysis. See Staff/200, Owings-Ball/7, lines 10–16 (Staff does not agree with the use of taxable income "at least for purposes of this filing").

PacifiCorp does not dispute that the Apportionment Method places a large emphasis on capital. See PPL/200, Fuller/11, lines 11–16 (PacifiCorp's apportionment of the consolidated group could decrease if Berkshire Hathaway adds other capital-intensive companies to the consolidated group). In his rebuttal, Mr. Fuller focuses on only the property factor of the three-factor method, but Ms. Blumenthal's opinion is that all three factors cause the over-allocation of consolidated tax liability to PacifiCorp. PPL/200, Fuller/12 at 14–17. Moreover, Mr. Fuller criticizes Ms. Blumenthal because she has produced no evidence in discovery to support her conclusion. ICNU, however, requested such information from PacifiCorp, and PacifiCorp refused to produce such information. See ICNU/200–204 (examples of PacifiCorp refusing to provide data).

Finally, Mr. Fuller mischaracterizes Ms. Blumenthal's opinion as focusing on results and not the methodology. PPL/200, Fuller/12, lines 18–20. Nothing could be further from the truth. Ms. Blumenthal's opinion is that the Apportionment Method does not produce an actual taxes paid result. ICNU/100, Blumenthal/11, lines 1–14. Whether or not the actual taxes paid result produces a surcharge or credit is not the issue.

3. The Consolidated Method does not Produce an Actual Taxes Paid Result and will Always Produce the Greatest Value of the Three Methods

Like the Apportionment Method, the Commission's consolidated method is also based on the taxes paid by the consolidated taxpayer, with the add back of the tax

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benefits of accelerated depreciation and investment tax credits. ICNU/100, Blumenthal/8, lines 16–18. The Commission's consolidated method will never represent taxes actually paid to governmental authorities in PacifiCorp's case because PacifiCorp is consolidated with hundreds of other entities. Apportioning the total tax liability of the consolidated group using the Commission's three factor method does not produce an amount that can be described as the actual taxes paid on PacifiCorp's regulated operations. The Commission's consolidated method will never be the method relied upon as long as PacifiCorp is owned by Berkshire Hathaway, because it will always produce the greatest result. Id. at lines 18–22.

C. The Commission has the Authority to Disallow the Stipulation Surcharge in this Case

ICNU recommends that the Commission deny continued surcharge recovery to PacifiCorp. Based on OAR § 860-022-0041, the surcharge does not reflect the amount of taxes paid to governmental authorities and properly attributed to the regulated operations of the utility. If adherence to OAR § 860-022-0041 violates the terms of SB 408, the Commission had no authority to issue its final order.

ICNU is aware of no cases that stand for the proposition that an agency cannot reject its own rules if it finds those rules violate the agency's statutory authority.[9/]

[9/] Nevertheless, PacifiCorp's witnesses seem to contend that the Commission cannot depart from its rules. When asked whether the Commission could delay a ruling in UE 177, Mr. Larson answered with an unqualified "No." PPL/100, Larson/9, lines 6–7. As authority for his proposition, Mr. Larson simply cited OAR § 860-022-0041. Id. at lines 7–10. Similarly, Mr. Fuller refutes the assertion that PacifiCorp's stand-alone calculation does not produce an actual tax number by contending that the stand-alone calculation is "defined in Oregon rules." PPL/200, Fuller/8 line 15 through Fuller/9, line 4. Such tautological reasoning, that the Commission must act or is

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In fact, in the exercise of its discretion, an agency is specifically authorized to act inconsistently with a rule, position, or prior practice if the inconsistency is explained by the agency. ORS § 183.482(8)(b)(B). If an agency adequately explains its reasoning for departing from its rule, position, or practice, a reviewing court has no basis for overturning the agency's decision. Gordon v. Board, 343 Or 618, 634–35 (2007).

Indeed, in Docket No. UE 170, the Commission recognized that it must follow the law. In that Docket, the Commission ordered an immediate reduction in the amount of taxes included in PacifiCorp's rates based on the passage of SB 408. Re PacifiCorp, Order No. 05-1050 at 17–19 (Sept. 28, 2005). Despite a long-standing Commission practice of setting the amount of taxes includable in rates on a stand-alone basis, the Commission recognized it no longer had the statutory authority to set rates on that basis due to the passage of SB 408. Id. at 18.

In addition, the Commission recently argued to the Oregon Court of Appeals that it is not required to follow its own rules when to do so would violate its statutory authority. Brief of Respondent at 24–25, Crooked River Ranch Water Co. v. Pub. Util. Comm'n of Oregon, 224 Or App 485 (2008) (CA A134177). One question presented in Crooked River was whether OAR § 860-036-0412 required the telephone number of each member of Crooked River Ranch Water Company petitioning the OPUC for regulation to be listed on the member's petition. The Commission's rule states that "[p]etitions *must*… include the member's . . . telephone number . . . ." OAR § 860-036-

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justified by mere reference to its rules, cannot stand in the face of contradictory statutory provisions.

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0412(3) (emphasis added). Yet, despite the requirements of this rule, the Commission argued that enforcement of this requirement "would itself be invalid, and would exceed any rulemaking authority granted by ORS 757.063 . . . which requires PUC to count any and every petition that is filed by an association's members." Brief of Respondent at 24, Crooked River, 24 Or App 485 (CA A13477) (internal quotation marks omitted). Although the Commission characterized its argument as an interpretation of its own rules rather than a waiver, it is clear the Commission recognizes that it cannot act contrary to its statutory authority, regardless of what its rules may provide.

ICNU requests that the Commission waive the operation of OAR § 860-022-0041 in this Docket in order to avoid further violating SB 408. In brief, "the amount reflected in PacifiCorp's tax report, based on OAR § 860-022-0041, does not comply with SB 408." ICNU/100, Blumenthal/3, lines 10–11. The Commission is only "a legislative agency and has only those powers granted it by the legislature." Advanced TV & Video v. Qwest Corp., OPUC Docket No. UC 454, Order No. 00-572 at 5 (Sep. 19, 2000). Allowing PacifiCorp to continue to collect a surcharge based on application of OAR § 860-022-0041 permits PacifiCorp to collect rates proscribed by SB 408. See ICNU/100, Blumenthal/14, lines 21–25; 15, lines 1-2. (PacifiCorp's tax report should be rejected or a recalculation made of taxes paid since the report "does not provide a calculation of actual taxes paid"). As a result, the Commission has adequate reason to act contrary to OAR § 860-022-0041.

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D. The Entire UE 177 Proceeding is Flawed because Additional Evidence has not been Properly Admitted into the Record

ORS § 756.558(1) requires that, once the record has been closed in a proceeding, "no additional evidence shall be received except upon the order of the commission and a reasonable opportunity of the parties to examine any witnesses with reference to the additional evidence and otherwise rebut and meet such additional evidence." On April 2, 2009, Judge Grant orally informed the parties that PacifiCorp's Motion in Limine is now denied and the earlier stricken evidence will now be admitted. However, while the decision to procedurally reverse the grant of the Motion in Limine is commendable, the admission of the stricken evidence is flawed on two accounts.

First, "the commission may not delegate . . . the authority to: . . . (d) Enter orders on reconsideration." ORS § 756.055(2). In this Docket, because the current proceedings are a reconsideration of Order No. 08-201, the Commission cannot have legally delegated authority to Judge Grant to issue an order reopening the record to admit any additional evidence.[10/] Second, ORS § 756.558(1) further requires that no additional evidence shall be received except upon "a reasonable opportunity of the parties to *examine any witnesses* with reference to the additional evidence and otherwise rebut and meet such additional evidence." (emphasis added).As should be apparent, ICNU has not had any opportunity to cross-examine witnesses regarding the testimony that was

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[10/] The Commission recently determined that, pursuant to ORS § 756.055(1), an ALJ had the delegated authority to reopen the record in Docket No. UE 196—a reopening not based on reconsideration. Order No. 09-046 (Feb. 5, 2009). The Commission explicitly contrasted the ALJ's authority to reopen the record in UE 196 with duties and powers that could not be delegated according to ORS § 756.055(2), including the authority to "enter orders on reconsideration." Id. at 4 n 8.

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previously stricken—certainly not in earlier proceedings, when the testimony had been stricken, nor at the present with no hearing scheduled on the reconsideration. In sum, though the Commission appears to have rightly reversed its decision to strike Ms. Blumenthal's testimony, that testimony still has not been properly admitted into the record.

V. CONCLUSION

Upon reconsideration, the OPUC should determine that it improperly contravened statute and precedent by refusing to regard the challenges posed by ICNU to OAR § 860-22-0041. Further, the Commission should cease from further reliance on OAR § 860-22-0041, because the rule is inconsistent with SB 408. The rule does not produce an actual taxes paid result. The surcharge ordered in this Docket should be immediately vacated, because the surcharge was calculated via OAR § 860-22-0041. Thus, the imposition of the surcharge based on a legally flawed rule violates SB 408. Finally, the entire proceeding in UE 177 is also flawed because additional evidence has still not been properly admitted into the record. While Judge Grant stated that Ms. Blumenthal's testimony will be deemed "comment" and admitted into the record, no such order has been issued. ICNU challenges the OPUC's legal authority under the Administrative Procedures Act to proceed in this fashion.

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Dated this 13th day of April, 2009.

Respectfully submitted,

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