

**BEFORE THE PUBLIC UTILITY COMMISSION
OF OREGON**

UE 228

In the Matter of)	
)	
PORTLAND GENERAL ELECTRIC)	CLOSING BRIEF OF
COMPANY 2012 Annual Power Cost)	THE CITIZENS' UTILITY BOARD
Update Tariff (Schedule 125))	OF OREGON
)	
)	<i>REDACTED</i>
_____)	

I. Introduction

Prudence reviews are based upon what a company knew or should have known at the time it executed a particular transaction.¹ The question is not whether the outcome was good or bad, but whether the judgment exercised by the company was reasonable at the time it was exercised. In this docket, CUB has demonstrated that PGE’s judgment was not reasonable at the time it was exercised by establishing that: PGE’s employees failed to provide senior management with a full analysis of each Mid Term Strategy (“MTS”) transaction as required by PGE policies; that PGE’s management failed to adequately supervise its employees to make sure they were following Company policy by adequately documenting transactions; that PGE’s employees and management knew, or should have known, that they were required to document their hedges; and that PGE hedged too much gas too early.

CUB supports ICNU’s request for an adjustment (disallowance) of **BEGIN**

CONFIDENTIAL [REDACTED] ²

[REDACTED]

[REDACTED]

¹ *In re PacifiCorp*, UM 995/UE 121, Order No. 02-469 at 5 (July 18, 2002); ICNU/108 Schoenbeck/2 lines 13-16.

² Transcript of Deposition of Donald W. Schoenbeck at 101, lines 6-25. **BEGIN CONFIDENTIAL** [REDACTED]

[REDACTED]
END CONFIDENTIAL Transcript of Deposition of Donald W. Schoenbeck at 101-102, lines 25-3.

[REDACTED]
[REDACTED] ; Transcript of Deposition of Donald W. Schoenbeck at 103, lines 11-15.

[REDACTED] END CONFIDENTIAL Transcript of Deposition of Donald W. Schoenbeck at 104, lines 15-20.
See also ICNU/100 Schoenbeck/7-9.

END CONFIDENTIAL CUB also requests that the Commission impose a limit to PGE's hedging volumes that is similar to the limit agreed upon by Avista in UM 1282 and require PGE to fully implement a portfolio approach that layers hedges on top of each other over time. A strategy based on hedging nearly 100% of gas requirements in the first two years simply contains too much risk.⁴ CUB requests that the Commission order PGE to do the following if it wants to obtain recovery from customers:

- follow its own policies
- meticulously document the reasons for any decision required to be in writing
- make prudent decisions
- provide appropriate training and oversight to all its employees
- audit its own programs to ensure that policies are being followed.

PGE failed to do all of the above in regard to hedging transactions that took place between 2007 and 2008 that were in excess of 48 months in tenor. Therefore, the disallowance requested by CUB and ICNU is appropriate.

CUB also respectfully requests that the Commission open a docket, or broaden the scope of AR 553, to encompass more than confidentiality issues related to SB 967. It is high time that the issue of utility designation of confidential and highly confidential materials be revisited.

CUB also notes that its choice not to address any issue raised by PGE in its Opening Brief should not be interpreted as agreement with PGE's positions. CUB does not agree with the positions taken by PGE in its brief. CUB's brevity in this Closing

³ ICNU/108 Schoenbeck/13 lines 1-4.

⁴ CUB/100 Jenks-Feighner/4, lines 4 – 23.

Brief is an indication only of the issues CUB finds to be most relevant to a determination of imprudence in this docket.

II. CUB’s response to PGE’s Opening Brief

A. PGE Bears the Burden of Proof

Contrary to the statements made in PGE’s Opening Brief, PGE has the burden of proving, by a preponderance of the evidence, that its hedging strategy is reasonable and prudent; CUB does not bear the burden of proving that PGE’s hedging strategy was unreasonable or imprudent. PGE has failed to produce documentation evidencing that the questioned transactions were entered into prudently. The one-page memos that exist contain no analysis, and few have supporting research, let alone actual workpapers.

B. PGE Failed to Document Its Transactions and as a Result Hedged Too Much Gas Too Early

As noted above, PGE has the burden of proof (of documenting) the reasonableness and prudence of its transaction decisions. This docket is a prudence review of PGE’s 2012 NVPC, which include

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[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]⁵

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As noted by ICNU in its Opening Brief at 5, “[W]hile the MTS created a framework for entering 3-5 year transactions, actually implementing the transactions was contingent on market analysis and a demonstration of liquidity.”

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[REDACTED]

[REDACTED]^{6,7,8} [REDACTED]

[REDACTED]^{9,10}

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PGE tries to mask the imprudence of its gas hedges by stating that it was implementing a combined gas and electric hedging strategy. The fact that PGE claims a combined policy – which again is not documented anywhere – does not negate the fact that its gas hedging was imprudent. As stated by ICNU in its Opening Brief at 23:

While ICNU understands that there is a correlation between gas and electricity, the idea that it was prudent for the Company to rush to hedge [Confidential] [REDACTED] [Confidential] that the traders were implementing the MTS ignores the fact that the company must still show a documented rationale for each transaction. Mr. Schoenbeck pointed out that [Confidential] [REDACTED] [Confidential] and most utilities spread their transactions over time to diversify risk, rather than trying to beat the market by trying to purchase

⁵ ICNU/108 Schoenbeck/10 lines 2-4; *See for example*, ICNU/110 page 37-40, 55, 66.

⁶ CUB CONFIDENTIAL Exhibit 102, page 1.

⁷ CUB/100 Jenks-Feighner/2 lines 6-7.

⁸ Transcript of Deposition of Donald W. Schoenbeck at 27, lines 15-19.

⁹ CUB CONFIDENTIAL Exhibit 102, page 2.

¹⁰ CUB/100 Jenks-Feighner/2 lines 7-11.

[Confidential] [REDACTED] **[Confidential]** in a short time frame. ICNU/108, Schoenbeck/11-12; ICNU/109, Schoenbeck/27. Any departure from this norm should require a reasoned contemporaneous justification.

In order to protect customers from this flawed strategy, the Commission should disallow all hedges in the current AUT that were entered into more than 48 months ahead of the gas delivery. Instead, this gas supply should be re-priced at the forward price curve for gas at the time of the final update in November.¹¹

CUB also recommends that the Commission impose a limit to PGE's hedging volumes that is similar to the limit agreed upon by Avista in UM 1282.¹²

C. PGE's Denigration of CUB's Reference to NW Natural's Transactions is Inappropriate

PGE denigrates CUB's reliance on the hedging positions of Northwest Natural (NWN), pointing to the fact that CUB supported the entry into a 30-year *physical* hedge by NWN. PGE misunderstands the circumstances of the 30 year *physical* hedge. CUB, NWIGU, and Staff spent several extremely intense months reviewing and analyzing that transaction. While CUB would have liked more time and better flow of documentation, a huge amount of review and analysis was undertaken and completed by CUB.¹³ But as the

¹¹ CUB/100 Jenks-Feighner/5 lines 17-22; Affidavits of Bob Jenks and Gordon Feighner.

¹² CUB/100 Jenks-Feighner/3 -4 lines 11-2.

¹³ Order 11-176 at page 4 "Evidence to support the Stipulation is found in NW Natural's applications and testimony, opening testimony filed by CUB, NWIGU, and Staff, as well as joint and individual testimony offered by the Parties in support of the Stipulation. This testimony included the parties' own internal investigations, as well as analyses performed by independent consultants retained to assist in evaluating the terms of the Proposed Transaction. These advisors included Netherland Sewell & Associates, Inc. (NSAI), ENVIRON International Corporation (ENVIRON), the accounting firm of KPMG, and independent legal counsel." *See also*, UM 1520/CUB 300/Jenks at 11-12 at lines 18-2: "through research necessary to respond to the Data Requests propounded by the Staff and Intervenors, and through changes made to the transaction as a result of that research CUB, based upon the information available to it at this time, believes that NW Natural has done sufficient due diligence for CUB to be able to recommend to the Commission that the Commission find that the Company has met the due diligence standard."

Stipulation and Joint Testimony show, while the parties approved the initial entry into that transaction, NWN and the parties agreed that every transaction entered into under that hedge will be subject to individual review for prudence.¹⁴

PGE did not seek approval for its MTS. PGE did not allow parties to access documents related to the MTS, and in fact, PGE argues that Intervenors should not be allowed to review the MTS or the individual transactions entered into under the MTS.

Clearly, the MTS and NWN deals are different in some respects but they are most different in the level of analysis and review conducted and documented prior to entry into the original policy/deal. It remains to be seen if they are different in the amount of analysis and review conducted for individual transactions, which will be determined during the prudence reviews of those transactions.

D. PGE Was Not Knowingly Using a “Stack and Roll” Policy

Not until after Mr. Schoenbeck’s deposition, where it learned about the books that Mr. Schoenbeck had studied, did PGE ever use the phrase “Stack and Roll.” This phrase was first used by PGE at the hearing. Mr. Schoenbeck did not mention it during his deposition. If PGE was really following a Stack and Roll theory, then why was this not mentioned in PGE’s Application and Direct Testimony filed April 1, 2011, in its Supplemental Application filed April 15, 2011, in the workshop on June 1, 2011, or its Rebuttal testimony filed August 15, 2011? It was not until Mr. Stoddard’s live Sur-sur-

¹⁴ Order 11-140 at page 3. “As stated in the stipulation, the finding of prudence does not prevent the parties from challenging the prudence of the Proposed Transaction if new information arises that demonstrates that NW Natural knew, or should have known, something of consequence to the Proposed Transaction at the time of entering it. Moreover, the finding of prudence at this time applies only to NW Natural's decisions to enter into the Proposed Transaction, and not any subsequent decisions the Company might make in terms of exercising its discretion to manage underlying contracts.”

rebuttal testimony at the hearing that PGE chose to tell us that it was following a Stack and Roll policy—but it still failed to provide any documentation to back this up.

For all of the above reasons, CUB does not allot any credibility to PGE’s claim that PGE has been using a Stack and Roll policy since 2007 and 2008—there is absolutely no documentation provided to support this claim. CUB respectfully recommends that the Commission find that PGE failed to document the reasonableness and prudence of the listed hedges and that the Commission then impose the disallowance advocated for by CUB and ICNU.

E. The Requested Disallowance Likely Will Not Create a Harm in the Form of Increased Collateral for the Company

PGE was not punished by its investors in regard to the Boardman allowance. Why should this disallowance be any different? It appears that PGE’s investors are less flighty than PGE thinks.

During the hearing, ICNU cross-examined PGE CFO Maria Pope. ICNU asked Ms. Pope whether PGE had taken write-offs as a result of the decision in UE 196, disallowing \$26.4 million in costs.¹⁵ Ms. Pope responded in the affirmative. She was, however, unable to provide any evidence that ratings agencies, such as Standard and Poor’s, had in fact responded negatively to that disallowance.¹⁶ PGE did not seek to supplement the record after the hearing in this regard—there is therefore no evidence in the record to support PGE’s claims.

¹⁵ Transcript of Hearing at 93, line 23 through 94, line 4.

¹⁶ Transcript of Hearing at 94, line 5 through 99, line 23.

The Commission needs to send a message to PGE management that hiding the ball from investors or customers will not prevent the Commission from imposing necessary and appropriate disallowances.

F. The Proposed Adjustment Is Not Based on Hindsight

PGE argues that the proposed disallowance advocated by CUB and ICNU is a hindsight adjustment and should not be granted.^{17,18,19} However, the adjustment being advocated for is the result of a prudence review, rather than a hindsight adjustment.

G. The Mid-Term Strategy Has Not Been Reviewed and Evaluated As Part of a Prior Commission Proceeding

PGE continues to try to portray that there was an extensive regulatory process related to its adoption of the MTS, but the record solidly refutes this. Upon review of the times at which the Intervenors are supposed to have had the opportunity to review, comment, and pass blessing on PGE's hedging policies, it becomes clear that no real review could ever be done.

Commission Staff, when asked for its opinion, stated:

We have indicated that - - that our support is contingent on there being liquidity in the market, and that PGE should document the analysis that supports the - - any transactions that they make. And so we think it's a good step.²⁰

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[REDACTED]

[REDACTED]

¹⁷ PGE/300 Pope-Valach 2 lines 1-2; PGE/300 Pope-Valach 3 lines 1-3; PGE/300 Pope-Valach/8-12.

¹⁸ Transcript of Hearing at 23 lines, 10-13 and lines 18-21.

¹⁹ PGE/500 Stoddard/8-10.

²⁰ ICNU Cr. Ex. 703 pages 10-11 lines 23 – 2.

[REDACTED]

21 [REDACTED]

[REDACTED] 22

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To bolster its failing argument, PGE also argues that there was some kind of preapproval process or estoppel as a result of its sharing a modicum of information on the topic of hedging with the Commission and intervenors.²³ Again, as demonstrated with the quotations above,

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H. CUB Wants PGE to Carry Out the MTS in a Prudent Manner

PGE’s Opening Brief devotes significant ink and paper to trying to suggest that CUB is advocating for something new and that the “something new” should be retroactively enforced.²⁴ Nothing could be further from the truth. This is a prudence review. CUB has merely pointed out that PGE did not follow its own policies and implement the layered portfolio strategy that the MTS was originally designed to achieve

²¹ Transcript of Hearing at 137, lines 4 – 11.
²² Transcript of Hearing at 151, lines 13 – 18.
²³ ICNU Opening Brief at 20 - 22.
²⁴ PGE Opening Brief at 14 Section VII.

and that PGE told the Commission it was using.²⁵ The only entity that did anything new here was PGE in that it failed to follow its own policies, failed to monitor and control its own employees with the result that they created, and enforced, an ad hoc policy separate from the MTS and the risk management policies designed to implement and regulate the MTS.

I. Future Proceedings Should Not Be a Substitute for CUB's Recommended Disallowance

PGE has recommended that the Commission consider a “go-forward” docket to look at workshops to inform the utility’s hedging policy. CUB supports a more in-depth review of each utility’s hedging policies, but does not support any kind of process that could be used as a claim of preapproval for its hedging strategy by PGE. CUB recommends that any workshops or other proceedings ordered as a result of this docket should not be ordered in lieu of the disallowance requested by the intervenors in this docket and should be specifically identified as not being a pre-approval process.

J. The Commission Needs to Tell All Parties that Designation, and Over-Designation, of Materials as Confidential and Highly Confidential Will Not Be Tolerated

The Commission needs to send a message in this docket and in all future dockets that the over-designation of information as confidential information will not be tolerated.

²⁵ PGE cites to a statement made by Maury Galbraith (PGE Opening Brief at 11) as saying Staff was supportive of what they were doing but the citation says, “You’re essentially starting to layer in purchases over a longer time frame, and we’re supportive of that.” As CUB has shown, in section II B. above, PGE did not in fact layer in purchases over the longer time frame. The statement PGE cites as support for its position is completely inapposite proving instead that there was no pre-approval of what it did by Staff, and that there was in fact no layering of the type anticipated by Staff.

The evidentiary record in this docket is incomplete because of the over-designation of confidential material. Short of doing its own investigation, the Commission will never know the full truth about hedging because the Intervenors are prevented from disclosing, and entering as evidence, all that they know. This is a matter that the Commission needs to address.

The Commission should consider opening a docket to review the designation of confidential documents, or alternatively, the Commission should consider broadening the scope of AR 553 to encompass more than confidentiality issues related to SB 967. It is high time that the issue of utility designation of confidential and highly confidential materials was revisited. No longer is it simply a case of one docket having an over-designation of confidential information; now, the dockets with an over-designation of confidential information are bleeding over into each other and forming a wall of silence through which Intervenors cannot penetrate. If every company is allowed to designate all the materials in regard to one topic as confidential, then, as we have seen in this docket, it is made virtually impossible for Intervenor experts to make comparisons and state opinions.

Far from promoting the review, analysis and implementation of fair, just, and reasonable rates, this will in fact ensure that unfair, unjust, and unreasonable rates are what will actually be implemented. CUB is deeply concerned about its future ability to obtain the information necessary to review and analyze utility applications. The broadening of AR 553, or the opening of another docket to review these issues, is very necessary. CUB respectfully requests that the Commission consider either broadening AR 553 or opening a new docket.

IV. Conclusions and Recommendations to the Commission

PGE's gas hedging was imprudent because PGE:

- entered into a front loaded strategy instead of a layered strategy,
- inadequately analyzed and documented the reasons for its transactions,
- provided the Commission with undocumented post game rationales for its hedging plays—the spurious Stack and Roll theory,
- attempted to shift the burden of proof to Intervenors,
- marked so many documents confidential that it has almost succeeded in muzzling Intervenors' experts,
- failed to exercise oversight and control over its traders and their managers, and
- allowed trades to occur beyond 48 months without adequate analysis or documentation

The bottom line is that it should not matter how flowery and self congratulatory the language of PGE's outside expert is—the evidence shows that Mr. Stoddard was hired a mere month before his testimony, relied only on the information fed to him by PGE, and did little or no independent analysis of the market conditions existing in 2007-2008. In fact, the evidence shows that PGE itself did little analysis of the market conditions in 2007 and 2008, saving that analysis for its post game rationalizations at the time of this hearing.

If PGE had put in half as much effort into its analysis and documentation in 2007 and 2008 as it has to orally recreating the missing information in 2011, we likely would not be discussing this issue today, because on review of its own analysis, PGE's

management would hopefully have acted prudently and prevented the contested transactions from occurring on the basis of the flimsy information provided by its employees.

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[REDACTED]

[REDACTED]

[REDACTED]²⁶

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CUB further requests that the Commission order PGE do the following if it wishes to obtain recovery from customers:

- Follow its own policies,
- Meticulously document the reasons for any decision required to be in writing,
- Make prudent decisions,
- Provide appropriate training and oversight to all its employees, and
- Audit its own programs to ensure that policies are being followed

And, as noted above, CUB also respectfully requests that the Commission consider opening a docket, or broadening the scope of AR 553, to encompass more than confidentiality issues related to SB967 so that the issue of utility designation of confidential and highly confidential materials can be revisited.

²⁶ ICNU/108 Schoenbeck/13 lines 1-4.

September 26, 2011

Respectfully submitted,

A handwritten signature in black ink, appearing to read 'G. C. M.', written in a cursive style.

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UE 228 – CERTIFICATE OF SERVICE

I hereby certify that, on this 26th day of September, 2011, I served the foregoing CITIZENS' UTILITY BOARD OF OREGON'S CLOSING BRIEF in docket UE 228 upon each party listed in the UE 228 OPUC Service List by email and, where paper service is not waived, by U.S. mail, postage prepaid, and upon the Commission by email and by sending one original and five copies by U.S. mail, postage prepaid, to the Commission's Salem offices.

(W denotes waiver of paper service)

(C denotes service of Confidential material authorized)

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