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**BEFORE THE PUBLIC UTILITY COMMISSION**

**OF OREGON**

UE 134  
UM 1047

In the Matter of )  
)  
PACIFICORP )  
)  
Application for Approval of Revised Tariffs )  
to Reflect New Net Power Costs. **(UE 134)** )  
\_\_\_\_\_ )

ORDER

In the Matter of )  
)  
PACIFICORP )  
)  
Application for an Accounting Order )  
Regarding Deferral of Trail Mountain Mine )  
Unrecovered Costs. **(UM 1047)** )

**DISPOSITION: ISSUES LIST ESTABLISHED**

The Public Utility Commission of Oregon (Commission) previously granted limited reconsideration of our order in this docket.<sup>1</sup> In our reconsideration order, we informed the parties that the Administrative Law Judge (ALJ) would determine the scope of future proceedings.

On August 19, 2002, ALJ Kathryn Logan asked the parties to submit issues lists by August 22, 2002. Commission Regulatory Staff (Staff), the Industrial Customers of Northwest Utilities (ICNU) and PacifiCorp each submitted a list.<sup>2</sup> On August 29, 2002, ALJ Logan issued a memorandum that set forth the two issues to be decided in the dockets as follows:

<sup>1</sup> Order No. 02-343 was the initial order in which we adopted the parties' stipulation regarding all issues in Dockets UE 134/UM 1047. The reconsideration order, issued August 8, 2002, was Order No. 02-543.

<sup>2</sup> The Citizens' Utility Board (CUB) did not submit an issues list, as it is no longer participating in this docket.

1. Is the cost of the West Valley Lease a necessary and ordinary recurring expense?
2. Does permitting recovery of the full costs of the lease violate OAR 860-038-0080(1)(b)?<sup>3</sup>

The parties were given until September 9, 2002 to submit any objections to the issues as determined by the ALJ, and to submit a proposed schedule for the docket.

On September 9, 2002, ICNU submitted objections to the issues list. Also on September 9, 2002, PacifiCorp submitted a response to the issues list, along with a motion and proposed procedural schedule. On September 24, 2002, ICNU filed a response to PacifiCorp's motion and proposed schedule.

ICNU claims that the issues list developed by the ALJ ignores the Commission's order and record in Docket UI 196.<sup>4</sup> In light of that assertion, the ALJ determined that the Commission should establish the issues list in this docket. Upon her own motion, the ALJ certified the following question to the Commission pursuant to OAR 860-012-0035(1)(i):

What are the issues that the Commission must decide in this reconsideration proceeding?

## **Background**

On March 29, 2002, ICNU, Staff, PacifiCorp and CUB submitted a stipulation that resolved numerous outstanding issues in Dockets UE 134/UM 1047, including the establishment of annual net power costs, the treatment of the Trail Mountain Mine closure costs and the Hermiston properties sale, the amortization of above market summer forward purchases, and the ratemaking treatment of the West Valley Lease.

Subsequent to the issuance of Order No. 02-343 (UE 134/UM 1047), ICNU challenged the stipulation's treatment of the West Valley Lease costs. ICNU claimed that the parties did not have a meeting of the minds when they reached agreement on the ratemaking treatment of the lease. Further, ICNU asserted that it informed all parties of ICNU's plan to oppose the affiliated interest application involving the lease. According to ICNU, it was told to raise lease challenges in the affiliated interest docket (UI 196) rather than in the UE 134/UM 1047 dockets.

The Commission granted reconsideration, but limited the reconsideration to Paragraph 9 of the stipulation involving the West Valley Lease.

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<sup>3</sup> This rule requires that electric companies must include new generating resources in revenue requirement at market prices, not at cost. This rule is currently being reviewed in a rulemaking docket (AR 417).

<sup>4</sup> Order No. 02-361, amended by Order No. 02-657.

**Positions of the parties**

ICNU

ICNU submitted the following issues to be determined in the reconsideration proceeding:

1. Are the costs of the West Valley Lease prudent and appropriate for recovery by PacifiCorp?
2. Has PacifiCorp established that the West Valley Lease benefits Oregon customers?
3. Will the generation facilities acquired by PacifiCorp through the West Valley Lease be used to provide service to any Oregon customers?
4. Have Oregon customers been harmed by the inclusion of the costs of the West Valley Lease in rates?
5. Does the West Valley Lease meet the requirements of the Commission's affiliated interest transfer pricing policy for the purpose of including the costs of the lease in rates?
6. Is the West Valley Lease the least cost alternative available to serve PacifiCorp's summer peaking load in Utah?
7. Did PacifiCorp adequately demonstrate that the costs of the West Valley Lease reflected the market cost for a generation facilities lease for the purpose of including those costs in rates?
8. Did PacifiCorp adequately demonstrate that the Request for Proposals process was a legitimate "competitive procurement" process for the purposes of applying the presumption in OAR 860-027-0040(2)(k) that the cost of the lease equals the market price?
9. Did PacifiCorp adequately demonstrate that the costs of the West Valley Lease reflected the market costs for a generation facilities lease for the purpose of the requirements of OAR 860-038-0080(1)(b)?

ICNU also reserved the right to raise additional issues as the proceeding progressed.

In its objections, ICNU contends that the issues identified by the ALJ are too limited, and do not allow for meaningful examination of the West Valley Lease. ICNU asserts that the ALJ improperly defined the standard for a prudence review, erred in holding that reasonableness issues regarding the lease were resolved in Docket UI 196, and failed to allow the parties to engage in discovery and submit additional evidence. ICNU asks that the issues list be revised to include the nine issues initially proposed, and for a schedule to be set that allows for discovery, testimony and briefing.

PacifiCorp

PacifiCorp filed the following issues list:

- 1(a). Is it appropriate in this reconsideration proceeding dealing with the ratemaking treatment of the costs associated with a specific, new Company resource (the Lease) to change the Commission's current interjurisdictional cost allocation policies?
- 1(b). If the answer to Issue 1(a) is yes, what standard (i.e. no harm, net benefit, least cost alternative, etc.) will apply to determine whether, and at what level, to permit the recovery of the costs of a specific, new Company resource in Oregon rates?
- 1(c). If the answer to Issue 1(a) is yes, has the Company satisfied the ratemaking standard specified in Issue 1(b)?
2. Does permitting recovery of the full costs of the Lease violate OAR 860-038-0080(1)(b)?

PacifiCorp responded to the ALJ's issues list, stating that the list properly defined the scope of the proceeding. In particular, PacifiCorp agreed that the Commission had previously resolved the reasonableness of PacifiCorp's action in contracting with PacifiCorp Power Marketing, Inc. in Docket UI 196, that the necessary and ordinary recurring expense standard is the appropriate standard, and that interjurisdictional issues are best left to Docket UM 1050. Finally, PacifiCorp agreed that it is not appropriate to address affiliated interest issues in the instant proceeding.

Staff

Staff filed its issues list after reviewing the lists prepared by ICNU and PacifiCorp. Staff suggested a combination of the issues proposed by the parties, as follows:

1. Are the costs of the West Valley Lease prudent?
2. Is it appropriate in this reconsideration proceeding dealing with the ratemaking treatment of the costs associated with a specific, new Company resource (the Lease), to change the Commission's current interjurisdictional cost allocation policies?
3. If the answer to Issue No. 2 is yes, what standard (i.e., no harm, net benefit, least cost alternative, etc.) will apply to determine whether and at what level, to permit the recovery of the costs of a specific, new Company resource in Oregon rates?
4. If the answer to Issue No. 2 is yes, has the company satisfied the ratemaking standard specified in Issue No. 3?
5. Is the West Valley Lease the least cost alternative available to serve PacifiCorp's summer peaking load in Utah?

6. Does permitting recovery of the full costs of the Lease violate ORS 860-038-0080(1)(b)?

Staff specifically did not include any issues related to affiliated interest transaction criteria, as those issues were not previously raised in this docket.

Staff did not file any response or objection to the ALJ issue list.

## **DISCUSSION**

The parties differ on the proper issues to be raised in a ratemaking proceeding and in an affiliated interest proceeding. Therefore, we will generally discuss the statutory schemes involved with these two types of proceedings. We will then explain the type of review needed in this reconsideration portion of the docket, and finish with an explanation of the issues to be resolved in this docket.

### Ratemaking proceedings

Under ORS 757.210, a utility bears the burden of showing that a proposed rate increase is just and reasonable. Any party may challenge the utility, claiming that the proposed rate increase is not just and reasonable. One basis for such a challenge is that the costs incurred by the utility, upon which the proposed rate increase is based, were not prudent. As we stated in *In re PacifiCorp*, UE 121, Order No. 02-469 at 4:

In a prudence review, the Commission examines the objective reasonableness of a company's actions measured at the time the company acted.

In determining whether a company's action was prudent, we look at the reasonableness of the action based on the information that was available, or could reasonably have been available, at the time the action was taken. If the action was reasonable, then the expense was prudently incurred. Likewise, if the action taken by the utility was not reasonable, then the expense was not prudently incurred. If the expense is not prudent, then the Commission will not include the expense in the calculation of the utility's rates.

### Affiliated interest proceedings

Under ORS 757.495, a utility must file with the Commission certain contracts entered into by the utility and an affiliated interest of the utility. ORS 757.495(3) requires the following:

When any such contract has been submitted to the commission, the commission promptly shall examine and investigate it. If, after such investigation, the commission determines *that it is fair and reasonable and not contrary to the public interest*, the commission shall enter findings and order to this effect . . . whereupon any expenses and capital expenditures incurred by the public utility under the contract may be recognized in any rate valuation or other hearing or proceeding. If, after such investigation, the commission determines that the contract is not fair and reasonable in all its terms and is contrary to the public interest, the commission shall enter findings and order accordingly and . . . it shall be unlawful to recognize the contract for the purposes specified in this section. (Emphasis added).

If the contract is found to be fair and reasonable, and not contrary to the public interest, the expenses incurred under the contract may be recognized in a rate valuation or other hearing. If the contract is not fair and reasonable, or is contrary to the public interest, then the expenses cannot be recognized in rates.<sup>5</sup>

#### Reconsideration review

ICNU claims that it was not prudent for PacifiCorp to enter into the West Valley Lease, and that any expenses incurred in the West Valley Lease arrangement should not be included in rates. ICNU wants the opportunity to present evidence that PacifiCorp's action of entering into the lease with PacifiCorp Power Marketing was not reasonable.

However, in Order No. 02-361 (UI 196), we concluded that the affiliated transaction between the affiliates was fair, reasonable and not contrary to the public interest. As we said in *In re PacifiCorp*, UI 15, Order No. 84-942 at 3:

ORS 757.495 . . . was designed to protect ratepayers from abuses which may arise from less than arm's length transactions. *CP National Corporation*, UF 3842, Order No. 82-593 at 2; *Portland General Electric Company*, UF 3739, Order No. 81-737 at 6.

\* \* \*

For rate-making purposes, the Commissioner reserves judgment on the *reasonableness of payments under the contract*. In subsequent rate proceedings, Pacific will be required to show that the payments are reasonable. *See* ORS 757.210. (Emphasis added)<sup>6</sup>

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<sup>5</sup> OAR 860-027-0040 sets forth the requirements of an affiliated interest filing. A utility must describe the services to be provided, the cost and market value of the services, the reasons relied upon by the utility for procuring the services, the benefits (if any) the utility customers and general public derive from the provision of the services, and a detailed description of the procurement process.

<sup>6</sup> *See, also*, Order No. 84-822 at 5; Order No. 84-267 at 3.

In Order No. 02-361 (UI 196), we also reserved the right to review for reasonableness all financial aspects of the transaction. The decision on the financial aspects of the transaction occurred in Order No. 02-343 (UE 134/UM 1047), the docket subject to the petition for reconsideration.

ICNU is correct that the Commission does not establish the ratemaking treatment of the contract in the affiliated interest docket. However, the subsequent ratemaking review is whether the payments set forth in the contract are reasonable. We have already determined that it was reasonable for PacifiCorp to enter into the contract in Docket UI 196.

This leaves the issue of the standard to be applied when reviewing the cost of the lease. The question is whether the costs of the lease are reasonable, i.e., is the cost of the lease a necessary and ordinary recurring expense.<sup>7</sup> If it is, the costs are included in rates. If not, the costs are not included in rates.

In reviewing ICNU's issues list, the first issue identified by ICNU is the same issue, in different words, that the ALJ set forth in her memorandum. Issue Nos. 2-8, excluding Issue No. 6, are either part of Docket UM 1050 or part of Docket UI 196. We will not address allocation issues in this docket. As for Issue No. 6, we find that it is included in the first issue set forth in the ALJ's memorandum. Issue No. 9, which relates to OAR 860-038-0080(1)(b), is appropriately summarized below. Therefore, we hold that the issues for us to consider in this reconsideration proceeding are as follows:

1. Is the cost of the West Valley Lease a necessary and ordinary recurring expense?
2. Does permitting recovery of the full costs of the lease violate OAR 860-038-0080(1)(b)?

Finally, we wish to address the question of testimony and evidence in this proceeding. Certainly a record needs to be developed upon which we can base our decisions. If the parties need further discovery to make that record, then that is appropriate. It appears to us, however, that the second issue could be briefed without further discovery, as it is a legal issue. We leave it to the ALJ to determine the schedule, discovery and evidence needed in this case.

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<sup>7</sup> See, A.J.G. Priest, 1 *Principles of Public Utility Regulation*, 48 (1969).

**ORDER**

IT IS ORDERED that:

1. The issues for reconsideration are as follows:
  - a. Is the cost of the West Valley Lease a necessary and ordinary recurring expense?
  - b. Does permitting recovery of the full costs of the lease violate OAR 860-038-0080(1)(b)?
2. The ALJ will determine the schedule, discovery and evidence needed in this case.

Made, entered, and effective \_\_\_\_\_.

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**Roy Hemmingway**  
Chairman

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**Lee Beyer**  
Commissioner

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**Joan H. Smith**  
Commissioner

A party may request rehearing or reconsideration of this order pursuant to ORS 756.561. A request for rehearing or reconsideration must be filed with the Commission within 60 days of the date of service of this order. The request must comply with the requirements in OAR 860-014-0095. A copy of any such request must also be served on each party to the proceeding as provided by OAR 860-013-0070(2). A party may appeal this order to a court pursuant to applicable law.