

**BEFORE THE PUBLIC UTILITY COMMISSION
OF OREGON**

UE 177(4)

In the Matter of

PACIFICORP, dba PACIFIC POWER

Annual Tax Filing under ORS 757.268

ORDER

DISPOSITION: STIPULATION ADOPTED AS MODIFIED

I. INTRODUCTION

In this order, the Public Utility Commission of Oregon (Commission) approves a stipulation that resolves all issues relating to PacifiCorp, dba Pacific Power's (Pacific Power) tax report for calendar year 2009, filed in compliance with Senate Bill (SB) 408. The stipulation authorizes Pacific Power to implement a surcharge of \$13.47 million for state and federal taxes, plus interest, and requires Pacific Power to refund approximately \$87,000 in local taxes. The stipulation also contemplates that Pacific Power will file for deferral of certain amounts pending resolution of a tax normalization issue.

SB 408, primarily codified at ORS 757.268, requires utilities to true up any differences between income taxes authorized to be collected in rates from customers and income taxes actually paid to units of government that are "properly attributed" to utilities' regulated operations.¹ Utilities must make annual tax filings reporting these amounts on October 15 of each year. If amounts collected and amounts paid differ by \$100,000 or more, the Commission must order the utility to establish an automatic adjustment clause to account for the difference, with a rate adjustment effective June 1 of each year.²

II. PROCEDURAL HISTORY

On October 15, 2010, Pacific Power filed its annual tax report for calendar year 2009. In the 2009 tax report, Pacific Power stated that the amount of state, federal, and local taxes paid and properly attributed to its regulated Oregon operations was approximately \$29.3 million more than the amount of taxes collected in rates. Pacific Power sought to collect this difference, plus interest, as a surcharge to customers through an automatic adjustment clause under ORS 757.268(6).

¹ ORS 757.268(4).

² See ORS 757.268(4), (6)(a); OAR 860-022-0041(8).

On November 2, 2010, the Industrial Customers of Northwest Utilities (ICNU) filed a motion to modify the protective order governing the treatment of confidential information in this docket. Pacific Power opposed the motion. On January 20, 2011, the Commission issued an order denying ICNU's motion.³

Through established procedures, Commission Staff reviewed Pacific Power's 2009 tax report for compliance with ORS 757.268 and OAR 860-022-0041. Following workshops and settlement conferences, to which all parties were invited, Staff filed an issues list, on December 23, 2010, identifying a number of issues with Pacific Power's filing.⁴

On January 6 and 7, 2011, Staff, Pacific Power, the Citizens' Utility Board of Oregon (CUB), and ICNU attended additional settlement conferences. On January 14, 2011, Staff, CUB, and Pacific Power (collectively referred to as the Stipulating Parties) filed a stipulation purporting to resolve all issues in this docket. On January 21, 2011, the Stipulating Parties supplemented their stipulation with supporting testimony. A copy of the stipulation is attached as Appendix A to this order. On February 7, 2011, ICNU filed timely objections to the stipulation, along with supporting testimony. The Stipulating Parties filed reply testimony on February 18, 2011. On March 11, 2011, Pacific Power filed an amended 2009 tax report reflecting a revised calculation consistent with the stipulation.

A hearing was held on February 25, 2011. Pacific Power, Staff, CUB, and ICNU filed simultaneous post-hearing opening and closing briefs on March 11 and March 21, 2011, respectively.

III. DISCUSSION

A. The Stipulation

The stipulation has two parts. Pacific Power, Staff, and CUB all agree to Part 1 of the stipulation, which reduces Pacific Power's originally requested surcharge of \$29.3 million to \$13.47 million. A large part of this reduction is due to a proposed amendment to OAR 860-022-0041. The key agreement in Part 2 of the stipulation would allow Pacific Power to seek deferral of part of the reduced surcharge until it obtains a private letter ruling (PLR) from the Internal Revenue Service (IRS) confirming that the proposed rule amendment is consistent with IRS normalization rules.⁵ Pacific Power and Staff agree to Part 2 of the stipulation. CUB objects to Part 2 on the grounds that the rule amendment is appropriate and a PLR therefore is unnecessary. ICNU objects to both parts of the stipulation.

³ See Order No. 11-026.

⁴ See Staff's Initial Findings for PacifiCorp (Staff's Issues List), attached to the stipulation as Exhibit A.

⁵ Part 2 is also contingent on the Commission adopting a permanent rule amendment to OAR 860-022-0041.

1. Part 1 of the Stipulation

a. Calculation of "Taxes Paid"

The Stipulating Parties explain how they reached agreement on the stipulated surcharge. After Pacific Power filed its 2009 tax report, Staff and other parties conducted a review of Pacific Power's filing. Staff initially identified three issues with Pacific Power's calculation of "taxes paid." Those issues, described in Staff's issues list,⁶ would have reduced Pacific Power's \$29.3 million surcharge to \$27.3 million.

In addition to these three issues, Staff believed it had discovered a potential issue with the Commission rule governing the calculation of SB 408 tax reports, OAR 860-022-0041. Under this rule, the Commission determines the amount of "taxes paid" for purposes of SB 408 by using three separate methods: a stand-alone method, a consolidated method, and an apportionment method.⁷ Generally speaking, the lowest of these three calculations is considered the amount of "taxes paid" that is properly attributed to a regulated utility for purposes of SB 408.

An exception has been carved out of this general methodology, however, to ensure that SB 408 calculations comply with IRS normalization rules. The Commission made housekeeping changes to OAR 860-022-0041 to address this issue in 2007.⁸ Addressing concerns that calculations under the rule might in some instances result in IRS normalization violations, the Commission modified subsection OAR 860-022-0041(4)(d) to preclude the calculation of "taxes paid" under the rule from falling below the level of the utility's deferred taxes related to the depreciation of its public utility property.

For purposes of the SB 408 calculation, the "(4)(d) tax limitation" means that the Commission can rely on the lowest of the three calculations of "taxes paid" for purposes of calculating the SB 408 refund or surcharge *unless* that method produces a result lower than the amount of certain deferred taxes related to public utility property.⁹ If it does, the OAR 860-22-0041(4)(d) deferred tax floor kicks in and ensures that the amount of "taxes paid" does not fall below the amount required under IRS rules.

Pacific Power's calculation of taxes paid in its initial 2009 tax report relied on the (4)(d) tax limitation. During its review of the report, Staff questioned whether the (4)(d) tax limitation was actually necessary to avoid normalization violations when the stand-alone method is used to calculate "taxes paid," and ultimately concluded that no

⁶ See Stipulation at 14.

⁷ See Order No. 09-177 at 8; Order No. 07-401 at 4.

⁸ The housekeeping amendments were adopted in Docket AR 517.

⁹ Staff explains that the floor is "deferred taxes related to public utility property for regulated operations of the utility, reduced by any tax refunds recognized in the reporting period, and allocated to the regulated operations of the utility." Staff's Issues List at 5. As a practical matter, this modified subsection (known as the "(4)(d) tax limitation") prevents ratepayers from sharing inappropriately in benefits received from accelerated depreciation, as the purpose of federal laws authorizing accelerated depreciation is to encourage capital investment.

risk of normalization violations exists when this method is used. All active parties, including ICNU, concurred on this point.

Based on its conclusion that the (4)(d) tax limitation in the rule was overbroad, Staff commenced a temporary rulemaking to conform the rule to Staff's view of its proper scope. The Commission issued an order approving the temporary rule on February 22, 2011.¹⁰ Relying on the temporary rule, the Stipulating Parties recalculated Pacific Power's taxes paid using the stand-alone method without the (4)(d) tax limitation. This calculation yielded a significantly lower surcharge to customers of \$13.47 million.

b. Implementation of Part I of the Stipulation

The stipulation would result in a surcharge of \$13,474,662 for federal and state taxes, as well as a refund of \$86,932 for local taxes. The Stipulating Parties propose using a blended treasury rate of 2.01 percent to calculate interest on both the surcharge and the refund. Pacific Power estimates the total amount amortized for the surcharge, including interest, will be approximately \$15,769,759. It estimates that the total refund for local taxes, including interest, will be approximately \$101,739.

The surcharge would be recovered over a 12-month period (June 1, 2011 through May 31, 2012) through Pacific Power's Schedule 102—the refund would be returned to customers over the same time period. The refund would be allocated by customer rate schedule on an equal cents per kilowatt-hour basis under the company's Schedule 103.¹¹

When combined with the currently effective Schedule 102 surcharge amounts, the surcharge resulting from the stipulation would result in an overall increase to Pacific Power's net revenues of 1.2 percent.

2. Part 2 of the Stipulation

In Part 2 of the stipulation, Staff and Pacific Power agree that Staff will support before the Commission an application by Pacific Power to defer the difference between the surcharge produced by the deferred tax floor (\$27.3 million) and the surcharge agreed to in Part 1 of the stipulation (\$13.47 million), which is a total of \$13.83 million. This agreement is contingent on the occurrence of two events: (1) the Commission's adoption of a *permanent* amendment to OAR 860-022-0041(4)(d) making the deferred tax floor inapplicable to the determination of taxes paid under the stand-alone method; and (2) the IRS's issuance of a PLR concluding that OAR 860-022-0041(d) as so revised is consistent with IRS normalization requirements.

Pacific Power agreed to file an application for deferral by February 15, 2011,¹² and request in the application that interest accrue during the deferral at the

¹⁰ See Docket No. AR 547, Order No. 11-064.

¹¹ See OAR 860-022-0041(8)(d).

¹² Pacific Power filed this application on February 15, 2011. It is docketed as Docket UM 1523.

blended treasury rate.¹³ Staff and Pacific Power also agree that if the deferral is granted, the deferred amount will not accrue interest beyond one year “commencing with the date the Commission adopts a permanent amendment to OAR 860-022-0041(4)(d).”¹⁴ Staff and Pacific Power agree to work cooperatively on the new PLR request, and to submit the request “expeditiously” upon issuance of a permanent rule amendment to OAR 860-022-0041(4)(d).

If the Commission does not adopt the proposed permanent amendment to OAR 860-022-0041(4)(d), or if the IRS concludes that OAR 860-022-0041(4)(d) as revised is not consistent with the normalization requirements of the IRS, Staff agrees to support Pacific Power’s request to amortize the deferral balance of \$13.83 million plus accrued interest.

B. ICNU’s Objections to the Part 1 of the Stipulation

1. Positions of the Parties

ICNU objects to both parts of the stipulation. With respect to Part 1, ICNU agrees with the Stipulating Parties that the Commission’s rule should be amended to remove the (4)(d) tax limitation as proposed. ICNU argues, however, that the rule should be further amended to allow for a modified calculation that would eliminate Pacific Power’s right to a surcharge in this tax year. ICNU asserts that PacifiCorp, Pacific Power’s corporate parent, paid no federal taxes in the tax year applicable to this docket, and contends that the Commission’s rule should therefore be amended to eliminate Pacific Power’s right to a surcharge. ICNU asserts the rule could be amended to achieve this goal consistent with IRS normalization rules.¹⁵

In response, the Stipulating Parties note that the purpose of this docket is to determine whether Pacific Power’s tax report complies with OAR 860-022-0041. Because ICNU concedes that the stipulation is consistent with OAR 860-022-0041, as amended in Order No. 11-064, the Stipulating Parties contend that ICNU’s arguments that the Commission should make further modifications to the rules are outside the scope of this docket.

Moreover, the Stipulating Parties argue, ICNU’s proposed calculation is inconsistent with other Commission rules, and is riddled with errors. For example, they argue that the alternative calculation proposed by ICNU’s witness, Ellen Blumenthal, uses improper allocators, resulting in a significantly inaccurate end result. They also argue that Ms. Blumenthal’s calculation violates various matching principles and improperly includes (and excludes) various items. Finally, they assert that Ms. Blumenthal’s calculation violates IRS normalization rules.

¹³ Pacific Power notes that its agreement to request the blended treasury rate is expressly for settlement purposes.

¹⁴ Stipulation at 7.

¹⁵ Written Objections of the Industrial Customers of Northwest Utilities to the Stipulation (ICNU Objections) at 2 (Feb 7, 2011).

ICNU rejects the Stipulating Parties' objections, and points out that the Commission's rules were modified to take into account the Stipulating Parties' agreement. According to ICNU, this demonstrates that the rule "can quickly be changed to better conform with the law."¹⁶ Therefore, ICNU argues, its proposed rule changes could and should be adopted.

ICNU also defends the methodology behind Ms. Blumenthal's calculation, dismissing the Stipulating Parties' assertion that the calculation uses improper allocators or violates matching principles or normalization rules. In any case, ICNU argues, Ms. Blumenthal's calculation was not meant to be a precise calculation, but a demonstration of an appropriate methodology for addressing SB 408 tax reports. To the extent that the Stipulating Parties criticize the specific details of Ms. Blumenthal's calculation, ICNU argues, it is because the protective order in this docket prevented Ms. Blumenthal from having access to the highly confidential documents that would have allowed her to produce a more precise calculation.¹⁷

2. *Commission Resolution*

The purpose of this SB 408 tax report docket is to determine whether Pacific Power's 2009 tax report complies with OAR 860-022-0041.¹⁸ Although ICNU suggested at various points in the proceedings that its calculation is somehow consistent with an expansive interpretation of the existing rule, its witness Ms. Blumenthal's proposed alternative methodology and ICNU's own complaints about the existing rule make clear that ICNU's proposal is inconsistent with the Commission's rule as written.¹⁹ While Staff instituted a rulemaking proceeding to implement its narrow rule change while this docket was pending, ICNU has not filed a petition to amend the rule.²⁰ We conclude that ICNU's objections to Part 1 of the stipulation are outside the scope of this docket.

Even if we were to open a rulemaking docket on our own motion to consider ICNU's proposals, which we decline to do, we find that ICNU has failed to specify how the rule should actually be changed. The Stipulating Parties proposed specific language to narrow the scope of the (4)(d) tax limitation. Neither Ms. Blumenthal nor ICNU (in its arguments or briefing) has given the Commission a clear idea of what ICNU's proposed rule amendments might actually look like. When asked during the hearing how she would amend the rule in accordance with her general recommendations, Ms. Blumenthal testified that her alternative methodology was

¹⁶ ICNU's Reply Brief at 8 (Mar 21, 2011).

¹⁷ ICNU's objections to the protective order were addressed in Order No. 11-026, and will not be revisited here.

¹⁸ See Order No. 11-002 at 1 ("The appropriate scope of UE 177(4) and UE 178(4) is to determine whether the tax reports filed by Pacific Power and PGE are in compliance with OAR 860-022-0041 (the rule adopted by the Commission to implement SB 408).").

¹⁹ ICNU's witness Blumenthal, concedes that Part 1 of the stipulation is based on the stand-alone calculation required by the Commission's rule, but she proposes her own alternative calculation of Pacific Power's stand-alone federal income tax expense. ICNU/100, Blumenthal/12; ICNU/104 (highly confidential) (Feb 7, 2011).

²⁰ Nor do ICNU's objections appear sufficient to operate as a request to amend a rule. See OAR 137-001-0070 (detailing requirements for petition to promulgate, amend, or repeal rule).

intended to open a new dialogue about the issue, now that she and the other parties better understood utility taxes.²¹ While we understand the general purpose of Ms. Blumenthal's alternative calculation, it provides us with insufficient guidance to grant the relief requested by ICNU here.²²

Finally, ICNU's assertion that its methodology is beneficial to ratepayers because it would eliminate Pacific Power's surcharge for the 2009 tax year—the underlying purpose of its objections—is not entirely convincing. The Stipulating Parties argue that ICNU's proposed methodology is inconsistent with SB 408, violates numerous matching principles, and contains other errors. We need not decide these issues here, but they illustrate the complexity of this issue and call into question the extent to which ratepayers would actually benefit from ICNU's proposed alternative methodology, if adopted.

In summary, we find ICNU's objections to Part 1 of the stipulation to be outside the scope of this docket. While we recognize that there are many ways to implement the calculations required by SB 408, this complexity is the very reason that the broader calculation methodology should be developed through the notice and comment procedures provided in a rulemaking proceeding. In any event, ICNU failed to provide the Commission with recommendations specific enough to allow us to grant the relief requested. We deny ICNU's objections to Part 1 of the stipulation.

C. Objections to Part II of the Stipulation

Both CUB and ICNU object to Part 2 of the stipulation.

1. Positions of the Parties

According to CUB, the proposed change to OAR 860-022-0041(4)(d) creates no possibility of a normalization violation, so the proposal that Pacific Power file for a deferral and seek a PLR on the issue is "simply unnecessary and a waste of taxpayer and ratepayer money." CUB asserts that ratepayer money will be required for Staff to track and process the deferral request and assist with a PLR, and for CUB (and possibly ICNU) to oppose the deferral request. Moreover, CUB adds that it will probably take at least a year to get a PLR, exposing Pacific Power to any normalization violation in the interim, whether Pacific Power seeks a PLR or not.

Like CUB, ICNU objects to Part 2 of the stipulation on the grounds that the Stipulating Parties' proposed change to the (4)(d) limitation is consistent with IRS normalization rules, making it unnecessary for Pacific Power to seek a PLR on this point. Because ICNU disagrees that Pacific Power is entitled to any surcharge, it also objects to Pacific Power's proposal to seek deferral of any surcharge amount.

²¹ Hearing Transcript at 68.

²² See ORS 183.390 (allowing any interested person to petition agency for amendment of a rule); OAR 137-001-0070 (requiring petition for rule amendment to "*set forth the proposed language in full*," among other things) (emphasis added).

2. *Commission Resolution*

We find Part 2 of the stipulation to be reasonable in part, but we modify Part 2 to recognize pending legislation to modify SB 408.

As Pacific Power notes, the rulemaking proceedings to adopt OAR 860-022-0041 raised concerns that the rule might create violations of normalization requirements of federal tax law.²³ To mitigate this concern, the Commission required utilities to seek PLRs from the IRS addressing whether SB 408 or the Commission's rule would cause a utility to violate federal tax law.²⁴ When the rule was amended in docket AR 517, the utilities were required to seek amended PLR requests. Pacific Power, like other utilities, sought and received a favorable PLR on the rule as written.

In this case, it is not clear how likely it is that the IRS would determine that the proposed amendment violates normalization rules. All parties agree that the amendment does not appear to give rise to any normalization violations. Nevertheless, given the amount of confusion surrounding the normalization rules and SB 408, we do not find it unreasonable that Pacific Power would wish to seek a determination from the IRS about the legality of the new amendment.²⁵ Obviously, if the IRS determines that the rule is appropriate as amended, the deferral balance would never be collected from ratepayers.

We will, however, modify one section of the stipulation. The stipulation states that Pacific Power will seek deferral of certain amounts, and that it will seek interest on the deferral balance at the blended treasury rate. According to the stipulation, the deferral balance "shall not accrue interest beyond one year commencing with the date the Commission adopts a permanent amendment to OAR 860-022-0041(4)(d)."²⁶ We conclude this provision should be modified to recognize that SB 967 has been introduced in the Oregon Legislature to revise SB 408. If SB 967 is ultimately passed and signed into law, our SB 408 rules would become moot, making it unnecessary and highly inefficient to conduct a permanent rulemaking proceeding to amend rules no longer substantively valid.

Consequently, we adopt Part 2 of the stipulation with the following modification: If SB 967 does not become law, the stipulation is approved as written. If SB 967 is passed this legislative session and signed into law, however, interest on the deferral balance may accrue for no longer than one year commencing with the date the Governor signs the bill into law. To the extent Pacific Power is able to seek a PLR based on the temporary rule or the stipulation, it may do so. The Commission cannot, however, commit to permanently amending rules that may no longer be applicable to Commission proceedings.

²³ See Docket AR 499, Order No. 06-532 at 3.

²⁴ *Id.* at 4.

²⁵ The Commission makes no determination in this docket about the merits of Pacific Power's deferral application, which is pending in docket UM 1523. The stipulation here is simply an agreement that Staff will support Pacific Power's application to seek a deferral under specific circumstances.

²⁶ Stipulation at 7.

In making this decision, we clarify that, in the event SB 967 becomes law, the temporary amendments to OAR 860-022-0041, made in Commission Order No. 11-064, will remain in effect and govern the automatic adjustment clause adopted with regard to Pacific Power's 2009 tax year. *See, e.g., BWK, Inc. v. Dep't. of Admin. Servs.*, 231 Or App. 214, 222 (2009) (temporary rule in effect at the time of relevant action governs proceeding even when new rules are later adopted).

IV. CONCLUSION

Staff and Pacific Power assert that the stipulation resolves all issues in this proceeding and request that the Commission issue an order adopting the stipulation in its entirety. CUB asks the Commission to adopt Part 1 of the stipulation but reject Part 2.

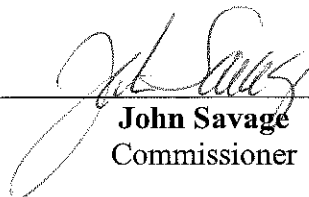
Based on our conclusions above, and our review of the stipulation and supporting documents, we agree with the Stipulating Parties that Pacific Power's amended 2009 tax report is consistent with ORS 757.268 and OAR 860-022-0041. We therefore adopt Part 1 of the stipulation. We find that Part 2 of the stipulation is reasonable as modified by this order, and adopt it as modified herein.

V. ORDER

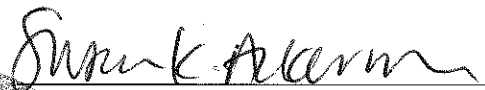
IT IS ORDERED that:

1. The stipulation, attached as Appendix A, as modified by this order, is adopted.
2. PacifiCorp, dba Pacific Power, must file compliance tariff schedules consistent with the terms of this order and the stipulation, as modified. The updated tariff schedules must have a June 1, 2011 effective date.

Made, entered and effective APR 11 2011


John Savage
 Commissioner




Susan K. Ackerman
 Commissioner

A party may request rehearing or reconsideration of this order under 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 860-001-0720. A copy of the request must also be served on each party to the proceedings as provided in OAR 860-001-0180(2). A party may appeal this order by filing a petition for review with the Court of Appeals in compliance with ORS 183.480 through 183.484.

BEFORE THE PUBLIC UTILITY COMMISSION
OF OREGON

UE 177(4)

In the Matter of:

PACIFICORP, dba PACIFIC POWER &
LIGHT COMPANY

Filing of tariffs establishing automatic
adjustment clauses under the terms of
SB 408

STIPULATION

This Stipulation resolves issues among the parties to this Stipulation related to PacifiCorp's 2009 Tax Report, filed in UE 177(4) pursuant to Senate Bill 408 (SB 408). SB 408 is codified in ORS 757.267, 757.268 and 757.210. Those statutes are implemented through OAR 860-022-0041.

I. PARTIES

The parties to this Stipulation are Staff of the Public Utility Commission of Oregon (Staff), PacifiCorp (or the Company), and the Citizens' Utility Board of Oregon (CUB) (together, the Parties). Other parties to this docket may join the Stipulation by signing and filing a copy of the Stipulation.

II. PROCEDURAL BACKGROUND

SB 408 requires certain Oregon public utilities to file an annual tax report with the Public Utility Commission of Oregon (Commission) that provides information on: (1) the amount of taxes paid by the utility to units of government or that was paid by affiliated groups and that is properly attributed to the utility's regulated operations; and (2) the amount of taxes authorized to be collected in rates. ORS 757.268(1). Under ORS 757.268(13)(f)(C), the Commission is required to adjust taxes paid "by deferred taxes related to the regulated operations of the utility."

1 The law requires the Commission to review the tax report to determine whether the
2 amount of taxes paid differs from the amount of taxes included in rates by more than
3 \$100,000. ORS 757.268(4). If so, the Commission must require the public utility to establish
4 an automatic adjustment clause to account for the difference. *Id.* The Commission must
5 complete its review of the tax report and order an automatic adjustment clause (AAC) if
6 necessary within 180 days after the tax report is filed. ORS 757.268(4); OAR 860-022-
7 0041(7).

8 As required by SB 408, on October 15, 2010, PacifiCorp filed its tax report for calendar
9 year 2009 (2009 Tax Report). The Commission held a prehearing conference on
10 November 1, 2010, at which Administrative Law Judge Wallace adopted a full procedural
11 schedule for this docket, including testimony and a hearing.

12 Staff served discovery and convened a workshop on November 17, 2010 to review
13 issues raised by the 2009 Tax Report. All parties were invited to participate, and
14 representatives from Staff, PacifiCorp, CUB, ICNU, and Portland General Electric Company
15 (PGE) attended. The parties convened settlement conferences on December 2 and 9, 2010,
16 and on January 6 and 7, 2011, which the Company, Staff, CUB and ICNU attended. The
17 settlement conferences were noticed to all parties in the docket.

18 As a result of the settlement conferences, the Parties have reached a two-part
19 settlement in this case. The first part of the settlement is supported by Staff, PacifiCorp and
20 CUB; the second part of the settlement is supported by Staff and PacifiCorp.

21 III. DESCRIPTION OF FILING

22 As originally filed, PacifiCorp's 2009 Tax Report reflected \$29.3 million of federal,
23 state, and local taxes paid above taxes authorized to be collected in rates. Cover Letter to
24 2009 Tax Report (October 15, 2010). Under SB 408, this difference, plus interest, is to be
25 collected as a surcharge through an Automatic Adjustment Clause (AAC). ORS 757.268(6).
26 PacifiCorp's AAC for state and federal taxes is contained in Schedule 102 and its AAC for

1 local taxes is contained in Schedule 103. In its originally filed 2009 Tax Report, PacifiCorp's
2 taxes paid were determined under the deferred income tax floor in OAR 860-022-0041(4)(d),
3 which was added to the SB 408 rules in Order No. 07-401 (Docket AR 517) and is designed
4 to ensure compliance with normalization requirements of the Internal Revenue Code by fully
5 protecting deferred taxes related to depreciation on public utility property.¹ The Internal
6 Revenue Code requires the inclusion of deferred income taxes associated with accelerated
7 tax depreciation on public utility property in rates in order for public utility property to be
8 eligible for accelerated depreciation for income tax purposes. The inclusion of deferred
9 income taxes associated with the regulated operations of the utility in determining taxes paid
10 is also required by SB 408 (ORS 757.268(13)(f)(C)). The Company reported increased
11 levels of deferred income tax expense during 2009 primarily as the result of the combination
12 of significant capital investment and bonus depreciation.

13 As described in Staff's Issues List attached hereto as Exhibit A, three initial issues
14 surfaced during the parties' audit of the 2009 Tax Report: (1) the Company's exclusion of
15 certain supplemental schedules in the calculation of taxes authorized to be collected in rates;
16 (2) the Company's inclusion of the impact of depreciation flow-through in the calculation of
17 the deferred tax floor under OAR 860-022-0041(4)(d); and (3) the Company's methodology
18 for allocating to Oregon the total Company book-tax difference for book and tax depreciation.
19 The first issue addresses the calculation of taxes collected and decreases taxes collected by
20 \$5.06 million; the second and third issues address the calculation of the deferred tax floor
21 and reduce the floor by \$7.18 million.

22 In the parties' initial settlement discussions, the Company agreed to Staff's
23 adjustments for purposes of settlement, lowering the Company's surcharge to \$27.3 million.
24 As partially described in Staff's Issues List, a final issue emerged at the conclusion of Staff's
25 investigation regarding the application of the deferred tax floor under OAR 860-022-

26 ¹ See Order No. 06-532, pages 3-5, for a discussion of normalization requirements.

1 0041(4)(d) as currently written. While Staff concluded that the Company properly applied the
2 deferred tax floor as required by OAR 860-022-0041(4)(d), Staff also reasoned that the
3 application of the deferred tax floor to the taxes paid result produced by the standalone
4 method is not necessary to ensure compliance with the normalization requirements of the
5 Internal Revenue Code. Staff has proposed to promptly commence a temporary rulemaking
6 process, followed by a permanent rulemaking to amend OAR 860-022-0041(4)(d) to conform
7 the rule to Staff's and CUB's view of its proper scope.

8 Under Staff's and CUB's approach to the deferred tax floor, PacifiCorp's taxes paid
9 would be determined under the standalone method, and Staff would continue to apply its
10 adjustment for supplemental schedules to PacifiCorp's taxes collected. The result is an
11 adjusted surcharge of \$13.47 million.

12 IV. AGREEMENT-PART 1 (STAFF, PACIFICORP, AND CUB)

13 A. Based upon the assumptions that: (1) the Commission will amend OAR 860-022-
14 0041(4)(d) so that the deferred tax floor does not apply to taxes paid determined under the
15 standalone method; and (2) the IRS will conclude that OAR 860-022-0041(4)(d) as so revised
16 is consistent with the normalization requirements of the Internal Revenue Code², the Parties
17 agree that PacifiCorp's taxes paid in its 2009 Tax Report shall be determined by the
18 standalone method. The Parties further agree that taxes collected shall be adjusted for the
19 inclusion of RAC deferrals in taxes authorized to be collected in rates. The result is an
20 adjusted surcharge of \$13.47 million.³

21 B. Upon issuance of a temporary amendment to OAR 860-022-0041(4)(d) making
22 the deferred tax floor inapplicable to taxes paid determined under the standalone method,
23 PacifiCorp will file a revised 2009 Tax Report incorporating these changes (Revised 2009
24 Tax Report). The Parties agree that the Revised 2009 Tax Report, filed pursuant to this
25

26 ² See Section V below for discussion on a request for a new ruling from the Internal Revenue Service.

³ See Joint Testimony filed separately in this docket for specifics of the calculation of the \$13.47 million.

1 Stipulation, complies with SB 408 and OAR 860-022-0041, as amended, and results in rates
2 that are fair, just, and reasonable.

3 C. The Parties agree that the 2009 Federal and State taxes paid results in a
4 surcharge of \$13,474,662 and a refund of \$86,932 for local taxes. Following is a table
5 showing PacifiCorp's estimates of interest during the deferral and amortization periods:
6

7 **Table 1**
8 **Amortization Summary**
9 **PACIFICORP 2009 Tax Report**

	<u>State /</u> <u>Federal</u>	<u>Local</u>
Surcharge (Refund)	\$ 13,474,662	(\$ 86,932)
Estimated interest through May 2011	\$ 2,137,802	(\$ 13,792)
Estimated interest June 2011 – May 2012	<u>\$ 157,295</u>	<u>(\$ 1,015)</u>
*		
Estimated amount to amortize	<u>\$15,769,759</u>	<u>(\$ 101,739)</u>

14 * Blended treasury rate of 2.01% calculated by PacifiCorp
15 per the methodology prescribed by Order No. 08-263 in
16 Docket UM 1147.

17 The total amortization for the combined 2009 Surcharge will be \$15,769,759 (including
18 interest) to be recovered during the 12-month period beginning June 1, 2011 through May 31,
19 2012 in Schedule 102 PacifiCorp's Income Tax Adjustment tariff. The proposed surcharge
20 will be allocated by customer rate schedule on an equal cents per kilowatt-hour basis, as
21 required by OAR 860-022-0041(8)(d). The local tax refund of \$101,739 reflected in the
22 Revised 2009 Tax Report will be implemented through Schedule 103, PacifiCorp's
23 Multnomah County Business Income Tax tariff.

24 Upon approval of this Stipulation, PacifiCorp will make a compliance filing to reflect (1)
25 the 2009 Surcharge of \$13,474,662, plus interest, in Schedule 102; and (2) the SB 408 local
26 tax refund of \$86,932, plus interest, in Schedule 103. The tariff schedules will reflect an

1 effective date of June 1, 2011, and reflect the 2011 Blended Treasury Rate (BTR) that will
2 apply to the amortization period.

3 The net change on June 1, 2011, will reflect the difference between the currently
4 effective Schedule 102 surcharge of approximately \$4.2 million implemented effective June
5 1, 2010, and the surcharge filed in the compliance filing in this docket. The resulting rate
6 impact will be an overall *increase* to net revenues of 1.2 percent.

7 **V. AGREEMENT-PART 2 (STAFF AND PACIFICORP)**

8 A. Under OAR 860-022-0041(8)(g), prior to the Commission implementing an
9 SB 408 rate adjustment, each utility was required to seek a Private Letter Ruling (PLR) from
10 the Internal Revenue Service (IRS) on whether the utility's compliance with SB 408 or OAR
11 860-022-0041 "would cause the utility to fail to comply with any provision of federal tax law,
12 including normalization requirements." Pursuant to OAR 860-022-0041(8)(g), PacifiCorp
13 initially submitted its PLR request to the IRS in December 2006.

14 After the Commission amended OAR 860-022-0041 in AR 517 to add the deferred tax
15 floor, the Company supplemented its PLR request by attaching the amended rules and
16 describing the deferred tax floor. The IRS issued PacifiCorp's PLR on January 9, 2008. The
17 ruling favorably determined that an adjustment to rates under SB 408, as constituted in ORS
18 statute and OAR rules presented at that time, would not violate the normalization
19 requirements of Internal Revenue Code §168(i)(9). PacifiCorp's favorable PLR was expressly
20 issued based on the representations and rule provisions cited in PacifiCorp's request. Priv.
21 Ltr. Rul. 101217-07 at 6 (Jan. 9, 2008). Because PacifiCorp's PLR was based in part on the
22 current language of OAR 860-022-0041(4)(d), PacifiCorp believes that it must submit any
23 revision of OAR 860-022-0041(4)(d) to the IRS and ask that a new, updated PLR be issued
24 in light of the proposed rule change. CUB does not agree that this step is necessary and
25 does not therefore support this Section V. of the Stipulation. CUB does not believe there is
26

1 any risk of a normalization violation, even with the amendment of the rule, or that a deferral is
2 needed.

3 B. Pending: (1) the Commission's adoption of a permanent amendment to
4 OAR 860-022-0041(4)(d) making the deferred tax floor inapplicable to taxes paid determined
5 under the standalone method; and (2) the IRS's issuance of a new PLR concluding that OAR
6 860-022-0041(4)(d) as so revised is consistent with the normalization requirements of the
7 Internal Revenue Code, Staff agrees to support before the Commission an application by
8 PacifiCorp to defer the difference between the surcharge produced by deferred tax floor
9 (\$27.3 million) and the surcharge agreed to in Part 1 (\$13.47 million) (2009 Tax Report
10 deferral). This difference is \$13.83 million.

11 Staff and PacifiCorp agree that PacifiCorp will file its application for deferral with the
12 Commission by no later than February 15, 2011, and that the application will request that
13 interest accrue during the deferral period at the Blended Treasury Rate (BTR); PacifiCorp's
14 agreement to request the BTR is expressly for settlement purposes only and is not
15 precedential.

16 Staff and PacifiCorp further agree that, if granted, the 2009 Tax Report deferral shall
17 not accrue interest beyond one year commencing with the date the Commission adopts a
18 permanent amendment to OAR 860-022-0041(4)(d). CUB does not agree to support the PLR
19 application.

20 C. Staff and PacifiCorp agree to work cooperatively on the new PLR request to the
21 IRS. Staff and PacifiCorp agree to submit the new PLR request to the IRS expeditiously upon
22 issuance of a permanent amendment to OAR 860-022-0041(4)(d).

23 D. If the Commission does not adopt a permanent amendment to OAR 860-022-
24 0041(4)(d) making the deferred tax floor inapplicable to taxes paid determined under the
25 standalone method; and/or the IRS concludes that OAR 860-022-0041(4)(d) as so revised is
26 not consistent with the normalization requirements of the Internal Revenue Code, Staff

1 agrees to support PacifiCorp's request to amortize the deferral balance of \$13.83 million plus
2 accrued interest.

3 **VI. GENERAL PROVISIONS**

4 A. The Stipulating Parties agree that the Stipulation represents a compromise of the
5 positions of the parties for the purpose of this docket. Without the written consent of all
6 parties, evidence of conduct or statements, including but not limited to term sheets or other
7 documents created solely for use in settlement conferences in this docket, are confidential
8 and not admissible in the instant or any subsequent proceedings, unless independently
9 discoverable or offered for other purposes allowed under ORS 40.190. Nothing in this
10 paragraph precludes a party from explaining as a factual matter what the Parties agreed to in
11 this Stipulation.

12 B. If this Stipulation is challenged by any other party to this proceeding, or any other
13 party seeks an adjustment amount that departs from the terms of this Stipulation, the
14 Stipulating Parties reserve the right to cross-examine witnesses and put in such evidence as
15 they deem appropriate to respond fully to the issues presented including the right to raise
16 issues that are incorporated in the settlement embodied in this Stipulation. Notwithstanding
17 this reservation of rights, the Stipulating Parties agree they will continue to support the
18 Commission's adoption of the terms of this Stipulation.

19 C. If the Commission rejects all or any material part of this Stipulation, or adds any
20 material condition to any final order that is not consistent with this Stipulation, each
21 Stipulating Party reserves its right, pursuant to OAR 860-001-0350(9), to present evidence
22 and argument on the record in support of the Stipulation or to withdraw from the Stipulation.
23 Parties shall be entitled to seek rehearing or reconsideration pursuant to OAR 860-001-0720.

24 D. This Stipulation will be offered into the record in this proceeding as evidence
25 pursuant to OAR 860-001-0350(7). The Stipulating Parties agree to support this Stipulation
26 throughout this proceeding and in any appeal, provide witnesses to support the Stipulation at

1 the hearing, and recommend that the Commission issue an order implementing the terms of
2 the Stipulation.

3 E. By entering into this Stipulation, no Stipulating Party shall be deemed to have
4 approved, admitted or consented to the facts, principles, methods or theories employed by
5 any other Stipulating Party in arriving at the terms of this Stipulation. Except as provided in
6 this Stipulation, no Stipulating Party shall be deemed to have agreed to any provision of this
7 Stipulation is appropriate for resolving issues in any other proceeding.

8 F. This Stipulation may be signed in any number of counterparts, each of which will
9 be deemed an original for all purposes, but all of which taken together will constitute one and
10 the same agreement.

11 This Stipulation is entered into by each party on the date entered below such Party's
12 signature.

Signature page follows

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STAFF

PACIFICORP

By: Paul A. Mahoney for Jason W. Jones

By: _____

Date: Jan 14, 2011

Date: _____

CUB

By: _____

Date: _____

1 STAFF

PACIFICORP

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3 By: _____

By: Andrea Kelly

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Date: _____

Date: 14 Jan 2011

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6 CUB

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ORDER NO.

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1 STAFF

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ORDER NO.

TT 120

UE 177 (4)

Exhibit A

To

Stipulation

January 14, 2011

**PUBLIC UTILITY COMMISSION
OF OREGON**

UE 177(4)

STAFF ISSUES LIST

**Carla Owings
Dustin Ball
Deborah Garcia**

**In the Matter of
PACIFICORP's
Senate Bill 408 Tax Filing
for 2009 Tax Period**

December 23, 2010

**SENATE BILL 408, TAX FILINGS
STAFF'S INITIAL FINDINGS
FOR PACIFICORP – UE 177(4)**

TO: LEE SPARLING, MAURY GALBRAITH, JUDY JOHNSON AND
JASON JONES

RE: PACIFICORP – UE 177 (4)
SB 408 TAX FILINGS
2009 TAX PERIOD

FROM: CARLA OWINGS, SENIOR UTILITY ANALYST,
DUSTIN BALL, SENIOR UTILITY ANALYST, AND
DEBORAH GARCIA, SENIOR UTILITY ANALYST
PUBLIC UTILITY COMMISSION

DATE: DECEMBER 23, 2010

CC: ALL PARTIES

On October 15, 2010, PacifiCorp (PPL or Company) filed UE 177(4), its tax report covering the 2009 calendar year pursuant to Senate Bill 408 (SB 408) (codified at ORS 757.267, 757.268 and OAR 860-022-0041).

Much of the information contained in these tax reports represents highly confidential and sensitive information. Staff has structured its initial findings in this report in a generic manner in order to avoid the possibility of disclosing confidential, or sensitive, information.

Staff has thoroughly reviewed each calculation and all documentation provided by the Company.

At the conclusion of Staff's review and after some of the Parties¹ had reached an agreement in principle for settlement Staff discovered a potential inconsistency between SB 408 and OAR 860-022-0041. The inconsistency involves the manner for determining the existence of a normalization violation² under (4)(d) of the commission rule and under Staff's template. The impact of improperly applying the normalization violation test (on Page 8 of Staff's template) results in a significant surcharge proposed by PPL's 2009 SB408 filing.

Upon discovering this issue, Staff immediately consulted with the Assistant Attorney General's (AAG or Staff's Counsel) office and our upper management team. As a result of those discussions, Staff requested a delay of six days from December 17, 2010 to December 23, 2010 to publish this issues list. In addition, Staff and its Counsel held phone discussions with each of the Utility companies as well as the Parties represented at the Settlement conference³ to notify them of the potential impacts of this issue. Staff also informed the Parties that we could not go forward with the initial agreements made at the Settlement Conferences.

The basis of the Staff recommendation in this report outlines the foundation of Staff's findings and agreements made in Settlement discussions. Most importantly, these recommendations are based upon rule implementation prior to Staff's discovery of the issue described above.

Staff is in the process of investigating the validity of the assumption that the rules and Staff's template conflict with the original intent of the test for a Normalization Violation. If Staff concludes there is a conflict in the rules and Staff's template from the intent of SB408, then the findings in the report below would change significantly. Staff's Testimony is scheduled to be published on January 11, 2011 which would incorporate the findings of Staff's investigation into this matter. If Staff's investigation concludes that there is no conflict between the current rules and Normalization Violations, Staff will likely propose settlement based upon the original agreements described below.

SUMMARY OF 2009 SB 408 IMPACT:

PPL reports the following for its Regulated Results of Operations for the 2009 tax period:

¹ The Parties to the Stipulated Agreements are defined in the section "Summary of Review" section on Page 4 below.

² Discussed in section "Staff Review" on page 5 below.

³ Id.

Table 1-Original Filing

Federal and State Taxes Paid to units of Government	Taxes Collected	Surcharge	Interest⁴ (7/1/09 through 6/1/2011)	Total Surcharge
\$98.4 million	\$69.0 million	\$29.4 million	\$4.7 million	\$34.1 million
Local Taxes Paid to units of Government	Taxes Collected	Refund	Interest⁵ (7/1/09 through 6/1/2011)	Total Refund
\$132,000	\$45,000	(\$87,000)	\$14,000	(\$101,000)

PPL's original filing reflected a total surcharge related to the Federal and State tax true-up for the 2009 tax period of approximately \$34.1 million including interest through the deferral period of approximately \$4.7 million.

The variance between local taxes paid and taxes collected results in a refund of approximately \$87,000. Interest of approximately \$14,000 will accrue on this balance beginning July 1, 2009 through June 1, 2011. PPL estimates an additional \$1,100 of interest will accrue during the amortization phase, based upon the current Blended Treasury rate.

Table 2 below shows the summary of changes proposed by Staff.

Table 2- Staff Recommendation

Federal and State Taxes Paid to units of Government	Taxes Collected	Surcharge	Interest⁶ (7/1/09 through 6/1/2011)	Total Surcharge
\$91.2 million	\$63.7 million	\$27.3 million	\$4.3 million	\$31.6 million

⁴ Estimate includes interest through deferral period.

⁵ Estimate includes interest applied through deferral period.

⁶ Estimate includes interest applied through deferral period.

Local Taxes Paid to units of Government	Taxes Collected	Refund	Interest ⁷ (7/1/09 through 6/1/2011)	Total Refund
\$132,000	\$45,000	(\$87,000)	\$14,000	(\$101,000)

Staff proposes amendments⁸ resulting in a surcharge of approximately \$27.3 million. Staff estimates interest accruing during deferral period to be approximately \$4.3 million, resulting in a total surcharge of approximately \$31.6 million. Additional interest will accrue during the amortization phase at the 2011 Blended Treasury rate. Currently that rate is 2.24 percent and represents an interest accrual of approximately an additional \$358,000.

PPL's surcharge based on Staff's findings total approximately \$31.6 million⁹ and would represent an increase of approximately 3.2 percent to PPL's retail rates without consideration of the removal of the current SB 408 surcharge that relates to prior periods.

For local taxes, Staff proposes no amendments and is in support of the amounts proposed by PPL for a refund of approximately \$102,000¹⁰. This refund would be implemented simultaneously with the surcharge generated from the true-up related to the State and Federal tax true-up. For this reason, PPL's Multnomah County ratepayers will experience a slightly smaller rate increase than those outside of the Multnomah County jurisdiction.

Prior to rate implementation June 1, 2011, Staff will review the balance remaining of the 12-month amortization for the prior year's SB 408 implementation related to 2008 tax period. Any estimates of over or under collections of previous years' surcharges will be updated and included in the compliance filing implemented June 1, 2011.

SUMMARY OF REVIEW:

At the conclusion of a settlement discussion held December 9, 2010, Staff, and the Company were able to reach an agreement in principal based upon modifications described in the Staff Review section below. The Citizens' Utility Board (CUB) and the Industrial Customers of Northwest Utilities (ICNU)(collectively, the Customer Groups) were unable to support a stipulation as of the time of this filing. Due to Staff's investigation of Normalization

⁷ Estimate of interest through deferral period.

⁸ See section on "Staff Review" for specific amendments.

⁹ Including interest during deferral and an estimate of interest during amortization based upon the current Blended Treasury rate.

¹⁰ Includes interest during deferral period and an estimate of interest during amortization.

Violations, Staff withdrew from the agreements made in the settlement conference described above.

STAFF REVIEW:

Staff conducted face to face interviews on November 17, 2010, December 2, 2010, and again on December 9, 2010. CUB and ICNU were present for each meeting and participated in these discussions. Staff sent data requests and conducted informal phone discussions.

The Company provided several work papers, an electronic version of Staff's Tax form and responses to Staff's data requests.

In general, SB408 defines taxes paid as the "lesser of" three alternative calculations: (1) the utility's stand alone tax liability; (2) the total consolidated tax liability of the affiliated group; and (3) the total consolidated tax liability of the affiliated group "properly attributed" to the regulated operations of the utility.

Commission Order 07-401 adopted specific rules to preclude "taxes paid" from falling below the utility's deferred tax balance related to the depreciation of its public utility property. Such a scenario would create a normalization violation by allowing ratepayers to share in the benefits received from accelerated depreciation. Specifically, OAR 860-022-0041(4)(d) requires that we rely upon the lowest of the three "taxes paid" methods except that the lowest method cannot produce a result that is less than the deferred taxes related to public utility property for regulated operations of the utility, reduced by any tax refunds recognized in the reporting period, and allocated to the regulated operations of the utility.

Page 8 of Staff's template, provides for this alternative calculation. Here the reporting utility must enter the amount of deferred taxes related to depreciation of public utility property (hereafter referred to as the "4(d) tax limitation") for the regulated operations in Oregon. This amount is then reduced by the amount of refund recognized in the reporting period that is allocable to the regulated operations.

For the 2009 tax period, PPL falls under the 4(d) tax limitation. The outcome of the three alternative calculations (described above) results in the deferred tax balance related to the depreciation of public utility property that is higher than the lowest of the three alternative methods. Choosing the any of the alternative methods would result in a normalization violation. Therefore, Staff supports the use of the 4(d) tax limitation.

One of the driving forces for this result is the extremely high level of accelerated depreciation associated with the renewable resources that PPL has

acquired during the 2009 tax period. As a result of our review, Staff identified the following issues regarding PPL's original filing:

(1) Taxes Paid – 4(d) Tax Limitation:

- Flow-Through;
- Allocation method verses separate Power Tax Report; and

(2) Taxes Collected – Net to Gross and Effective Tax Ratios.

(1) Taxes Paid – 4(d) Tax Limitation:

After the application of the three methods described above, PPL reports that its balance of its 4(d) tax limitation is greater than the lowest of the three methods to calculate "taxes paid" described above.

Although PPL does acknowledge receipt of a tax refund during the same tax period, PPL states that this refund is not "allocable" to the Oregon regulated operations and further, that the status of the refund is non-final as current estimates of final determination are June 30, 2012¹¹. Staff concurs, the refund does not appear to be allocable to the Oregon jurisdiction.

Flow-through - PPL includes approximately \$5.2 million of "flow-through" in the amount attributable to the 4(d) tax limitation which represents flow-through depreciation for pre-1981 assets. Flow-through is simply allowing the benefit of depreciation to "flow-through" to ratepayers. In years prior to 1981, the sharing of the benefit of depreciation was allowed by the Internal Revenue Service. Currently, the sharing this benefit is referred to as a normalization violation and is the very purpose of establishing the 4(d) tax limitation.

Commission Order No. 07-401 adopts the 4(d) tax limitation¹² to protect against normalization violations. Since the \$5.2 million of flow-through represents the benefit of depreciation that has *already* passed to ratepayers prior to 1981, excluding it from the 4(d) tax limitation does not create a normalization violation. As pointed out at page 6 of the above-referenced Order; "a normalization violation is not a matter of degree; it either *is* or *is not* a normalization violation." It is Staff's position that the benefit of depreciation cannot be passed a second time, therefore, Staff believes it is appropriate to remove this amount from the balance of deferred taxes.

¹¹ PPL's response to Staff DR No. 7

¹² See Commission Order 07-401 at 6.

After discussions with Staff, PPL has agreed to remove this adjustment in an effort to resolve differences and come to a Stipulated agreement with Staff.

Staff recommends that PPL remove \$5.2 million from the balance reported on the Staff Template, page 8, Line 1 resulting in a decrease to PPL's surcharge of \$5.2 million.

Allocation method verses separate Power Tax Report - In previous SB 408 filings, PPL has calculated the balance of deferred taxes that relate to depreciation of public utility property by using the values determined for PPL's total system operations and then allocating those amounts to Oregon using the factors that are generated when preparing the Results of Operations Report for Oregon.

For the 2009 tax period, PPL ran a separate report using its power tax system to determine the value of the balance for deferred taxes. During the review process, Staff compared the outcome of the two methods and determined that the variance between the two methods creates a significant gap in amounts attributable to the deferred tax balance for the Oregon jurisdiction and thus, to the balance of the 4(d) tax limitation¹³. The tax benefit related to the larger amount of deferred taxes determined in the Power Tax program results in an increase to PPL's surcharge of approximately \$2.9 million.

PPL believes that the separate report provides better accuracy as well as more clarity by separately identifying the exact balances attributable to each asset.

Staff believes that since deferred tax balances are established in rates on a jurisdictional allocation basis, that using the allocations would more properly reflect what is being collected in rates.

Staff recommends that PPL allocate the amount attributable to the deferred tax balance of depreciation for public utility property to the Oregon Regulated Operations rather than to run a separate Power Tax report to determine the balance. Using allocations to determine the balance results in a reduction of approximately \$2.9 million to PPL's proposed surcharge.

(2) Taxes Collected – Net to Gross and Effective Tax Ratios;

OAR 860-022-0041(2)(A)(i)-(ii) states that the revenue reported in a utility's results of operations shall be multiplied by the ratio of *net revenues to gross revenues* using the pretax income and revenue the Commission authorized in establishing rates and revenue requirement; and, the effective tax rate used by the Commission in establishing rates for the time period covered by the tax report

¹³ Discussed in "Staff Review" on page 5 above.

as set forth in the most recent general rate order or *other order that establishes an effective tax rate*, calculated as the ratio of the total income tax expense in the revenue requirement to pre-tax income.

Further, OAR 860-022-0041(2)(n) describes "revenue" as being the utility's Oregon retail revenues, excluding supplemental schedules or other revenues not included in the utility's revenue requirement and adjusted for any *rate adjustment* imposed under this rule.

Staff believes that to determine the net to gross and effective tax ratios, Staff must rely upon the most recent general rate proceeding modified for any rate revisions that take place during the tax period. Any schedule that includes a revenue requirement and thus includes a tax component for the collection of taxes in rates should be included in the calculation of these ratios.

PPL originally excluded supplemental schedules related to its renewable adjustment clauses (or RAC) filings from the calculation of net to gross and effective tax ratios due to the language in the rule that allows for the exclusion of supplemental schedules.

Due to the generous tax credits available to the utilities for renewable resources, RAC filings have a negative tax component set in the proposed rate structure in order to pass the benefit of tax credits to ratepayers through rates. Including these schedules in the calculation of the ratios increases PPL's surcharge by approximately \$5.8 million. However, Staff believes that this modification is consistent with OAR 860-022-0041(2)(n) and recommends that PPL modify its filing to reflect the change.

Staff recommends PPL recalculate the net to gross and effective tax rate ratios to include all schedules that contain a tax component and reflect a rate modification during the tax period. This modification increases PPL's surcharge by approximately \$5.8 million.