BEFORE THE OREGON PUBLIC UTILITIES COMMISSION

DR 10/UE 88/UM 989

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In the Matters of

The Application of Portland General Electric Company for an Investigation into Least Cost Plan Plant Retirement. (DR 10)

Revised Tariffs Schedules for Electric Service in Oregon Filed by Portland General Electric Company. (UE 88)

Portland General Electric Company's Application for an Accounting Order and for Order Approving Tariff Sheets Implementing Rate Reduction. (UM 989)

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OPENING BRIEF OF UTILITY REFORM PROJECT, ET AL. AND CLASS ACTION PLAINTIFFS

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I. THE "NET BENEFIT ANALYSIS" IS IRRELEVANT TO DETERMINING WHETHER RATES ARE LAWFUL, FAIR, JUST, OR REASONABLE. . . 41

The Utility Reform Project (URP), et al., and the Class Action Plaintiffs (Gearhart, Morgan, Kafoury Brothers, Inc.) [hereinafter URP/CAP or "we"] file this Opening Brief.

We incorporate by reference the Answering Brief of URP filed in the UM 989 proceeding (October 21, 2001), except as modified below, to the extent that the discussion in that brief does not violate the scope of this proceeding, as established by the Ruling and Notice of Conference (February 22, 2008) [hereinafter "Phase 3 Scoping Order"].

I. THE COMMISSION SHOULD REPLACE ITS ORIGINAL RATE ORDERS IN THE UM 989 DOCKET WITH THE RATE TREATMENT RECOMMENDED BY WITNESS JIM LAZAR.

The Phase 3 Scoping Order (p. 2) states that the rates adopted in OPUC Order No. 02-227 were to implement a settlement among Staff, PGE, and CUB in 2000.[1]

> Phase III of these remand proceedings will address the Court of Appeal's [sic] remand of Order No. 02-227 in docket UM 989. The rates adopted in Order No. 02-227 implemented a settlement reached by Staff, PGE, and the Citizens' Utility Board of Oregon (CUB) in 2000. That settlement was intended to respond to the Court of Appeals' decision in Citizens' Utility Board v. Commission by prospectively removing both the return on and the return of PGE's remaining Trojan investment from rates.

Thus, the ultimate issue is, "what rate treatment of the remaining Trojan investment should the Commission have adopted in response to ***Citizens' Utility Bd. of Oregon and Utility Reform Project v. Public Utility Com'n of Oregon***, 154 Or App 702, 962 P2d 744 (1998), *pet rev dis'd*, 355 Or 591, 158 P3d 822 (2002) ("***CUB/URP v. OPUC***")?" Another way to express this would be: What rate treatment of the

1. We object to all references to a "settlement" or "stipulation." Either of those terms refers to an agreement among all of the parties in a proceeding. URP, et al., never agreed to any of the so-called "settlement" or "stipulation."

remaining Trojan investment would have been lawful, just and reasonable? The answer then provides the baseline for deciding whether the rates adopted in OPUC Order No. 02-227 were just and reasonable, which is one of the subissues identified in the Phase 3 Scoping Order.

It seems strange that the Commission would wait for more than 2 years (June 1998 to September 2000) from the Court of Appeals decision before instituting the UM 989 docket. Further, the UM 989 docket itself appears to violate the Commission's alleged rule against "single-issue ratemaking," as it addressed the single issue of adjusting the charges to ratepayers stemming from the Trojan investment without also addressing any other element of PGE rates, such as rate of return, power costs, etc. But, if responding to the Court of Appeals decision was indeed the purpose of the UM 989 proceedings (and is the purpose of this remand), the choice for rate treatment for the remaining Trojan balance is simple and does not involve manipulating over a dozen other accounts of funds owed to ratepayers by PGE or diverting refunds on nuclear insurance premiums paid for by ratepayers or creating a "regulatory asset" and charging ratepayers $47 million for having done so.

Instead, the clear and simple answer would have been to remove from PGE rates the charges for Trojan return on investment, as of October 1, 2000 (or any other date). The illegality of Trojan return on investment was the only issue addressed and decided against OPUC Order No. 95-322 in ***CUB/URP v. OPUC***, and removal of that unlawful component of rates should have been the sole purpose and result of the UM 989 docket. This would have left open the issue of returning to ratepayers the unlawful Trojan return on investment charged pursuant to OPUC Order No. 95-322 prior to the effective date of the order in the UM 989 docket. Separating the OPUC Order No. 95-322 period from the UM 989 period is now exactly what the Commission in the Phase 3 Scoping Order demands.

A. SUMMARY OF STRAIGHTFORWARD RESPONSE TO COURT'S REMAND.

We have previously, in Phase 1 of these consolidated remand dockets, identified and documented the charges that were in PGE rates, through September 2000, for Trojan return on investment. Those charges were $35.202 million per year. URP Exhibit 202, p. 2 (May 19, 2005). Witness Lazar's testimony then explained why $35.202 million per year is the correct number. URP Exhibit 200, pp. 3-4. The proper course for the Commission in September 2000 would have been to order PGE to reduce its rates, on an annualized basis, by $35.202 million in order to remove the Trojan return on investment component from rates. As the courts concluded that PGE could lawfully charge ratepayers for its Trojan return of investment, the charges to ratepayers representing amortization of the Trojan investment balance itself would have continued, as set forth in OPUC Order No. 95-322. In sum, the Commission would have removed and corrected via UM 989 the only defect in OPUC Order No. 95-322, as decided by the courts--allowing PGE to charge ratepayers a return on investment on its Trojan investment.

In the next following general rate case (which happened to have an effective date of October 1, 2001), the Commission would have determined new PGE rates, without having removed the $161.9 million (minimum) in return-bearing accounts, without having diverted NEIL insurance premium rebates to PGE shareholders, and without having created the $36.7 million (present value) FAS 109 "regulatory asset." There was also no need for the elaborate and flawed "net benefit analysis" to attempt to justify this myriad of adjustments and revenue stream diversions.

Since the rates in the next general rate case took effect on October 1, 2001, the UM 989 reduction of $35.202 million annually would have lasted for one year. OPUC Order No. 02-227 claims that, compared with OPUC Order No. 95-322, OPUC Order No. 00-601 and OPUC Order No. 02-227 reduced PGE rates in the first year by $10.2 million. Thus, PGE today still owes ratepayers the difference for that first year, which is $24.002 million with an average incidence date of April 1, 2001 (6 months after the effective date of OPUC Order No. 00-601). That amount must be scaled to the present, using PGE's authorized pre-tax rate of return on investment in the meantime, and then be credited back to ratepayers. This amount will be $68.1 million at October 1, 2008, as shown by Exhibit URP 501, p. 1 ("UM 989 Overcharge").

B. SUMMARY OF CONVOLUTED PATH COMMISSION FOLLOWED.

Instead of this simple and accurate response to ***CUB/URP v. OPUC***, the Commission approved a "stipulation" reached by only some of the parties that involved dozens of transactions that had nothing to do with Trojan. In essence, the Commission treated the UM 989 proceeding as if it were a remand of UE 88. But, instead of addressing only the remanded issue, the Commission went far afield and included a variety of unrelated matters. The Commission's decision in UM 989, OPUC Order No. 02-227, would have transgressed its own Phase 3 Scoping Order of this docket.

But the Commission in OPUC Order No. 02-227 took an approach that sought to preserve for PGE the right to charge ratepayers for a Trojan return on investment. In fact, that was the Commission's express purpose.

> This immediate recovery preserves the outcome we ordered in Order No. 95-322 and which we found resulted in just and reasonable rates and furthered important Commission policy goals.

OPUC Order No. 02-227, p. 12. The Commission took away from ratepayers:

1. interest bearing accounts containing at that time at least $161.9 million (and probably more), as indicated in UM 989 in 2001 in the Lazar testimony and the URP Answering Brief;

2. the $15.4 million in NEIL insurance rebates diverted to shareholders.

And the Commission imposed upon ratepayers the $36.7 million (present value) "regulatory asset."

The removal of the interest bearing accounts from ratepayers, the diversion of $15.4 million in NEIL insurance rebates, and the imposition of the $36.7 million (present value) obligation of ratepayers to PGE were all designed to provide PGE with continued and unimpaired return on Trojan investment. Thus, the charges to ratepayers resulting from those ratemaking manipulations constitute unlawful charges under ORS 757.355. The Commission should now so declare.

The Lazar testimony (Exhibit 501) quantifies the cost to ratepayers imposed by each of these manipulations, taken to present value as of October 1, 2008 (the approximate date of a Commission order in this phase). With appropriate interest (PGE's authorized pre-tax rates of return):

1. Termination of the interest-bearing accounts due to ratepayers has cost them $473,100,699.

2. Diversion of the $15.4 million NEIL rebate has cost them $45,001,546.

3. Continuing to charge ratepayers for return on Trojan until the effective date (October 1, 2001) of the rates adopted in the next PGE general rate case has cost them $68,130,924.

4. Imposing the FAS 109 "regulatory asset," amortized over a 5-year period, has cost them $103,714,077 million.

On the other hand, OPUC Order No. 00-601 and OPUC Order No. 02-227 relieved ratepayers from continuing to pay Trojan investment amortization during the period 2001-2011, which was the remaining amortization period for Trojan under OPUC Order No. 95-322. The present value of that revenue stream, as of October 1, 2008, is $253,455,291.[2] Thus, Exhibit URP 501 shows that the net cost to ratepayers of OPUC Order No. 00-601 and OPUC Order No. 02-227 is $436,491,924 (as of October 1, 2008), compared with an order, effective October 1, 2000, that lawfully revised PGE rates merely to remove Trojan return on investment from rates.

For the time value of money in all of the above calculations, Lazar used PGE's with-tax authorized return on investment (return on ratebase, or ROR) authorized for each period, assuming that PGE's current authorized with-tax ROR would continue through 2011. This approach most accurately reflects the revenue requirement consequences of each alternative.

There was nothing in Commission rate orders, after OPUC Order No. 02-227, which changed the amount being charged to ratepayers for Trojan investment. Thus, the errors in OPUC Order No. 02-227 were carried forward, and their effect was not

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2. For this calculation, Lazar assumed that the unamortized Trojan investment as of October 1, 2000, was the $180.5 million asserted by PGE, although he did not express agreement with that assertion. Based on an assumed straight-line amortization of this amount over the period starting with the fourth quarter of 2000 and ending at the close of 2011, this would reduce the amount due to ratepayers by $253.4 million (present value as of October 1, 2008). He used straight-line amortization of the principal, as that is the technique (1) typically employed by regulators to amortize principal and (2) used by this Commission when amortizing the principle of the Trojan investment in these consolidated dockets.

truncated by any subsequent rate order. To the extent necessary, we request official notice of the records in those post-UM 989 dockets.

C. URP/CAP RECOMMENDATION.

The Commission should adopt this number, $436,491,924, as the amount charged to ratepayers under OPUC Order No. 00-601 and OPUC Order No. 02-227 (current to October 1, 2008) in excess of a lawful revision to rates as of October 1, 2000, to halt additional return on Trojan investment as of that date.

If the Commission believes that any of the constituent components of this number are incorrect, it can adjust the number accordingly. For example, if the Commission believes that ratepayers would have had to pay PGE for the FAS 109 "regulatory asset" in any event (a conclusion we contest), then the Commission should adopt $332,888,847 as the correct amount of the improper charges to ratepayers, as of October 1, 2008.

Staff witness, Judy Johnson, expressed no objection to this proposal to reverse the rate treatments adopted in OPUC Order No. 02-227, as long as all elements of OPUC Order No. 02-227 were reversed and accounted for. She testified as follows during cross-examination (TR 72-73).[3]

```
23     Q.  Okay.  So our proposal is to -- assuming our
24  proposal is to return the calculated benefit to PGE,
25  then that is a proposal that you would support;
 1  correct?
 2     A.  I still don't know if I'm understanding your
 3  question.  What proposal are you talking about?
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3. All TR references are to the transcript of July 10, 2008. Counsel was hampered in preparing this brief by the absence of the transcript until Saturday, July 19.

4   Q. The Lazar proposal to reverse out all of order
5 02-227.
6   A. Okay.
7   Q. Okay. You're saying that if the commission
8 were to apply such an approach, then the calculated
9 benefit that customers receive from the settlement
10 should be returned to PGE.
11   A. Uh-huh. Okay.
12   Q. If that -- if that benefit is returned to PGE,
13 then you would find the proposal, the Lazar proposal,
14 to reverse 02-227 to be acceptable?
15   A. Yes.

Her prepared testimony identified the items to be returned to PGE. She testified that, if the Commission were to apply the approach suggested by Lazar (unwinding the elements of OPUC Order No. 00-601 and OPUC Order No. 02-227), "then the calculated benefit that customers received from the settlement should be returned to PGE - for example, reversing the rate decrease on October 1, 2000; and the write-off of the residual balance sheet amount ($5 million); and adding a return on the FAS 109 liability to customer rates."

The Lazar proposal, described above, already explicitly accounts for the "rate decrease on October 1, 2000" and gives full credit for it back to PGE. The "write-off of the residual balance sheet amount ($5 million)" is sometimes referred to as the "rate credit." This write-off or "rate credit" is a chimera. It does not represent any particular cost that PGE absorbed and did not charge to ratepayers. It does not affect the cost to ratepayers of each of the OPUC Order No. 02-227 rate treatments described above (which add to $436,491,924). Even so, if the Commission believes otherwise, it can reduce the $436,491,924 owed to ratepayers by the amount of this write-off, escalated to October 1, 2008.

Whether the Commission has authority to refund the overcharge to ratepayers is a question, yet unresolved, addressed in previous phases of this remand docket. But ratepayers need not depend upon a Commission-ordered remand in order to recover the overcharges. Once overcharges are confirmed and not refunded, ratepayers can file a class action suit under ORS 756.185 to recover the overcharge. ***Dreyer v. Portland General Electric Co.***, 341 Or 262, 142 P3d 1010 (2006).

II. THE SPECIFIC SUB-ISSUES.

A. Issue 1: What was PGE's remaining undepreciated investment in Trojan as of October 1, 2000?

Here, the Phase 3 Scoping Order prohibits any evidence on how the Commission should have calculated the PGE's remaining undepreciated investment in Trojan as of October 1, 2000. It allows only "evidence regarding the actual Trojan balance as of October 1, 2000." Since the actual Trojan balance as of October 1, 2000, is a function of the books kept by PGE, we are precluded by the scoping order from presenting any contrary evidence on this subject. This restriction on the scope of evidence is clearly improper.

Nevertheless, we point out that the proper Trojan investment balance as of October 1, 2000, is not the $180.5 million claimed by PGE. As admitted by PGE witnesses in cross-examination, the actual Trojan investment balance on that date was zero. Witness Hager stated "that on the 1st of October there was nothing remaining in ratebase." TR 12.

Further, PGE method of calculating the Trojan investment balance failed to account for the actual charges to ratepayers for Trojan return of investment during the 5.5-year period that the OPUC Order No. 95-322 Trojan investment-related rates were in effect. PGE's method was shown in PGE's rebuttal testimony in UM 989 as follows:

Table 3 – Trojan Balances and Activity since UE-88

Period	Activity[1]	Balance
4/1/1995	--	$340,162,435
4/1/1995 – 12/31/1995	$(39,139,295)	$301,023,140
1/1/1996 – 12/31/1996	$(25,562,922)	$275,460,218
1/1/1997 – 12/31/1997	$(23,697,173)	$251,763,045
1/1/1998 – 12/31/1998	$(22,560,925)	$229,202,120
1/1/1999 – 12/31/1999	$(26,519,186)	$202,682,934
1/1/2000 – 9/30/2000	$(22,197,125)	$180,485,809

[1]Activity includes amortization, TIRA, retirements, salvage costs, etc. For the period 4/1/95 to 12/31/95, activity reflects the offset of $20.2 million pre-tax per Order 95-1216.

As witness Lazar demonstrated, without contradiction, the amount actually charged to ratepayers for Trojan return of investment did not decline during the 5.5-year period, as asserted by PGE's Table 3. Instead, the amount charged to ratepayers for Trojan return on investment and return of investment stayed the same in each year.

> I did not include that provision for accumulated depreciation, because PGE did not file any general rate cases to update its rate base or rate of return during the 5.5-year period. Therefore, while the Company undoubtedly DID accrue depreciation of its books, it DID NOT reduce the amount being charged to ratepayers. . . . The Company approach would be appropriate only if the Company had filed for annual rate reductions for the Trojan component of rates, which it did not.

Lazar, Exhibit URP 200 (May 18, 2005) in Remand Phase 1, p. 4. Lazar continued:

Declining Trojan Investment

Q. Please begin with the issue of the asserted declining Trojan investment. Why is this issue flawed?

A. While the Company did reduce the amount of Trojan carried on its books over this period, it did not reduce the charges to customers to reflect this reduction. Customers continued paying rates based on the amount at the time of the rate decision in 1995.

Q. In fact, did ratepayers pay even more than you calculated?

A. Yes. The 1995 Trojan balance was used to set rates. If sales volumes increased or decreased after that time, PGE's revenue for Trojan would track sales. While the Company's costs of carrying Trojan may have been declining, as the investment was amortized, the amount paid by ratepayers did not decline. It was set at the 1995 level and remained there.

Q. What happened to PGE sales between 1995 and 2001?

A. In 1995, PGE retail sales totalled 17.56 billion kilowatt-hours. In 2001, those had increased to 19.04 billion kilowatt-hours. Therefore, PGE consumers were paying about 8% MORE than the amount I assumed by 2001, even though PGE's cost of carrying the Trojan investment had declined.

Q. What finding should the Commission make on this issue?

A. The Commission should find that my original assumption was conservative. It should not be adjusted downward. The fact that PGE's costs (balance of Trojan investment on its books) declined during the 5.5-year period is irrelevant to measuring what the PGE consumers paid during this period.

Lazar, Exhibit URP 300 (August 1, 2005) in Remand Phase 1, pp. 2-3.

PGE’s Table 3 above can be used to illustrate what PGE actually charged to ratepayers for Trojan return of investment during the 5.5-year period. The amount must have been more than the $25,562,922 charged for 1996, since the PGE table reflects a declining balance amortization of the Trojan investment. So ratepayers were

actually charged not less than $25.56 million for Trojan return of investment annually during the 5.5-year period. It is obvious that the Table 3 "Activity" numbers include elements other than merely declining balance amortization of the Trojan investment, as the numbers do not decline in an orderly progression. Development of the exact numbers was precluded by the Phase 3 Scoping Order, which stated (p. 7):

> Furthermore, URP's request for a month-by-month accounting of the exact amounts collected in rates from April 1995 through September 2000 for the return of and the return on PGE's remaining Trojan investment reflects a misunderstanding of utility accounting. The money collected in rates is not color-coded or otherwise earmarked to be used for certain purposes. The records sought by URP simply do not exist.

The Commission should countermand the Phase 3 Scoping Order issued by the ALJ and require PGE to produce the monthly detailed information. Failing to do so denies fundamental due process to URP/CAPs by excluding the development of centrally relevant facts.

The bottom line is that the Trojan investment balance should have been reduced by the amounts PGE ratepayers were actually paying for Trojan return of investment during the 1995-2000 5.5-year period preceding October 1, 2000. The hearing officer has refused to allow the discovery of this information. Because PGE did not annually adjust its Trojan charges to ratepayers downward, there is no justification for reducing the Trojan investment balance by the assumed declining balance for Trojan on PGE's books of account.

B. Issue 2: Do the rates approved in Order No. 02-227 provide PGE with the functional equivalent of a "return on" the remaining undepreciated investment in Trojan?

Yes, they do, for several reasons.

First, the rates provide the functional equivalent of a "return on" the remaining undepreciated investment in Trojan, because the "net benefit analysis" which formed the basis for OPUC Order No. 02-227, assumed that the baseline for measuring "net benefit" would be the continued, unabated collection by PGE of a return on investment for Trojan through 2011. The "net benefit analysis" did not compare the rate treatments proposed in UM 989 with a legal baseline, which would certainly not include continued return on investment for Trojan. The Commission then concluded that the rate treatments adopted in OPUC Order No. 00-601 and OPUC Order No. 02-227 were just and reasonable, because they would be better for ratepayers than the only alternative considered by the Commission--the continued, the unabated collection by PGE of a return on investment for Trojan through 2011.

The PGE witnesses admitted that the "net benefit analysis" assumed continued return on Trojan. Exhibit URP 600, prepared by PGE, quantified the amount of return on Trojan they assumed each year through 2011 and the assumed income tax liability that would accompany that return on investment. TR 16-17.

The second reason is that the "stipulation" approved by OPUC Order No. 02-227 caused ratepayers to trade interest-earning assets which are due them for a non-interest earning asset (Trojan) held by PGE. PGE and Staff have agreed that the "offset" accounts shown in Staff-PGE Exhibits 203-205 (AR 269-71) (totalling at least

$161.9 million) were interest- or return-bearing accounts. The majority of the credits to ratepayers cancelled under the "Stipulation" were those stemming from the Enron acquisition of PGE (M Credit) and from the power sale contract settlement with Southern California Edison Co. (SCE). These accounts and the others listed as "offsets" were credits to ratepayers which accrued interest for the benefit of ratepayers at the company's post-tax authorized return on investment. The trading of a non-return bearing Trojan ratebase amount in exchange for the cancellation of return-bearing credits that PGE owes to ratepayers produces the functional equivalent of a "return on" the remaining undepreciated investment in Trojan.

The entire trade is, from a ratepayer perspective, absurd. Imagine that I offer to trade to you $300 million in zero-coupon U.S. Treasury bonds due in 2012. In exchange, I would receive from you $300 million in U.S. Treasury bonds, also due in 2012, which carry a 7% rate of interest. Would anyone consider this a reasonable exchange of value? Obviously not, because the zero-coupon bonds are worth far less than the bonds which carry the 7% rate of interest. This is the utility-industry equivalent of Wimpy's adage: "I will gladly pay you tomorrow for a hamburger today," except in this case Wimpy is offering to pay you that same hamburger more than 10 years from now.

Staff witness Judy Johnson recognized this, when during cross-examination she stated that she would not trade $200 million of interest-bearing bonds in exchange for $200 million of non-interest-bearing bonds.

21 Q. Now, let's say that you have a $200 million
22 bond that carries a rate of 12 percent and has a term

23 of ten years, and say I have a $200 million bond that
24 matures in ten years and has a 0 coupon, 0 percent
25 interest.
1 Would you agree to swap your bond for mine?
2 MS. ANDRUS: Objection. Relevance. What
3 Miss Johnson would do with respect to a personal
4 financial transaction, that has no relevancy to the
5 analysis.

[DISCUSSION OF OBJECTIONS OMITTED]

4 ALJ GRANT: I think that objection goes
5 more to the weight rather than relevance. I'll
6 allow the question.
7 THE WITNESS: Okay.
8 BY MR. MEEK:
9 Q. So are you ready to swap your interest-bearing
10 bond for my zero coupon bond?
11 A. No, I am not.
12 Q. Why not?
13 A. Because I might be able to get some interest.
14 Q. Because the bond that you own in this
15 hypothetical does carry 12 percent interest. You
16 would not swap that for a 0 percent bond carrying the
17 same face value.
18 A. I personally would not.
19 Q. And would a reasonable person swap those bonds?
20 MS. ANDRUS: That calls for a legal
21 conclusion, Judge. I object.
22 ALJ GRANT: I'll allow it. You're
23 basically asking her opinion, so I'll allow her to
24 provide her opinion.
25 THE WITNESS: I would say a reasonable
1 person probably would not.

TR 73-76. Yet, it is exactly this trade that OPUC Order No. 02-227 imposed on PGE ratepayers, and the "net benefit analysis" treats the face value of interest-bearing accounts as exactly equivalent, and tradeable one-for-one, with the face value of the non-interest bearing account, the Trojan investment balance.

The forced trading of interest-bearing accounts due to ratepayers in exchange for an account which by law must be non-interest bearing has exactly the same result as placing the remaining Trojan investment into ratebase which earns a return on investment. OPUC Order No. 02-227 removed from PGE's rate calculations credits of

at least $161.9 million that PGE admittedly owed to ratepayers, all of which were carried on PGE's books in accounts which earned a return on investment for the ratepayers and credited to the ratepayers on an annual basis. Cancelling these accounts produces an exactly equivalent result as placing a $161.9 million item into return-bearing ratebase, but in a roundabout route which is what ORS 757.355 prohibits. It forbids return on investment, whether such is accomplished "directly or indirectly."[4] Given that the forced trade is economically irrational and unjustified, the roundabout nature of accomplishing the detrimental rate impact on ratepayers certainly seems indirect in the more sinister meaning: "not straightforward; not fair and open."

C. Issue 3: Was the FAS 109 liability properly considered part of PGE's return of its Trojan investment?

No, the FAS 109 liability was not *properly* considered part of PGE's return of its Trojan investment. Instead, the creation of this liability by the Commission constituted a means for allowing PGE to charge ratepayers more than the depreciated investment balance of Trojan. Its creation merely allowed PGE to charge ratepayers an extra $47.4 million over approximately 6 years.

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4. The usual and primary definition of "indirectly" means not directly, obliquely, in a roundabout manner, dishonestly. ***Rust v. Missouri Dental Board, [348 Mo***. 616,] 155 SW2d 80, 83 (1941). WEBSTER'S DICTIONARY (College Edition 2001): "not direct, specifically a) not straight; deviating; round about; b) not straight to the point; or to the person or thing arrived at; as, an indirect reply; c) not straightforward; not fair and open; dishonest; * * *." Accord, MERRIAM-WEBSTER (on-line 2008): "not direct: as (a)(1): deviating from a direct line or course: roundabout (2): not going straight to the point <an indirect accusation> * * * (b): not straightforward and open: deceitful * * *."

PGE claims that the "Trojan FAS 109 asset represents the value of accelerated tax benefits previously flowed through to customers that are expected to reverse over time through higher tax expense in future years." Missing from the evidence is any statement that PGE thereupon experienced the higher tax expense. The Circuit Court Opinion and Order (p. 6) reversing OPUC Order No. 02-227 highlighted this lack of evidence.

> Frankly, this Court would be inclined to agree with Plaintiffs as to some of these additional claims, particularly with respect to the handling of the FAS 109 amounts and the final NEIL distribution. Charging rate payers for purported increases in PGE taxes without requiring proof that those taxes were ever actually paid is certainly questionable. Similarly, no persuasive explanation was offered to justify the shift of much of the final NEIL insurance refunds from the rate payers to PGE.

Further, the entire rationale for creating this "asset" and making ratepayers pay for it is that "Trojan FAS 109 asset represents the value of accelerated tax benefits previously flowed through to customers **that are expected to reverse over time through higher tax expense in future years**." The crucial question, then, is whether, at the time of the issuance of OPUC Order No. 00-601 and/or OPUC Order No. 02-227, did PGE have a reasonable expectation that it would, as a result of the Trojan FAS 109 "reversal," have a "higher tax expense in future years." On cross-examination, the PGE witnesses were specifically asked whether PGE had a reasonable expectation that it would be paying income taxes to either the federal or statement governments in each of the years over which the Trojan FAS 109 asset was charged to ratepayers (2001 - first quarter of 2006). PGE counsel refused to allow the PGE witnesses to answer the question. Thus, PGE has itself procured the absence of

evidence in the record to support its claim of an "expectation" that "higher tax expense in future years" would occur.

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 5     Q.  As of September 30th, 2000, did PGE have a
 6  reasonable expectation that it would be paying income
 7  taxes to the federal government in 2001?
 8            MR. CONABLE:  Objection.  Lack of
 9  foundation.
10            MR. MEEK:  Doesn't need a foundation.
11            ALJ GRANT:  Are you referring to some
12  testimony there?
13            MR. MEEK:  Sure.  We're back to the --
14  there's a reference -- of course, a reference to
15  testimony is not a foundation, but --
16            PGE 7500, Page 6, lines 11 through 13,
17  refers to PGE's expectation about tax expenses in
18  future years.
19            ALJ GRANT:  So will you ask your question,
20  Mr. Meek.
21            MR. MEEK:  Can you read back the question.
22            (The reporter read the pending question as
23            follows:
24            Question:  As of September 30th, 2000, did
25            PGE have a reasonable expectation that it
 1            would be paying income taxes to the
 2            federal government in 2001?)
 3            MR. CONABLE:  For my objection, the basis
 4  is not that these gentlemen haven't testified about
 5  higher tax expense.  It's been that there's been no
 6  testimony in the -- contrary testimony on the idea
 7  that PGE expected, reasonably or otherwise, to make
 8  tax payments to the federal government in 2000.  It's
 9  simply not the statement in the testimony.
10            Mr. Hager said repeatedly that PGE
11  expected to have a tax expense on the stand-alone
12  basis and to make a payment on that basis.  So
13  whether PGE had a reasonable expectation of making a
14  tax payment to the federal government has not been
15  this testimony, nor does it come from the scope of
16  it.
17            ALJ GRANT:  Mr. Meek, no response?
18            MR. MEEK:  No.
19            ALJ GRANT:  Then I'll strike the question.
20            MR. MEEK:  Then I would make a
21  representation that I would ask the same question for
22  the years 2002, 2003, 2004, 2005 and the first
23  quarter of 2006, and I would also have the same
24  question with regard to PGE's having a reasonable
25  expectation that it would pay income tax -- or paid
 1  income taxes to the state government in each of those
 2  years, and so I propose to ask those questions as
 3  well.
 4            ALJ GRANT:  Just to clarify your question,
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 5  as of --
 6             MR. MEEK:  September 30th.
 7             ALJ GRANT:  Whether they had expectations
 8  of paying taxes in any of those years?
 9             MR. MEEK:  Yes.
10             ALJ GRANT:  All right.  Same ruling.
11  Beyond the scope.
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TR 66-68. When asked about what federal or state income taxes were actually paid by PGE between 1998 and 2006, the PGE witnesses repeatedly stated their lack of knowledge.

Staff asserts that the FAS 109 asset should indeed be charged to ratepayers. Staff claims that it is fine to have created this "asset" and then charge PGE ratepayers to pay for the asset. Staff's approach assumes that, in the early years of Trojan operation (1970s -1980s) that, because of accelerated depreciation and other features of federal and state income tax laws, PGE ratepayers paid less in income taxes than would have been "normal"--i.e., than would have been the case if these tax law features did not exist and the Trojan investment (for tax purposes) were depreciated ratably over its expected operating life and did not generate any investment tax credits. Thus, reasons PGE and Staff, having paid less than "normal" income taxes in the early years of Trojan operation, ratepayers should now pay more than "normal" income taxes.

This analysis is flawed for several reasons. First, there is no evidence that PGE paid any of its asserted federal and state "income taxes" at any time prior to 2006 (after the tax reporting requirements of Oregon's SB 408 of 2005 took effect). It is now known that the amount of federal and state income taxes paid by or on behalf of PGE under its Enron ownership (1997 - early 2006) was effectively zero, despite the fact that PGE was reporting to the OPUC "income tax" expenses on the order of $80 to $100 million per year. Prior to its ownership by Enron, PGE had its own corporate hierarchical structure and may or may not have paid in income taxes the amounts asserted in its reports to the OPUC. So there is no proof that PGE ratepayers in the

early Trojan years were somehow benefitting from accelerated depreciation or other tax features applicable to the Trojan investment.

More important, the "net benefit analysis" assumes that PGE (as of October 1, 2000) was somehow required to pay more in income taxes than "normal" for the remainder of Trojan's originally expected operating life (to 2011), because the effects of accelerated depreciation and other tax features applicable to the Trojan investment had "reversed" so that the result of all of the separate depreciation accounts would reach zero at the end of Trojan's expected operating life. But there were effectively no federal and state income taxes paid by or on behalf of PGE during the first 5.5 years after October 1, 2000, the effective date of the rate orders in UM 989. During 2003, PGE did pay $789,510 in federal income taxes in 2003, offset by a net refund of $63,265 in 2002. See Exhibit URP 601.

So, OPUC Order No. 00-601 and OPUC Order No. 02-227 apparently required PGE ratepayers to pay not only for income taxes that were not being paid to the federal or state government but also to pay extra income taxes, above and beyond "normal." Under those orders, the FAS 109 "asset" was charged to ratepayers over a 5-year period commencing October 1, 2000--during the same period that PGE was not actually paying any income taxes. Thus, those orders required PGE ratepayers to pay an extra $47.4 million for alleged PGE income taxes costs, even though there existed no actual payments of those income taxes to the federal or state governments and thus no actual "costs" to cover.

PGE currently contends in these remand dockets that, once a rate treatment is reversed and remanded by the courts, it is *void ab initio*. PGE's Opening Brief with respect to the Authority of the PUC to Award Relief (June 20, 2007), pp. 13-14.[5] The remanded rate treatment must then be replaced by another rate treatment, under

5. The entire rate order may not be *void ab initio*, because it may contain rate treatments that are lawful and are independent of the rate treatment that is reversed and remanded. In UM 989, however, there was only one rate treatment at issue, the rate treatment of the Trojan investment.

PGE's theory of ratemaking. Obviously, the new rate treatment must comply with laws applicable to OPUC ratemaking at the time of the decision adopting the new rate treatment. SB 408 (2005) deems rates not to be "fair, just and reasonable," if they "include amounts for taxes" which do not "reflect the taxes that are paid to units of government." ORS 757.267(1)(f). The effective date of this new standard was September 5, 2005, as recognized in OPUC Order No. 06-379 and OPUC Order No. 07-351. The new standard applies to rate orders issued after that date. Thus, this new standard obviously applies to the OPUC's rate order to be issued in this remand docket. An order allowing PGE to charge ratepayers for the FAS 109 asset would be a violation of SB 408, because it would impose rates that include the cost of income taxes that were not actually paid to government.

Further, if PGE had not been allowed to charge ratepayers for the full return on investment on Trojan, PGE would have been compelled to write off a large share of its remaining Trojan investment. That write-off would have reduced PGE's reported net income and, accordingly, its nominal income tax liability. Thus, OPUC Order No. 02-227 forces ratepayers to pay even more in income taxes, because it preserves for PGE the functional equivalent of a return on investment on Trojan.

D. Issue 4: Did the rates approved in Order No. 02-227 improperly transfer the proceeds and/or premium rebates from PGE's NEIL policy from ratepayers to PGE?

Yes. PGE agreed that the premiums paid to NEIL have previously been included in the test years upon which PGE rates have been based and that previous NEIL distributions back to PGE have been credited to ratepayers. Thus, PGE agreed that ratepayers have paid the NEIL insurance premiums and in the past have received any rebates of those premiums from NEIL to PGE. Consequently, the diversion of 45% of all future distributions by NEIL to PGE represents a new net cost to ratepayers,

because it removes from them money that has been credited to ratepayers in the past.

The record shows that this new OPUC Order No. 02-227 treatment of NEIL rebates has cost ratepayers at least $15.4 million in NEIL rebates diverted to PGE's shareholder (45% of the $34.3 million payment by NEIL to PGE that occurred) in October 2000. Here again, the situation is quite simple: the ratepayers paid the underlying premium that gives rise to the rebate, and are entitled to the rebate.

Diverting NEIL distributions to PGE's shareholder contradicts the fundamental tenets of ratemaking. Ratepayers paid the premiums. Over the years, NEIL found that it was not necessary to use all of the premium revenue to pay claims and administrative costs, so it has been returning the surplus funds to its members, including PGE. Since the premiums were counted as a cost charged to ratepayers, then return of surplus premiums should be credited to ratepayers.

Allowing shareholders to capture the premium rebates opens a hole through which the utility can funnel tens of millions of ratepayer dollars into the pockets of its shareholders. It is a "heads I win, tails you lose" system, where the costs are borne by ratepayers but subsequent rebates are diverted to the shareholder. As noted by witness Lazar:

> I have said in many of the courses I teach in utility regulation: "***All regulation is incentive regulation***." The clear incentive of accepting PGE's position in this docket would be for the Company to intentionally acquire excessive insurance, the premiums for which could be included in test year operating expenses, knowing that there was a likelihood of receiving future refunds that could be flowed to shareholders.

In prior phases of this docket, PGE has argued that "PGE's shareholders were subject to a variety of risks for these payments. For example, PGE's shareholders bore the risk that premiums would increase between rate cases, that NEIL might experience a greater number of claims than anticipated, and that the NEIL investment strategies might fail." All this is true in the opposite direction. Ratepayers were also subject to a variety of risks. Under the Commission's approach, they would have continued to pay higher NEIL premiums between rate cases, even if the actual NEIL premiums were reduced. As for NEIL investment strategies failing, NEIL investment strategies could have been more successful, also. There is no evidence as to the astuteness or success of those investment strategies. All the record shows is that NEIL is distributing money back to the utilities from which they derived the premiums but that it was PGE ratepayers who paid the premiums, not PGE's stockholders.

There can be no credible suggestion that the NEIL rebates to PGE would be considered unusual or non-recurring events that would be disregarded when setting rates. PGE paid premiums to NEIL every year, until 1994. PGE received NEIL "distributions" in every year between 1987 and 1999 (steadily increasing from $239,000 in 1987 to $4.97 million in 1999), before PGE received the $34.3 million "settlement" in 2000. Distributions from NEIL were not unusual and were not non-recurring. In addition, the $34.3 million "settlement" money from NEIL was not unexpected. PGE spent considerable time negotiating that settlement and examined numerous "scenarios." It is outrageous for a regulator to allow a utility to retain for shareholders a 45% share of a "settlement," when the fund at issue consists of money

paid in by ratepayers. It is beyond outrageous to suggest that this can be fully planned by the utility and then disregarded as a non-recurring event.

The bottom line is that there is no dispute that the 100% of the NEIL premiums had been forecasted and fully included in rates and were paid for by ratepayers. In Phase 3 discovery, PGE refused to indicate which of its payments to NEIL it has ever excluded when presenting its test year cost of service in every general rate case since the beginning of transactions between PGE and NEIL. It also refused to state which of the payments it has received from NEIL it has previously excluded when presenting its test year cost of service in general rate cases. Having refused to provide the requested information, PGE cannot later claim that maybe those premium payments were somehow not fully included in rates.

But OPUC Order No. 02-227 nevertheless diverted 45% of the premium rebates away from PGE ratepayers. This is contrary to the principles of ratemaking and opens the door to future abuse. Such abuse was recognized as a real problem by the Circuit Court in its review of OPUC Order No. 02-227:

> Clearly at least a potential source of mischief, adoption of the filed rate doctrine in the form urged by PGE could well encourage increasingly aggressive and perhaps even deceitful utility rate proposals. Once approved by the OPUC, the full financial benefit of all rates collected, no matter how poorly warranted and justified, would be permanently locked in and would never become refundable even when finally determined to be unlawful after years of successive court appeals. In short, Defendants' version of the filed rate doctrine has more in keeping with the satiric scenarios of Joseph Heller's *Catch 22* and Lewis Carrol's *Through the Looking Glass* than with responsible utility rate regulation.

Allowing PGE shareholders to retain the NEIL distributions paid for by ratepayers would fit nicely with the writings of Heller and Carrol.

Staff's position on the NEIL rebates is a flawed policy position for a regulatory staff to assert. Staff asserts:

> If the benefit [NEIL premium rebate] came in between rate cases, customers may not have benefited at all. In addition, even if the benefits were recognizable during a test period, the crediting of a NEIL benefit might have been considered a one-time occurrence for purposes of a rate case and removed from the test period as a non-recurring item.

This approach would bless any scheme under which the utility makes regular payments (or overpayments) to some other entity and then later receives a lump sum settlement or rebate. The regular payments would of course be included in the test years upon which rates are based. But, says Staff, maybe the lump sum settlement or rebate would be ignored. Thus, the utility can handsomely profit merely by making estimated "pre-payments" (or arranging to overpay vendors on a regular basis) and then receive lump sum true-ups from the vendors, conveniently scheduled between rate cases or conveniently labeled "non-recurring items." This is another "heads-I-win--tails-you-lose" technique that Staff should not be endorsing. It is also contrary to the practice OPUC staff recommended regarding distributions of the proceeds from the multi-state settlement paid by the Williams Companies, Inc., to settle suits brought by the Attorneys General of California, Washington and Oregon for price manipulation and antitrust violations for its manipulations of wholesale prices during the West Coast energy crisis in 2000.[6] (The Oregon share of the Williams Settlement proceeds were distributed on a one-time basis to current customers, based on estimates of each customer's usage in the month of distribution.)

Finally, in discovery PGE has provided no additional NEIL transactions. Thus, we must assume that NEIL provided no further money to PGE. PGE is obligated to negate that assumption, if it is not true.

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6. "AG Announces Distribution on Williams $15 Million Settlement," March 13, 2003, on the Oregon Department of Justice website, http://www.doj.or.us/releases/rel031303.htm.

E. Issue 5: Were the rates approved in Order No. 02-227 just and reasonable?

In the original Commission proceeding and on appeal, PGE's justification for the massive shifts of costs onto ratepayers and massive shift of benefits to shareholders is that ratepayers were still better off, under the "net benefit analysis" in the stipulation.

PGE and Staff admitted that, as of the end of the first year after implementation of the OPUC Order No. 00-601 rates (also adopted by OPUC Order No 02-227 at the culmination of the contested case proceeding), the result of adopting the "Stipulation" was to **increase** rates by $25.7 million in Year 2, to **increase** rates by $15.7 million in Year 3, and to **increase** rates by $15.7 million in Year 4. Staff-PGE Exhibit 204 (AR 270), column 17; TR 115-18 (AR 429-32). And this is $25.7 million on top of and in addition to the level of rates that the Oregon courts declared unlawful in ***CUB/URP v. OPUC***, because those rates included Trojan return on investment (profit).

OPUC Order No. 02-227 is seriously misleading on this subject, stating that the "Stipulation" results in a rate reduction of at least $10.2 million over first 12 months (October 1, 2000 - 2001) and an additional $2.5 million reduction in the future. These claimed "rate reductions" are in comparison to the assumed continuation of the OPUC Order No. 95-322 rates regarding Trojan investment, which the Oregon courts have found to have been unlawful due to inclusion of Trojan return on investment.

The amounts that PGE claims as a "benefit" for ratepayers in its net benefit analysis include an unspecified amount of Trojan return on investment. When

specifically asked for the Trojan amortization amounts from past years, Staff and PGE did not provide them. TR 42-43 (AR 356-57).

PGE witness Hager admitted that none of their testimony identified the amounts of amortization, return on investment, or other elements of the Trojan investment-related revenue requirement. TR 45. The PGE witness guessed that the amount of amortization (return of investment) in the $59 million alleged first year benefit from removing the Trojan investment-related annual revenue requirement (shown in Staff-PGE Exhibits 203, 204, 205) was $24 million.

The uncontroverted evidence now shows that the Trojan profits authorized in OPUC Order No. 95-322 were $35.202 million per year. Exhibit URP 202, p. 2. Thus, the net benefit calculations offered by PGE are based upon the assumption that removing the very charges found unlawful by the Court of Appeals is counted as a huge "benefit" for ratepayers. So, PGE's alleged "$16-18 million rate reductions," even if in any way accurate, would represent a reduction from a baseline that itself is unlawful by easily over $125 million.

In addition, the "net benefit analysis" adopted by OPUC Order No. 02-227 was conceptually and mathematically faulty for several reasons:

1. It used an incorrect discount rate, consisting of PGE's authorized rate of return on investment without taxes.

In the ratemaking methodologies used by the OPUC, that number is merely an intermediate step to determining the actual authorized multiplier applied to PGE's ratebase in order to calculate the actual rates charged to ratepayers. Applying the

“without taxes” rate of return skips over the Net-to-Gross step in the cost of capital calculations. There is no legitimate rationale for skipping that step.

2. It used an inconsistent discount rate, applying a higher rate of return to PGE’s Trojan return on investment in order to inflate the alleged benefit of stopping that return.

On cross-examination, PGE witness Hager admitted that the "net benefit analysis" actually did escalate the assumed continued OPUC Order No. 95-322 Trojan investment revenue requirement by PGE’s pre-tax return on investment, listed on Exhibit URP 600, p. 2, as 12.97%.

5 BY MR. MEEK:
6 Q. Back to the questions on Page 2. Ask you to
7 look at Page 2, column F, which is entitled, Pretax
8 return on investment 12.97 percent. Are those -- is
9 that the return on Trojan investment that was assumed
10 in the revenue requirement based test model?
11 A. (By Mr. Hager.) It does appear that way.
12 Again, I look at Exhibit -- Staff PGE 204, and I can
13 match the revenue requirement, check numbers there
14 with what is in that -- with these numbers here, so
15 it would appear that way.

So it appears that PGE selectively applied a much higher assumed rate of return to the "continue OPUC Order No. 95-322" case than to the "stipulation" case. This would have greatly inflated the alleged benefit of the "stipulation" case.

3. It used an incorrect baseline, consisting of continued full recovery of Trojan return on investment.

The "net benefit analysis" is also fatally flawed by its baseline. It allegedly finds a small benefit for ratepayers, compared to an alternative which consists of continuing in place the unlawful rate treatment for Trojan adopted in OPUC Order No. 95-322.

Staff's testimony asserts that somehow ratepayers are better off under OPUC Order No. 02-227. That is not the case. Lazar's testimony shows how much worse off they are. The correct measurement of the relative position of ratepayers is in my testimony, which shows the effect of:

(1) reversing out all of OPUC Order No. 00-601 and OPUC Order No. 02-227, thereby returning ratepayers to the status quo ante on September 30, 2000, from a ratemaking perspective;

(2) in its place, removing as of October 1, 2000, all Trojan return on investment from rates, while continuing to charge the same Trojan return of investment as had previously been authorized in OPUC Order No. 95-322, because the courts ruled that Trojan return on investment was unlawful.

Lazar's testimony shows that ratepayers are, as of October 1, 2008, $436.4 million worse off under OPUC Order No. 00-601 and OPUC Order No. 02-227 than they would be, if instead the Commission in 2000 had adopted a order producing fair, just, reasonable, and lawful rates by removing the Trojan return on investment from PGE rates and doing nothing else.

4. It counted as a benefit not charging ratepayers for CWIP on Trojan.

OPUC Order No. 02-227 contends that the $10.3 million in construction work in progress (CWIP) included in the Trojan balance as of September 30, 2000, was for contracts "that would have been transferred to a plant in service account," if indeed the fuel had been delivered and consumed. But it was not. "When Trojan closed prematurely, these contracts and other projects were cancelled and remained in accounts as CWIP." ER-15.

OPUC claimed that ORS 757.355 does not prohibit a utility from charging CWIP to ratepayers. But, throughout the last 12 years of litigation, the OPUC has consistently stated that CWIP is the only type of charge that ORS 757.355 does ban. This is discussed at length at ***CUB/URP v. OPUC***, 154 Or App at 708-11, 962 P2d at 747-49. For example:

> PUC and PGE agree that the language of the statute and the history of measure 9 demonstrate that the target of the measure and the concern of the statutes are with rates for "construction work in progress" (CWIP), i.e., uncompleted facilities or those planned for prospective use that are not yet in use. * * *
>
> In the present case, there are at least two aspects of the surrounding statutory language that are at odds with PUC's and PGE's understanding that the word "presently" and the statute relate only to CWIP and do not also apply to facilities and plant that are no longer in use.

Id., 154 Or App at 708, 962 P2d at 747.

> PUC argues further, however, that the "legislative history" of Measure 9 demonstrates that its concern, as communicated to the electorate, was exclusively with CWIP.

OPUC does not explain why "ORS 757.355 does not encompass CWIP attached to an operating plant." OPUC in its brief to the Court of Appeals in ***Utility Reform Project v. OPUC***, 215 Or App 360, 170 P3d 1074 (2007) [hereinafter "***URP v. OPUC*** (UM 989)"] (p. 28) further stated:

> Had Trojan not closed, those contracts would have been included as part of the Trojan investment base.

True, but Trojan ***did*** close. If Trojan had remained operating, there would not have been a violation of ORS 757.355, as recognized in ***CUB/URP v. OPUC***.

OPUC in that brief also stated that "the CWIP would have eventually become plant in service in the future under the 'no closure' scenario." Yes, but the "no closure" scenario did not come to pass. Whether or not including such costs in one or

both sides of an equation would cause the outcome of the equation to be different is immaterial. Yes, it is true, as the OPUC brief (p. 28) stated, "The closure alternative would always have the benefit of excluding CWIP costs that would be included in the no closure alternative," because, in the "no closure alternative," there is no ban on charging CWIP to ratepayers.

OPUC (pp. 28-29) then claimed that the CWIP was added to the Trojan investment balance "at the time the closure decision was made in 1994," although the closure decision was made in January 1993. In any event, OPUC Order No. 02-227 applies to rates taking effect on October 1, 2000, and any failure to object to this CWIP in earlier rate cases is not relevant. This $10.3 million imposed upon ratepayers by OPUC Order No. 02-227 constitutes additional charges banned by ORS 757.355.

5. It inflated the asserted benefit by a faulty assumption about future rate changes.

The entire case for the "Stipulation" rests upon the assertion that it somehow produced a small net benefit for ratepayers, compared with the alternative scenario of continuing to charge ratepayers both return <u>of</u> investment and return <u>on</u> investment, regardless of the decision in ***CUB/URP v. OPUC***.

The Staff-PGE net benefit analysis assumed that the $59 million Trojan investment-related annual revenue requirement would have continued for the full calendar year of 2001, based on the mere assumption that there would be no general rate revision effective prior to January 1, 2002. Their net benefit analysis assumed that, as soon as a general rate revision became effective, the annual Trojan investment-related charges would fall from $59 million to $33.3 million, which is $25.7 million less. Staff-PGE Exhibits 203-205 (AR 269-71).

The reason for this huge drop in annual charges under the "no settlement" scenario is that PGE had no general rate revision between 1995 and 2001, so the amount set for annual Trojan investment-related charges to ratepayers stayed at $59 million, even though on its books of account PGE was assuming that the charges were going down each year (being based on a declining investment balance as each year's depreciation was taken). With a new general rate case, the Trojan investment-related charges would be reset so that ratepayers would be paying both depreciation and return on investment on the new Trojan investment balance (although that balance would remain artificially high).

In any event, the Staff-PGE net benefit analysis was not an annualized analysis. It was an analysis that went at least 12 years into the future and then reduced the expected costs and revenues to present value. Part of the stream of "costs" that ratepayers were assumed to bear in the "no settlement" scenario was payment of full return of investment and return on investment for Trojan, according to the terms of OPUC Order No. 95-322 (despite its reversal by the courts) until January 1, 2002. After that, under the "no settlement" scenario, the cost of the Trojan investment to ratepayers would sharply decline, because of the situation described in the previous paragraph.

In reality, however, PGE did not want to wait until January 2002 to get new rates under a new general rate case. The general rate case order that actually took effect for PGE on October 1, 2001 (UE 115 docket) granted to PGE an overall rate increase of 38%. OPUC Order No. 01-777 (August 31, 1997). The percentage increase was

noted in the order denying reconsideration, OPUC Order No. 01-988, p. 1. This amounted to an increase in revenue requirement of about $400 million per year. Getting this rate increase in place faster, however, had the effect of rendering the Staff-PGE net benefit analysis in UM 989 incorrect by a sum of one quarter of the difference between $59 million and $33.3 million. Thus, the Staff-PGE net benefit analysis, simply by assuming that the $59 million Trojan investment-related annual revenue requirement would have continued for the entire calendar year of 2001, TR 30 (AR 344), overstated the alleged "benefit" to ratepayers by one-quarter of $25.7 million, which equals $6.425 million. All of the parties knew this, long before the OPUC issued OPUC Order No. 02-227 in 2002, since the order increasing PGE's rates on October 1, 2001, OPUC Order No. 01-177, issued on August 31, 2001.

This also illustrates the underlying illogic of the "net benefit analysis." Merely by assuming that the unlawful rate treatment, allowing Trojan return on investment, would continue for some future period, the OPUC could have inflated the alleged "net benefit" for ratepayers to any desired level. This inflation of alleged benefit would then have justified, according to the OPUC, PGE and Staff, any number of other highly irregular transactions and adjustments to as to move money owed to ratepayers out of their pockets and into the pockets of PGE shareholders.

6. It appears that, even with the erroneous inflation and faulty assumptions, the final calculation of the "net benefit" was only $1.5 million.

PGE provided in discovery a spreadsheet file named Net Benefit Analysis Corrected Original.xls. It shows a corrected "Net benefit before NEIL split" of $1.5

million. It then adds $13.1 million to that for "55% of NEIL Value to Customers." Thus, it counts as a "net benefit" to ratepayers the return to them of 55% of the known NEIL distribution. But the principles of ratemaking would require that 100% of the NEIL distributions be returned to ratepayers, because ratepayers paid 100% of the premiums that are being re-distributed to PGE. Merely following ratemaking principles does not confer a "net benefit" on ratepayers, merely because ratepayers could indeed be made worse off by disregarding ratemaking principles and simply allowing the utility any number of "heads-I-win--tails-you-lose" arrangements, with ratepayers paying in amounts that shareholders then withdraw. A "net benefit" to ratepayers from any scenario or proposed rate treatment must have a lawful and principled rate treatment as the baseline for comparison. It is clear that the "net benefit analysis" in this docket has neither.

F. Issue 6: Was Order No. 02-227 supported by adequate findings of fact and conclusions of law?

This issue appears to be moot. The Court of Appeals remanded OPUC Order No. 02-227 to the Commission, which will produce a new order containing new findings of fact and conclusions of law.

G. Issue 7: Did the Commission deny URP due process in docket UM 989?

On this issue, we rely upon the content of the briefs filed in the Court of Appeals, for which we request official notice. Those briefs are available upon request to those not possessing them.

III. ADDITIONAL LEGAL ISSUES.

A. THE COMMISSION HAS ERRED IN RESTRICTING THE SCOPE OF THE REMAND PROCEEDING TO EXCLUDE THE ONE ISSUE EXPRESSLY REMANDED BY THE COURT OF APPEALS.

The Court of Appeals in ***Utility Reform Project v. OPUC***, 215 Or App 360, 170 P3d 1074 (2007) [hereinafter "***URP v. OPUC*** (UM 989 appeal)"], expressly analyzed one issue: Whether the Commission in OPUC Order No. 02-227 should have considered the return on Trojan previously received by PGE under OPUC Order No. 95-322 in determining the correct Trojan investment balance as of September 30, 2000. Over the objection of URP, the Phase 3 Scoping Order excluded that very issue. Thus, the Commission excluded on remand consideration of the issue that the Court of Appeals singled out as representing legal error by the Commission.

A remand is supposed to deal with the agency decision on one or more issues found by the courts to have been unlawful or otherwise invalid. ***Bank of Commerce v. Ryan***, 157 Or 231, 234, 69 P2d 964 (1937). Here, the Commission erred by excluding the only such issue identified by the Court of Appeals in ***URP v. OPUC*** (UM 989 appeal).

B. THE COMMISSION HAS ERRED IN REFUSING TO HEAR ANY ISSUES NOT RAISED IN THE ORIGINAL UM 989 PROCEEDING OR IN THE APPEAL OF THE UM 989 FINAL ORDER.

In this Phase 3, the Commission restricted the issues to include only those that had been raised in the original UM 989 proceeding or on appeal of the orders produced by that proceeding.

In Phase 1 of this consolidated remand docket, however, the Commission expressly rejected the URP/CAP position that the issues in that phase should have been similarly restricted. Instead, at the urging of PGE and Staff, the Commission allowed many issues in the remand that were never raised at all in the original UE 88 proceeding and never raised on appeal of the orders produced by that proceeding. See OPUC No. 04-597.

Thus, either Phase 1 improperly considered extraneous issues, or the Commission committed legal error in restricting the issues in Phase 3 in the manner described above.

C. THE COMMISSION HAS ERRED IN RESTRICTING EVIDENCE ON REMAND TO "FACTS AS THEY EXISTED ON OR BEFORE OCTOBER 1, 2000."

The Phase 3 Scoping Order restricted the facts in this remand proceeding to the "facts as they existed on or before October 1, 2000." Phase 3 Scoping Order, p. 5.

In Phase 1 of these remand dockets, URP moved to exclude all evidence consisting of "future facts" offered by PGE witnesses. "Future facts" were defined as those not in existence as of the date that the evidentiary record closed in the original UE 88 proceeding. That motion was denied. Thus, the Commission had adopted contradictory approaches to the scope of evidence allowed in a remand proceeding.

D. THE COMMISSION HAS ERRED IN REFUSING TO HEAR EVIDENCE ON THE TROJAN INVESTMENT BALANCE, OTHER THAN THE "ACTUAL" BALANCE.

The Phase 3 Scoping Order precluded the presentation of any evidence on how the Commission should have calculated the PGE's remaining undepreciated investment in Trojan as of October 1, 2000. It prohibited the offering of any "*hypothetical* balance premised on rate adjustments in Phase I." Instead, it allowed only "evidence regarding the actual Trojan balance as of October 1, 2000." Since the actual Trojan balance as of October 1, 2000, is a function of the books kept by PGE, we are precluded from presenting any contrary evidence on this subject.

E. THE COMMISSION HAS ERRED IN REFUSING TO HEAR A WIDE RANGE OF EVIDENCE.

The Phase 3 Scoping Order (p. 7_, stated:

> Therefore, I deny URP's requests to present new evidence to quantify the continuing rate effects of any error in Order No. 02-227, update the cost to ratepayers from trading the non-interest-earning Trojan balance with interest-earning ratepayer credits and to bring these sums to present value, update the amounts of NEIL proceeds to determine the amount diverted from ratepayers and to bring these amounts to present value, and update the amount of the rate increase caused by Order No. 02-227.

This ruling essentially precluded URP/CAPs from making any case in Phase 3 of this remand docket.

F. THE COMMISSION HAS ERRED BY FAILING TO REINSTATE THE SCHEDULE PREVIOUSLY ADOPTED BY THE COMMISSIONS, FOR REASONS STATED BY MOTION BY CAPS.

On January 14, 2008, the CAPs moved to reinstate the schedule established by OPUC Order No. 07-157. The ALJ denied the motion. Doing so was error, for the reasons stated in the motion, which we hereby incorporate by reference.

G. THE COMMISSION HAS ERRED IN REFUSING TO HEAR EVIDENCE PERTAINING TO PGE'S ACTUAL RESULTS OF OPERATIONS.

The Phase 3 Scoping Order (p. 6) excludes consideration of "actual results from subsequent years."

> The Commission would violate the rule against retroactive ratemaking if it adjusted past authorized rates to reflect actual revenues and costs.

Id. But Staff and PGE have recently proposed exactly that in Docket No. UM 1224. The issue there is whether it was lawful for PGE to charge ratepayers for income taxes it was not actually paying during the last quarter of 2005, after SB 408 had taken effect. The main defense of PGE, seconded by Staff, is that PGE should not be required to refund the amount charged to ratepayers for the nonexistent income taxes, because PGE during the period October 1, 2005, through September 30, 2006, actually earned less than its authorized return on equity.

Thus, Staff and PGE see no problem in introducing and relying upon the utility's actual results of operation in UM 1224. Yet the same type of evidence is expressly forbidden in this docket.

H. THE COMMISSION HAS ERRED IN ASSUMING THAT THE COMMISSION CAN ORDER REFUNDS, WHEN RATE ORDERS HAVE BEEN REMANDED TO THE COMMISSION.

The Phase 3 Scoping Order (p. 8) erred in assuming that Commission can order refunds. The parties to the consolidated remand docket have extensively briefed this issue, and the Commission has issued no order resolving it.

We have shown that the Commission is not capable of providing an adequate remedy to former PGE ratepayers who have paid unlawful or otherwise invalid rates. We hereby incorporate the argument in Class Action Plaintiffs' Motion to Reinstate Schedule of OPUC Order No. 07-157 (January 14, 2008), pp. 5-8. Merely giving "unclaimed amounts" owed to former ratepayers to "current customers," as suggested by the Phase 3 Scoping Order, provides no remedy for the former ratepayers.

In their *Opening Comments ...on The Proffered Question Regarding Remedies*, filed June 20, 2007, the CAPs expressed concerns about the authority and power of the Commission to afford any relief at all to those who have become "former" customers in the 15 years since the illegal Trojan charges were included in rates. In the *Opening Comments* (pp. 62-66) the CAPs set out the costs of newspaper notice and administering any refunds to former customers. No party, including staff, commented in reply upon this discussion or submitted counter-affidavits as to the large costs involved. Newspaper and mail notice to former customers are the minimum standard of fundamental due process notice set out in ***Mullane v. Central Hanover Bank & Trust Co.***, 339 US 306, 314, 70 SCt 652, 657, 94 LEd 865 (1950), a "quasi-class" action of trust beneficiaries. There the court directed the government trustee

"shall direct to the members of the class the best notice practicable under the circumstances, *including individual notice to all members who can be identified through reasonable effort*." (Emphasis supplied). Accordingly, "[a]n elementary and fundamental requirement of due process in any proceeding which is to be accorded finality is notice reasonably calculated, under all the circumstances, to apprise interested parties of the pendency of the action and afford them an opportunity to present their objections. *Id.* (internal citations omitted).

CAPs questioned whether:

> The Commission does not have express authority required by ***McPherson v. Pacific Power & Light Co***., 207 Or 433, 449, 296 P2d 932 (1956), 207 Or at 449; **CUB/URP**, 154 OrApp 708, 713 (1998), to order and enforce such costs and mandates. True, the Commission has general powers "to do all things necessary and convenient" to protect the public from "unjust and unreasonable exactions and practices," ORS 756.040(1) and (2), but we question whether the OPUC has the plenary powers of a court to order a utility to pay for locator services, take out multiple newspaper notices in California, Western Washington, and Nevada (areas with the highest out-migration rates from Oregon), and the other judicial powers necessary to administer individual refunds.
>
> Consider that the Oregon Court of Appeals invalidated, as beyond its authority, the OPUC's "tagline rule," which required no expenditure of funds by the utilities but only required that they disclose in all advertisements whether the advertisement was paid for by customers or stockholders. Such authority could not be inferred from 756.040(1) and (2). ***Pacific Northwest Bell v. Davis***, 43 Or App 999, 608 P2d 547 (1979), *review denied* 289 Or 107 (1980). The necessity for strict construction of OPUC's powers under those sections was required because:
>
>> [T]the people, by adopting the state constitution, conferred upon the Legislative Assembly the power to legislate. Therefore this power is not by implication to be delegated to nonelective officers. The tendency of administrators to expand the scope of their operations is perhaps as natural as nature's well-known abhorrence of a vacuum. But no matter how highly motivated it may be, the

> tendency to make law without a clear direction to do so must be curbed by the overriding constitutional requirement that substantial changes in the law be made solely by the Legislative Assembly, or by the people. Oregon Constitution, Art IV, s 1 * * *.

43 Or App at 1006 (quoting ***Oregon Newspaper Publishers Ass'n v. Peterson***, 244 Or 114, 123-124, 415 P2d 21, 24-5 (1966)).

> Although the Commission claims it will not engage in "piecemeal" adjudication, it has refused to discuss due process notice for former ratepayers, has received no comments suggesting any remedies available for former ratepayers, and now claims it has the authority (never before demonstrated, cited or used) to afford relief to former ratepayers because through negotiated settlement, it has used highly inadequate newspaper notices in the past.

The only authority the ALJ offered was the plan in UT-121, a negotiated settlement and not an exercise of the Commission's authority, to order the considerable costs of best practicable notice upon the company. There is no evidence in the record what might even constitute "best practicable" notice to the hundreds of thousands of former customers.

I. THE "NET BENEFIT ANALYSIS" IS IRRELEVANT TO DETERMINING WHETHER RATES ARE LAWFUL, FAIR, JUST, OR REASONABLE.

Rates are not lawful, fair, just, or reasonable, merely because they (allegedly) produce a "net benefit" for ratepayers, compared with an unlawful order that has been reversed and remanded by the courts. The reversed order does not constitute any sort of valid benchmark from which to compare or measure. Thus, the "net benefit analysis" in OPUC Order No. 02-227 is completely irrelevant, as it compared the OPUC Order No. 02-227 outcome with what ratepayers would have paid, if the unlawful OPUC Order No. 95-322 had continued in effect for the Trojan investment. The OPUC Order No. 02-227

result could have been $100 million better for ratepayers than continuation of OPUC Order No. 95-322; it does not matter one bit. Rates do not become lawful, fair, just, or reasonable merely by being better (allegedly) than rates declared invalid by the courts.

As for the so-called the "asset based test," among its defects are these:

1. It assumes that th face value of interest-bearing assets are worth the same as the face value of non-interest bearing assets.

2. It failed to account for last quarter of 2000.

3. It appears to have failed to account for NEIL.

4. There is no reason to think it is an appropriate test for whether rates are lawful, just or reasonable. Merely because assets of equal face value are traded does not establish anything.

Further, it appears that the "asset based test" in fact constructed "assets" out of revenue or cost streams. Thus, it did not, as alleged, merely offset the face value of assets as of September 30, 2000. As we argued to the Court of Appeals:

> The OPUC Reply Brief (p. 21) says "All of the balances, whether credited to PGE or to ratepayers, were reduced to their present value for purposes of the settlement." This contradicts the PGE contention that the OPUC Order No. 02-227 merely offset the "face value of that [Trojan] investment." Reply by PGE to Answering Brief [hereinafter PGE Reply Brief], p. 47.
>
> On this issue, the OPUC is right and PGE is wrong. OPUC Order No. 02-227 does not merely offset the "face value" of the remaining Trojan investment with the "face value" of the accounts that PGE admittedly owed ratepayers. Instead, as the OPUC states, the offsetting amounts were determined by calculating the present value of various future revenue streams that would have resulted from the rates in effect prior to OPUC Order No. 00-601, including the unlawful rates established by OPUC Order No. 95-322. The present value figure for the Trojan investment balance is based on the unlawful assumption that the balance is entitled to and would earn a return on investment at PGE's authorized rate of return on investment.
>
> The OPUC understands this. OPUC Gray Brief (p. 22) states:

> The order on review simply takes the amortized amount that ratepayers were previously ordered to pay (which this court affirmed) and prepays it at its present value. AR 247. URP arrives at contrary figures by removing the amortization - the interest - that PGE was legally entitled to receive. AR 247. In other words, URP argues that future interest is valuable to ratepayers, but would not allow PGE interest on money it "loaned" to ratepayers.

But what does OPUC mean here by "the amortized amount that ratepayers were previously ordered to pay (which this court affirmed)"? It means the principal of the Trojan investment balance. Yet, what "ratepayers were previously ordered to pay" regarding this principal, in OPUC Order No. 95-322, was to pay it over a 17-year period in amount of about $20 million per year. In ***CUB/URP v. OPUC***, the Court concluded that adding interest or return on investment to that repayment of principal was unlawful. The Court did not affirm anything other than that particular treatment of the principal. Yet, the OPUC's present value analysis in OPUC Order No. 02-227 wholly depends upon continuing to assume that ratepayers must repay the principal with return on investment.

Back to the OPUC quotation: Yes, we remove the "the interest - that PGE was legally entitled to receive", because ***CUB/URP v. OPUC*** ruled that PGE was not entitled to receive interest on its Trojan investment. The OPUC arrived at its decision in OPUC Order No. 02-227 only by disregarding the final outcome in ***CUB/URP v. OPUC*** (perhaps because OPUC Order No. 02-227 was issued at a time prior to the final confirmation of that outcome by the Oregon Supreme Court in November 2002).

OPUC Order No. 02-227 did not merely offset the balances but increased the Trojan "balance" in favor of PGE by assuming that PGE would be collecting that balance, with return on investment, for the remaining years through 2011. Conversely, OPUC Order No. 02-227 seems to have reduced the "balances" PGE owed to ratepayers due to other transactions by applying a discount rate. This was explained in the Testimony of Jim Lazar in the agency proceeding.

> Under the "stipulation," in exchange for removing the remaining $180.5 million balance of Trojan ratebase from its books, the "stipulation" plan also removes from the books $161.9 million in accounts that are owned by PGE to ratepayers in accounts that accrue interest for ratepayers at the company's authorized rate of return on investment.

> The amount in the affected accounts owed to ratepayers is presently not clear. PGE has provided several documents summing those amounts, as of September 30, 2000, at $161,896,122. The latest spreadsheet provided by PGE after the Workshop shows that the "stipulation" would cancel amounts otherwise due to ratepayers equal to $186.5 million nominal or $145.2 million PV. This is indicated in the spreadsheet file entitled workshoplazar.xls (sheet Final NPV, cells E27-E28) attached to the electronic distribution of this testimony. If the $161.9 million is indeed in accounts to which the Company's authorized rate of return is applied, it is not clear why the PV of those accounts is not also $161.9 million.

Testimony of Jim Lazar (May 15, 2001), p. 6.

Reply Brief of Plaintiffs-Respondents-Cross-Appellants (September 5, 2006) in ***URP v. OPUC*** (UM 989 appeal), pp. 13-15.

Dated: July 21, 2008

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CERTIFICATE OF SERVICE

I hereby certify that I filed the original and 8 copies of the foregoing by email to the Filing Center and by mail, postmarked this date, and that I served a true copy of the foregoing OPENING BRIEF OF UTILITY REFORM PROJECT, ET AL. AND CLASS ACTION PLAINTIFFS by email to the physical and email addresses shown below, which comprise the service list on the Commission's web site as of this day (email service only to those who have waived physical service).

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