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March 14, 2008

Via Electronic and US 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 Industrial Customers of Northwest Utilities' Opening Brief in the above-referenced matter.

Thank you for your assistance.

Sincerely yours,

/s/ Brendan E. Levenick
Brendan E. Levenick

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, shown below, on the official service list by causing the foregoing document to be deposited, postage-prepaid, in the U.S. Mail to those parties which have not waived paper service, and service via electronic mail to all parties.

Dated at Portland, Oregon, this 14th day of March, 2008.

/s/ Brendan E. Levenick
Brendan E. Levenick

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(W) = Paper Service Waived

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 OF THE INDUSTRIAL CUSTOMERS OF NORTHWEST UTILITIES'

Pursuant to the Prehearing Conference Memorandum issued on November 7, 2007, the Industrial Customers of Northwest Utilities ("ICNU") submits this Opening Brief to the Oregon Public Utility Commission ("OPUC" or the "Commission"). The Commission's rules implementing SB 408, OAR § 860-022-0041, do not result in the calculation of a utility's *actual* tax expense. Rather, the methodology required by OAR § 860-022-0041 produces only hypothetical numbers that do not accurately reflect taxes paid to units of government, as required by SB 408. 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.

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I. BACKGROUND

Pursuant to ORS § 757.268(1), on October 15, 2007, PacifiCorp filed its tax report for the 2006 tax year with the Commission. A prehearing conference was held on November 5, 2007, setting the procedural schedule for this Docket. ICNU attempted to review PacifiCorp's tax report under the safe room procedures ordered by the Commission in Order No. 06-033, but was unable to conduct a meaningful review due to the limited access to the necessary data. As a result, on December 14, 2007, ICNU filed a Motion to Modify the Protective Order. The Commission denied ICNU's Motion in Order No. 08-002. ICNU also filed a Motion to Compel on December 24, 2007, after PacifiCorp repeatedly refused to produce information regarding the affiliated group of which PacifiCorp was a part. That motion was also denied by the Commission in Order No. 08-003.

On December 19, 2007, Staff filed a report detailing its initial findings regarding PacifiCorp's tax report and ICNU circulated an issues list. A settlement workshop was held on January 7, 2008. No settlement was reached between the parties.

On January 22, 2008, Staff and ICNU filed direct testimony. 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 OAR § 860-022-0041 produced a result that was consistent with SB 408. PacifiCorp filed rebuttal testimony on February 12, 2008.

The hearing in this Docket was originally scheduled for February 22, 2008. Two business days before the hearing, on February 19, 2008, PacifiCorp submitted

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a Motion in Limine objecting to Ms. Blumenthal's testimony and requesting that certain portions be stricken. On February 19, 2008, ICNU informed the Commission and other parties of its intent to waive cross-examination. On February 20, 2008, Staff also informed the Commission and other parties of their intent to waive cross-examination. PacifiCorp, however, stated its intent to cross-examine ICNU witness Ellen Blumenthal whether or not its Motion in Limine was granted. The day before the hearing on February 21, 2008, Ms. Blumenthal encountered flight delays due to the weather and was unable to attend the scheduled hearing. ICNU, PacifiCorp, and ALJ Arlow conducted a telephone conference to discuss how to proceed, and established a new hearing date of March 4, 2008, for cross-examination of Ms. Blumenthal. During this telephone conference, Judge Arlow requested that ICNU be prepared to respond to the Motion in Limine at the hearing originally scheduled the next morning.

Although Ms. Blumenthal was unavailable and no other witness was subject to cross examination, the parties proceeded with the February 22, 2008 hearing at the request of PacifiCorp. At the hearing, both PacifiCorp (PPL/100-105 and PPL/200-206) and Staff (Staff/100-102 and Staff/200) entered testimony into the record without objection. In addition, at the request of ALJ Arlow, ICNU submitted its response to PacifiCorp's Motion in Limine.

On March 3, 2008, ALJ Arlow granted PacifiCorp's Motion in Limine striking a majority of Ms. Blumenthal's Testimony.[1/] At the hearing on March 4, 2008, ICNU objected to ALJ Arlow's ruling. ICNU's objection was noted, and Ms.

[1/] ICNU has separately requested certification of ALJ Arlow's ruling to the Commission.

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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. ICNU/200-213 exhibits were admitted without objection.[2/] Id. at 37, lines 14-20.

After cross-examination of Ms. Blumenthal by PacifiCorp, PacifiCorp offered PPL/300-307 into the record. PPL/300 and 301 were admitted without objection. Id. at 84, lines 7-8. PPL/302-303 consisted of testimony and a Stipulation from Docket No. UE 178. ICNU objected to the introduction of this evidence. After lengthy argument, ALJ Arlow agreed to take official notice of PPL/302 instead. Id. at 91, lines 2-4. PacifiCorp withdrew PPL/303. Id. at 93, line 8. ICNU also objected to the introduction of PPL/304-306, which consisted of past comments of ICNU in SB 408 rulemaking dockets. ALJ Arlow also agreed to take official notice of these documents. Id. at 94, lines 2-8. PPL/307, which is a timeline of SB 408, was admitted as a demonstrative exhibit subject to verification by ICNU.[3/] Id. at 95, lines 10-12.

II. STANDARD OF REVIEW

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

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[2/] PacifiCorp later objected to the admission of ICNU/207-213, which was denied by ALJ Arlow.

[3/] ICNU has verified the dates in PPL/307.

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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.

III. ARGUMENT

A. 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. If the rule does not comply with SB 408, 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. See ICNU/100, Blumenthal/7, lines 16-26; ICNU/100, Blumenthal/8, lines 1-22, ICNU/100, Blumenthal/9, lines 1-2 (none of the three methods specified in the Commission's rules produces an actual tax calculation as required by SB 408).

"SB 408 requires this Commission to track the amount of taxes *actually paid* and 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 (Sep. 14, 2006)

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(emphasis added) ("Order No. 06-532"). The automatic adjustment clause under SB 408 by its terms applies only to the difference between actual taxes paid to governmental authorities that are properly attributed to regulated operations of the utility and taxes collected in rates. ORS § 757.268(6).

SB 408 is intended to ensure that consolidated tax savings that reduce the amount of taxes actually paid to governmental authorities 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 § 756.267(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 amount of taxes paid that are properly attributed to the regulated operations of the utility (the Apportionment Method) cannot be more than the stand-alone tax liability (subsection (a)) or the total amount of consolidated taxes paid by the taxpaying entity (subsection (b)). All three of these calculations plainly require a calculation of taxes actually paid. In this case, the stand-alone method produced the lowest figure, and is used by Staff and PacifiCorp in determining the difference between taxes paid and taxes collected.

None of the methodologies in OAR§ 860-022-0041, however, are actual tax calculations as required by statute. ICNU/100, Blumenthal/7, lines 16-26; ICNU/100, Blumenthal/8, lines 1-22; ICNU/100, Blumenthal/9, lines 1-2. Rather, the Commission's rules involve hypothetical calculations that do not produce the actual taxes PacifiCorp paid to governmental authorities. See ICNU/100, Blumenthal/7, lines 16-18 (stand-alone method is a "hypothetical" calculation). Moreover, because an actual tax return has been prepared for the 2006 tax year, the tax return and PacifiCorp's taxable income should be the starting point for an actual taxes paid calculation. ICNU/100, Blumenthal/7, lines 13-16.

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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. This is problematic because, for as long as PacifiCorp is owned by Berkshire Hathaway, the stand-alone method will almost always produce the lowest amount of the three methods and be used for determining the taxes PacifiCorp paid to governmental authorities. ICNU/100, Blumenthal/5, lines 20-22.

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 each entity in the consolidated group. Id. at lines 15-16. The pro forma tax figures are

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based on book net income, 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. Reviewing and verifying these Schedule M adjustments is a very time intensive process, and is a significant waste of resources considering an actual tax return already exists for the utility. Id. at lines 11-14.

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' 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 may be the most convenient method for PacifiCorp, convenience cannot overcome the plain language of the statute.

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;

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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, depreciation expense should be included on a straight line basis in order to produce an actual tax result. ICNU 100/Blumenthal 6, lines 18-21. 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 subtract depreciation of public utility property.

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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.

Staff simply asserts 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. Ms. Blumenthal acknowledges that removal of accelerated tax depreciation expense is required to avoid a normalization violation, but is of the opinion that it must be added back on a straight line basis to produce an actual tax calculation. It is simply not apparent 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. 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 collected never get 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

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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).

Mr. Fuller also disputes the notion that the stand-alone method will almost always produce the lowest dollar amount. PPL/200, Fuller/10, lines 14-19. As an example, Mr. Fuller points to times of "major natural disaster or terrorist attacks." PPL/200, Fuller/11, lines 1-5. It is doubtful that SB 408 was intended to require Berkshire Hathaway to share its consolidated tax benefits with PacifiCorp customers only during times of extreme financial duress due to such extreme, infrequent events. Thus, while it may be true that the stand-alone method may not produce the lowest amount during such times, this example provided by Mr. Fuller proves that the Commission's rules do not comply with SB 408.

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 2, 2007, PacifiCorp's financials for the nine-months ending December 31, 2006 are listed. PacifiCorp 10-K at 55.[4/] In addition, 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.

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

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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 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.

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

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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 calculation required by the Commission's rules, however, does not produce an actual taxes paid result.

Using the amount of taxes paid by Berkshire Hathaway as the starting point in addition to the three-factor methodology under the Commission's rules will always allocate too much of the consolidated tax liability to PacifiCorp. INCU/100, Blumenthal 7, lines 25-26; Blumenthal/8, lines 6-9. 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); Re Adoption of Permanent Rules to Implement SB 408, Docket No. AR 499, Order No. 06-532 at 2-3 (Sep. 14, 2006). This is the same methodology used to determine the state income tax of multi-state corporations.

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. Because PacifiCorp is in a more capital-intensive

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business than any other company in Berkshire Hathaway's consolidated group, 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. 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. Whether or not the actual taxes paid result produces a surcharge or credit is not the issue.

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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 consolidated method is also based on the taxes paid by the consolidated taxpayer, with the add back of the tax benefits of accelerated depreciation and investment tax credits. ICNU/100, Blumenthal/8, lines 16-18. This method will never represent taxes actually paid to governmental authorities in PacifiCorp's case because PacifiCorp is consolidated with hundreds of other entities. In any event, the 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.

B. The Commission has the Authority to Disallow PacifiCorp's Requested Surcharge in this Case

ICNU recommends that the Commission deny PacifiCorp recovery of its requested surcharge because the surcharge, based on OAR § 860-022-0041, 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 would violate the terms of SB 408, the Commission has no authority to issue such an order.

ICNU is aware of no cases that stand for the proposition that an agency cannot reject its own rules if that agency finds its rules violate the agency's statutory authority. In fact, in the exercise of an agency's discretion, an agency is specifically authorized to act inconsistent with a rule, agency position, or prior practice if the inconsistency is explained by the agency. ORS § 183.482(8)(b)(B). If an agency

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adequately explains its reasoning for departing from any agency rule, position, or practice, a reviewing court has no basis for overturning the agency's decision. Gordon v. Board, 343 Or. 618, 635 (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, Docket No. UE 170, Order No. 05-1050 at 13 (Sep. 28, 2005). Despite 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.

In addition, in a pending case before the Court of Appeals, the Commission argues that it is not required to follow its own rules when to do so would violate its statutory authority. Crooked River Ranch Water Co. v. Pub. Util. Comm'n of Oregon, CA A134177, Respondent's Brief at 24-25 (Jan. 22, 2008). The question presented in Crooked River is whether OAR § 860-036-0412 requires 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 § 860-036-0412(3) (emphasis added). Despite the requirements of this rule, the Commission argues 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." Crooked River, CA A134177,

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Respondent's Brief at 24 (internal quotation marks omitted). Although the Commission characterizes 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.

Further, if ICNU chooses to appeal, ICNU is required to give the Commission an opportunity to first rule on whether to follow its own rules. ORS § 183.400(1) provides that:

> The court shall have jurisdiction to review the validity of the rule whether or not the petitioner has first requested the 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*.

(Emphasis added.) This case falls into the above-emphasized portion of ORS § 183.400(1). Because ICNU is a party to a contested case in which a court can determine the validity of the rule on appeal, ICNU must first request the Commission to "pass upon the validity of the rule in question," in this case, OAR § 860-022-0041. If ICNU does not first give the Commission the opportunity to determine the validity of its rules, ICNU is barred from raising such arguments on appeal, should ICNU choose to do so. See Minor v. Adult and Family Serv. Div., 105 Or. App. 178, 182 (1991) (an independent rule challenge is prohibited when a party is a participant in a contested case where the rule challenge may be raised). Therefore, not only may the Commission determine the

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validity of its own rules in this Docket, but ICNU *must* give the Commission the opportunity to do so should ICNU choose to appeal.[5/]

ICNU respectfully requests that the Commission waive the operation of OAR § 860-022-0041 in this Docket in order to avoid violating SB 408. After all, the Commission "is a legislative agency and has only those powers granted it by the legislature." Advanced TV & Video v. Qwest Corp., Docket No. UC 454, Order No. 00-572 at 5 (Sep. 19, 2000). Granting PacifiCorp's requested surcharge based on OAR § 860-022-0041 would not reflect the difference between taxes paid and taxes collected, as required by SB 408. As a result, the Commission has adequate reason to act contrary to OAR § 860-022-0041.

C. The Commission Should Not Adopt Staff's Recommendations which Increased the Surcharge by $2.4 Million Dollars

PacifiCorp originally used its actual interest deduction to calculate PacifiCorp's interest expense. PPL/200, Fuller/4, lines 18-19. Staff, however, recommended that PacifiCorp switch to the interest synchronization method. This change results in an increase of $2.4 million to the hypothetical taxes paid. As stated previously, however, Staff acknowledges that the use of the interest synchronization method does not accurately approximate tax liability and needs to be addressed in a future rulemaking proceeding. Supra at 10; Staff/200, Owings-Ball/6, lines 8-20. The Commission should not adopt a method that Staff admits is flawed. If the Commission

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[5/] In Docket No. UE 178, despite a complete settlement of the outstanding issues regarding Portland General Electric Company's ("PGE") tax report, PGE intends to raise arguments regarding the Constitutionality of SB 408. PGE's arguments will challenge the validity of the *entire* statute, and by implication, the Commission's rules implementing the statute. These arguments are relevant to Docket No. UE 178, as PGE must raise these arguments to preserve their arguments for appeal.

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rejects ICNU's recommendation to disallow any surcharge in this Docket, at the least, the Commission should reject Staff's adjustment based on the interest synchronization method and authorize only a $32.1 million surcharge.

D. ICNU's Position in this case is Consistent with its Position in Prior SB 408 Rulemakings

At the hearing, PacifiCorp ALJ Alrow granted official notice of various comments submitted by ICNU in the SB 408 rulemaking dockets. From PacifiCorp's failed cross-examination of Ms. Blumenthal with these comments, it is apparent that PacifiCorp will argue that ICNU's position in this case is inconsistent with its position in the SB 408 Rulemaking dockets. This assertion is absolutely false.

In its Reply Comments to the proposed rules in AR 499, dated July 31, 2006, ICNU advocated for use of the Apportionment Method on a *situs basis*. ICNU did not argue that the Apportionment Method should be adopted by the Commission to determine what portion of taxes paid to government authorities that are properly attributed to the regulated operations of the utility. To the contrary, as memorialized in the interim order in AR 499, ICNU supported the method selected for the temporary rule, which "allocates taxes paid within the affiliated group, *on the basis of taxable income*, to every affiliate with taxable income within that company." 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) (emphasis added).

The Commission rejected ICNU's recommendation to use taxable income, and instead adopted the three-factor Apportionment Method. Id. at 5. ICNU chose not to

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challenge the Commission's decision at that time because it was not apparent until analyzing actual tax data that the Apportionment Method would produce a result contrary to what is required by SB 408. PacifiCorp's misleading attempts to discredit ICNU's position in this case should be ignored.

E. This is the First Opportunity to Challenge the Rules

Not only did ICNU oppose the Apportionment Method in the SB 408 rulemaking proceedings, but this Docket presents the first opportunity to determine how the Apportionment Method and the other provisions of OAR § 860-022-0041 operate with actual tax data. In typical rulemaking dockets, it is difficult to test theories that seem correct without actual numbers. See Transcript at 97, lines 6-14 (Ms. Blumenthal testifies that "theory might lead you one place, and when you put actual numbers to it, you might end up somewhere else."). Staff even admits that a future rulemaking is required because the Commission's rules do not work as intended. Staff/200, Owings-Ball/6, lines 8-20.

The Commission adopted OAR § 860-022-0041 on September 14, 2006, in Docket No. AR 499. PacifiCorp filed a tax report for the 2005 tax year on October 16, 2006, which was docketed under UE 177.[6/] No rate change was required for PacifiCorp's tax report for the 2005 tax year because the SB 408 automatic adjustment clause did not apply to taxes collected and paid before January 1, 2006. As a result, on January 18, 2007, Staff filed a letter with the Commission informing the Commission that there were no contested issues with respect to PacifiCorp's 2005 tax report and requesting that the

[6/] PacifiCorp's filing occurred on October 16, 2006 because October 15 fell on a Sunday.

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Commission suspend the procedural schedule. On January 23, 2007, ICNU filed a letter with the Commission supporting Staff's position, but clarifying that ICNU's support was based on the fact that there was no rate change at issue and that ICNU was expressly reserving all arguments for future filings when an actual rate adjustment will be at issue. OAR § 860-022-0041 was further amended in Docket No. AR 517. Because PacifiCorp's tax report for the 2006 tax year is the first time an actual rate adjustment is involved, this Docket presents the first opportunity to test the final rules passed in AR 517 with actual tax data.

F. Docket No. UE 178 is Irrelevant to this Docket

PacifiCorp attempted to introduce into evidence the Stipulation that ICNU was a party to in Docket No. UE 178, Portland General Electric Company's ("PGE") SB 408 docket. ALJ Arlow rejected the introduction of the Stipulation into evidence, but granted official notice. The Stipulation is irrelevant to this Docket, and should not be considered by the Commission under any circumstances.

First, the use of a settlement to attack a party in another Docket sets a dangerous precedent. If the fact of settlement may be used against a party, it will have a chilling effect on the willingness of parties to compromise in the spirit of settlement. In questioning the relevance of the UE 178 Stipulation, ALJ Arlow stated at the hearing, "One of the points of the stipulation is that while the parties do not agree with respect to the underlying matters, they are willing, for the purposes of agreement, to accept certain findings as being legal." Transcript at 47, lines 8-12. This is precisely the reason why most stipulations, including the Stipulation in UE 178, contain provisions specifically

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stating that no party to the stipulation agrees to any facts, principles, methods or theories, and that the stipulation cannot be used to resolve issues in other proceedings. See Re PGE, Docket No. UE 178, Stipulation at ¶ III(E) (Feb. 1, 2008).

Second, ICNU's position in UE 178 is not inconsistent with its position in this Docket. The Stipulation specifically states that ICNU does "not agree whether the methodologies set forth in OAR 860-022-0041 are consistent with the goals of [SB 408]." Id. at ¶ II(B)(2); Joint Stipulating Parties/200, Owings-Ball-Tinker-Blumenthal-Jenks/3, lines 1-3. The parties in UE 178 only agreed that the net refund amount was a proper compromise for resolving the issues in that Docket. Moreover, as stated by Ms. Blumenthal at the hearing, ICNU had the opportunity to ensure that PGE's tax report satisfied the Commission's rules because PGE was "gracious enough to give [Ms. Blumenthal] a copy of the tax report . . . ." Transcript at 89, lines 6-8. Because PacifiCorp did not provide ICNU with its tax report, however, ICNU was not able to do the same in this Docket. Id. at lines 2-5.

G. PacifiCorp's Amortization Proposal should be Rejected

As previously stated, should the Commission approve a surcharge, that surcharge should only be $32.1 million. Supra at 18-19. Even if the Commission approves this surcharge, the Commission should still reject PacifiCorp's amortization proposal. PacifiCorp proposes to amortize only $27 million of the requested surcharge and place the remaining balance plus interest into PacifiCorp's SB 408 balancing account, where the interest will continue to accrue. PPL/100, Larson/4, lines 3-17.

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PacifiCorp should be required to amortize the entire $32.1 million amount, and should be required to apply a more reasonable interest rate to the surcharge.

1. Refund of the Entire $32.1 Million More Closely Matches Benefits and Burdens

The SB 408 balancing account is a deferred account, and should be treated as such. One goal of deferred accounting is to "match appropriately the costs borne by and benefits received by ratepayers." ORS § 757.259(2)(e). In this case, the appropriate matching is achieved by amortizing the surcharge amount over the same time period over which those amounts were collected. See Re PGE, Docket No. UM 1234, Order No. 07-049 at 9 (Feb. 12, 2007) (shorter time period of rate impact better aligns benefits and costs).

While PacifiCorp asserts its proposal was intended to limit its SB 408 surcharge to a 3% rate increase, ICNU believes ratepayers will be harmed more by the accrual of interest on the balance (already $5.8 million). PPL/100, Larson 4, line 14; Larson 5, lines 1-9. PacifiCorp specifically states in its testimony that it does not object to a one-year amortization period should ICNU persist in its objection. PPL/100, Larson/5, lines 11-13. As a result, the Commission should order a one-year amortization period for the surcharge.

2. The Interest Rate Applied by PacifiCorp is Unreasonable

PacifiCorp plans to apply an interest rate of 8.16% to its SB 408 balancing account, an amount equal to PacifiCorp's authorized rate of return ("ROR"). ICNU/208. Considering that any amount in the SB 408 balancing account is required by statute to be

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amortized, leaving no risk of non-recovery, an interest rate equal to PacifiCorp's ROR is simply unreasonable.

The Commission has found that an interest rate equal to a utility's ROR is inappropriate during the amortization stage of a deferred account because of the lower risk of non-recovery. Re Staff Request to Open an Investigation Related to Deferred Accounting, Docket No. UM 1147, Order No. 05-1070 at 14 (Oct. 5, 2005); Docket No. UM 1147, Order No. 06-507 at 4-5 (Sep. 6, 2006). Thus, the Commission concluded that the utility "need only be kept whole on such investments." Docket No. UM 1147, Order No. 06-507 at 5.

The Commission has not yet issued a final order resolving the appropriate interest rate to be applied to deferred accounts during amortization. One thing, however, is clear; the interest rate should be *less* than a utility's authorized rate of return. The application of a lower interest rate is even more compelling in this Docket, as SB 408 eliminates any risk of non-recovery for PacifiCorp.

V. CONCLUSION

PacifiCorp's requested surcharge should be rejected because the surcharge would violate SB 408. The OPUC cannot rely upon OAR § 860-22-0041 to impose this requested surcharge since the rule does not produce an actual taxes paid result. Alternatively, if the Commission imposes PacifiCorp's requested surcharge, the Commission should order the surcharge amortized over a one-year period and at a lower interest rate that is more reflective of the risk of non-recovery.

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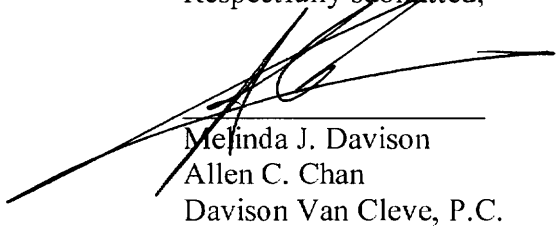
Dated this 14th day of March, 2008.

Respectfully submitted,



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