ORDER NO. 00-111

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BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

UP 158

In the Matter of the Application of PORTLAND GENERAL ELECTRIC COMPANY in Regard to the Sale of Property.	))))	ORDER

DISPOSITION: APPLICATION FOR APPROVAL OF COLSTRIP SALE DENIED

Background. On March 18, 1999, Portland General Electric Company (PGE) applied for Commission approval for the sale of its 20 percent ownership share of Colstrip generating units 3 and 4 along with associated transmission assets to PP&L Global, Inc. (Global), a subsidiary of PP&L Resources, Inc. PGE's sale of its share of Colstrip generating units 3 and 4 was part of the auction of all of Montana Power Company's (MPC) generating assets. PGE amended its application on April 7, 1999, to correct an error in the calculation of transition costs.

Staff reviewed PGE's application and on September 2, 1999, filed testimony recommending disapproval of the application. On September 27, 1999, PGE filed rebuttal testimony contesting Staff's position. The parties agreed that no hearing was necessary and filed two rounds of briefs on November 15 and December 6, 1999. Industrial Customers of Northwest Utilities (ICNU), an intervenor, filed a reply brief as well.

Global offers $230.4 million to PGE for its Colstrip interest plus transmission facilities and $193 million for the Colstrip interest alone. Global's offer arose out of an auction conducted by an investment firm for MPC, the owner of 30 percent of Colstrip. Puget Sound Energy, Inc. (PSE), which owns 25 percent of Colstrip, and PGE, which owns 20 percent, also participated in the auction.[1]

[1] Washington Water Power (now known as Avista) owns 15 percent of Colstrip; PacifiCorp owns 10 percent. Those companies elected not to sell their shares of the plant.

Colstrip is included in PGE's rate base, and PGE uses Colstrip to meet its obligations as a public utility. Colstrip is capable of producing 750 megawatts (MW) of power. At the time PGE filed its application, Colstrip had a remaining productive life of 26 years.

Statutory Standard. ORS 757.480 provides that PGE must obtain the Commission's approval before selling any property of a value in excess of $100,000. In applying that statute, the Commission adopted OAR 860-027-0025(1)(l), which provides that a utility must show that any proposed sale will be "consistent with the public interest." In its testimony, Staff argued that the rule language means the Commission must make a finding that customers would benefit from the sale. PGE asserted that the proper standard in this case is one of "no harm" to the customers. In its brief, Staff agreed with PGE that a proper application of the public interest test in OAR 860-027-0025(1)(l) means that the Commission need only find that ratepayers will not be harmed by the sale.

ICNU urges the Commission not to adopt a precedential standard of review in this case but to retain the flexibility to consider standards of review on a case-by-case basis, consistent with the public interest standard articulated in the rule. ICNU believes that the standard in this case should be a showing of net customer benefits. ICNU argues that neither Staff nor PGE cites to any authority to support their position that the rule should be read as requiring no harm to ratepayers. Under certain circumstances, ICNU argues, a weighing of benefits may be more appropriate than the no harm standard. ORS 757.480 applies to mergers as well as sales of utility property; ICNU contends that the no harm standard may not be appropriate in the case of mergers.

The Commission agrees with PGE and Staff that the no harm standard should apply in this case. We agree with ICNU that the public interest may, in another case, and under additional statutes, require a different standard. [2] We find that in this case the no harm standard is consistent with the public interest.

Standards for Decision. Two issues merit discussion before we examine the parties' positions and the consequences we draw from their arguments. First, the parties have advanced arguments about the role of the Commission in view of Senate Bill (SB) 1149, the electric restructuring bill passed by the Legislature in 1999. SB 1149 encourages divestiture as one way of introducing competition into the generation of electricity.

PGE implies that it must sell Colstrip in light of industry restructuring. We disagree. Section 6 of SB 1149 reads:

> The commission may provide incentives for divestiture to unaffiliated persons of the generation assets of an electric company, or the structural separation of such assets. The commission shall ensure that divestiture

[2] ORS 757.511 applies to mergers.

> does not deprive consumers of the benefit of the utility's or the region's low-cost resources, independent of the power supplier.

Leaving aside the question whether Colstrip is a low-cost resource, the above passage states that the Commission's role in providing incentives for divestiture is discretionary. We intend to move toward competition, but not at the expense of protecting ratepayers. Further, nothing in SB 1149 restricts our statutory duty to ensure that the sale of utility assets is consistent with the public interest. Our job under SB 1149 is to encourage divestiture where it is appropriate. That can be judged only on a case-by-case basis. Our job under existing statutes is to ensure that utility behavior over which we have jurisdiction does not harm ratepayers. The two mandates are not contradictory.

Second, we believe that in applying the no harm standard, we must look to the applicant to convince us that no harm will accrue to ratepayers from the sale. We have evaluated the parties' arguments from this perspective. Our decision, detailed below, reflects our assessment that PGE has not prevailed in convincing us that ratepayers will suffer no harm by the sale of its Colstrip assets. This does not mean that we adopt Staff's position or accept Staff's arguments without reservation. It does not mean that we reject out of hand PGE's arguments that ratepayers would benefit from the Colstrip sale in the near term. It means that, in our view, Staff has raised enough serious questions about the effect of the Colstrip sale to outweigh the benefits that PGE claims will flow from it. In short, the benefits that PGE points out do not override the potential harm to ratepayers that Staff claims.

Position of the Parties. *Overview.* PGE asserts that the Commission should approve its application because PGE must sell the facilities and the sale price represents maximum value for PGE's ownership interest in Colstrip, as the winning bid in an auction. PGE reads the no harm standard to mean that if PGE received fair market value for the Colstrip assets, considering the context of the reasons for and against the sale, ratepayers are not harmed and the sale should be approved. ICNU also contends that the Commission should approve PGE's proposed sale of Colstrip.

Staff analyzed PGE's application and on a cost/benefit analysis determined that PGE's ratepayers will be harmed by the sale. Staff argues that the sale of Colstrip as structured will result in a $71.3 million loss to ratepayers over Colstrip's remaining life. As a result of its analysis, Staff takes the position that the Commission should not approve the proposed sale of Colstrip.

Staff's Analysis of PGE's Application. Staff's analysis shows that ratepayers will suffer a $71.3 million loss from Colstrip's sale over the 26-year remaining life of the plant. Staff's analysis used the net present value method and was based primarily on PGE's initial analysis. Staff made seven major adjustments to PGE's analysis, as set out below.

1. PGE's analysis assumed that the Colstrip sale would close by January 1, 1999, allowing Colstrip to be removed from rate base. PGE estimated that removing Colstrip from rates and replacing it with less expensive purchases of wholesale power would reduce revenue requirement by $32.1 million. The Staff analysis assumes that PGE customers would not experience a rate reduction in 1999, because the PGE proposed sale of Colstrip would not be approved until late 1999, at the earliest. Therefore, Staff reduced PGE's estimate of the Colstrip benefits by $32.1 million. Staff's analysis (and PGE's initial analysis) also indicates that as time goes on, Colstrip will depreciate and the price of market power, according to forecasts, will increase.

2. Staff adjusted PGE's base case to include the capital loss recovery of $18.9 million associated with the Colstrip sale. According to Staff, PGE calculated a nearly identical stranded cost, or capital loss, from the sale, based on subtraction of the plant's book value from the sales price received, and accounting for related tax effects. PGE did not include the $18.9 million in its analysis, although ratepayers are responsible for paying for it and those monies would be included in rates.[3]

3. Staff recalculated Colstrip's historic availability in opposition to the annual availability factor (AAF) that PGE uses. The AAF indicates plant reliability. The higher the number, the more electricity a plant will produce at the same fixed operating cost. The higher the AAF, the more replacement power is required if the plant is sold. Thus the higher Colstrip's AAF, the more costs are associated with selling it.

PGE developed its AAF of 84 percent using a broad national average of electric generation plants. PGE based its AAF on a national average because Colstrip has a relatively short operating history (14 years). Staff considered it best to use actual data but did not use the entire 14-year history of the plant. Instead, Staff relied on a three-year and an eight-year Colstrip AAF. Staff reasoned that the earliest years in a plant's operation always show startup difficulties, while reliability improves over time. Maintenance and equipment upgrades are targeted to ensure that the problems from the earliest years do not recur. According to Staff, Colstrip has rarely had an AAF equal to or lower than PGE's suggested 84 percent. The use of more recent data reflects numerous upgrades PGE has made to improve Colstrip's output and reliability. Staff's AAF is 87 percent.

4. Staff's fourth adjustment uses a natural gas price forecast based on an average of several recent independent gas price forecasts. The price of natural gas is assumed to have an effect on the market price of electricity and thus on replacement

[3] Order No. 99-033 (UE 102) directed that excess deferred tax benefits and investment tax credits, which customers would receive if the plant remained in service, should be included in the calculation of transition costs. On April 12, 1999, PGE requested a ruling from the Internal Revenue Service (IRS) regarding whether the proposed treatment would violate the normalization requirements and thus could not be followed. If the IRS rules that those tax benefits cannot be passed on to customers, Order No. 99-033 will have to be modified. The IRS preliminary ruling found that the excess deferred tax benefits and investment tax credits must be assigned to shareholders. The final ruling has not yet been issued, however, so calculation of transition type costs cannot be made at this point.

power costs for Colstrip. Lower natural gas prices will contribute to lower market prices for electricity and vice versa. The higher the price of natural gas, the lower the benefits of selling Colstrip, because replacement power costs for Colstrip are higher. Staff used more recent information with respect to natural gas price forecasts than was available at the time of the auction. Staff's adjustment decreases the benefit of selling Colstrip by $8.1 million.

5. Staff assumes a 40-year operating life for Colstrip, as opposed to PGE's assumption that Colstrip 3 will have an operational life of 40 years and Colstrip 4 of 38 years. Staff believes that Colstrip's combined economic life should be at least one year longer. The current owners of Colstrip have depreciation schedules that assume a 40-year life for Colstrip 3 and 4 together. Adding the year 2025 to the analysis decreases the net benefits of selling Colstrip by $5.9 million.

6. Staff assumes that PGE will purchase replacement power for Colstrip at the market price for the first two years after the sale. When Staff filed its testimony, PGE had entered into negotiations with Global to purchase replacement power but had not agreed on a price. Staff assumed that PGE will not agree to a price above the market price of electricity. Staff therefore used its estimate of the market price for electricity for the first two years of its cost/benefit analysis. This assumption increases the benefits of selling Colstrip by $4.1 million. Subsequently, PGE entered into a contract for power with PP&L Montana. Staff used the contract price in its revised analysis. The effect of using the contract price is to increase the loss to ratepayers by about $3.9 million, bringing the loss to ratepayers from the sale of Colstrip to approximately $75 million.

7. Finally, Staff reviewed the Montana energy tax and uses a different forecast than PGE used. PGE had originally forecasted that the energy tax would increase at the rate of inflation. New information indicated that the tax would remain constant over the life of Colstrip. This adjustment raised the cost of selling Colstrip by $1.9 million.

Other Concerns: BPA. In reviewing PGE's application, Staff noted some additional concerns. Staff maintained that the Colstrip sale would likely have a negative effect on the level of access to federal power. The Bonneville Power Administration (BPA) and other parties have been discussing how to provide federal power benefits to the residential and small farm customers of the Pacific Northwest investor owned utilities. BPA has begun a process of developing final policies on the treatment of loads and resources under the Pacific Northwest Power Planning Act (the Act). These policies will determine the level of power eligible customers can purchase from BPA under a net requirements contract. If a utility does not have enough power to cover its loads, the utility can purchase BPA power to cover its deficit. BPA has said that it would continue to count resources as being available to the utility if the sale of the resource was not handled in a way that BPA deems reasonable. BPA has not published its final policy statement on this issue.

PGE has obtained no assurance from BPA with respect to how the Colstrip sale will be treated, and Staff fears that the proposed sale could receive unfavorable treatment from BPA, thus causing residential and small farm customers to face reduced access to federal power. Staff believes that PGE should obtain written confirmation from BPA regarding how it will treat the Colstrip sale.

Other Concerns: PGE's Need for Colstrip. Staff expresses concern that with respect to BPA, PGE claims to have loads greater than resources and in deciding whether it needs Colstrip, PGE claims to have resources greater than loads. Putting aside the question of loads and resources, however, Staff argues that the decision whether to approve the Colstrip sale is an economic one. If over the life of the plant, Colstrip's costs are below market, then the cost of electricity to PGE's customers will be lower if PGE retains the plant. Given the same assumption, retention of Colstrip will also help PGE hedge its risks on the open market.

PGE contends that it does not need Colstrip to meet its load requirements. PGE's chart comparing its resources and loads (Exhibit Hager/1) assumes that PGE serves no commercial or industrial loads. The order in Docket UE 102, however, assumes that PGE could continue to serve commercial and industrial customers on a cost based rate. Staff asserts that under the assumption that PGE continues to serve 50 percent of its commercial customers and 15 percent of its industrial customers, Colstrip is necessary to serve loads. Staff believes that even under PGE's approach of retaining resources to match load obligations, Colstrip is necessary to serve retail loads.

Staff argues that PGE's claim not to need Colstrip is erroneous. PGE's Exhibit Hager/1 alleges that absent 100 percent of its industrial customers, and given the weather in 1998, PGE would have been able to meet its loads without Colstrip. Staff assumed that 50 percent of commercial customers and 15 percent of industrial customers would either stay with PGE on a cost of service plan or would use PGE as a default supplier. In addition, Staff used the moderate growth figure from PGE's last least cost plan to estimate residential load growth. PGE responded positively to Staff data requests 93-94 asking whether Colstrip would be used to meet native load. PGE's data request responses support Staff's conclusion that even under its conservative assumptions, PGE needs Colstrip just to meet its load requirements.

Staff argues that the assumptions it made in its data requests 93 and 94 regarding industrial and commercial customers are more reasonable than PGE's, based on past Commission orders and recent legislation. The UE 102 order provides for a cost of service rate to both commercial and industrial customers. Order No. 99-033 states, at 32:

> We adopt a cost of service rate. A cost of service rate will reduce for all customers the market risk which is one of our primary reasons for not adopting PGE's plan as a whole. It will also provide customers with a stable rate—a matter that is of particular importance to residential customers. We will also adopt Staff's proposal that industrial and commercial customers who choose direct access would not be allowed to go back to the cost of service rate. We agree with Staff that such switching, with attendant resource planning and cost effects, could harm

both the customers remaining on the cost of service rate and the company providing that service.

This implies that the Commission did not require all industrial and commercial customers to leave the system. SB 1149 requires PGE to offer a cost of service rate to small commercial customers. SB 1149 also allows the Commission the option of requiring a cost of service rate for larger commercial and industrial customers. Given the cost of service rate option, fewer customers than PGE predicts are likely to leave the system.

Other Concerns: Revenue Requirement Issues. If the application is approved, Staff and PGE agree that the rate consequences would be a $26.55 million rate reduction excluding transition costs. Staff also recommends that the Commission should direct PGE to establish a balancing account for subsequent Commission disposition. Staff opposes PGE's request to set up a deferred account as part of the order in this proceeding. Because we elect not to approve the sale, this issue does not come into play and is not further developed.

Other Concerns: Penalty Provision. The sale is structured in such a way that Global will pay $248 million if PGE's share of Colstrip is sold, but only $193 million of that amount would go to PGE and its customers. MPC and PSE would split the remaining $55 million. Staff is concerned that this payment plan reflects interests other than PGE's and indicates that PGE may not be receiving market value for its Colstrip share.

PGE's Position. PGE agrees with Staff that the no harm standard should apply. However, PGE and Staff disagree about the implications of that standard. Staff relies on a 26-year numerical cost/benefit analysis for its recommended denial of the application. PGE argues that such an analysis is inappropriate to this case. PGE also contends that Staff’s reliance on its numerical analysis is at odds with prior Commission orders. For instance, in Order No. 93-1117, the Commission differentiated between net benefits and the public interest, stating that a finding of public interest is potentially much more inclusive than the economic calculation that constitutes a determination of net benefits.

PGE maintains that the Commission should determine whether PGE received fair market value for its assets given all the pros and cons of the sale. PGE points out that SB 1149 raises the specter of loss for regulated utilities. One goal of the bill is divestiture of utility generating assets. The issue for PGE is whether to retain generation sufficient to serve all of its current and expected future customers or whether it should dispose of resources that may represent excess capacity in the future. PGE argues that it would be unwise to saddle its native load customers with surplus generation capacity.

PGE also argues that the Commission should consider the timing of the proposed sale. Colstrip is jointly owned. MPC owns the largest share of the plant, and the State of Montana has ordered deregulation of its electric utility system. MPC initiated an auction process and invited other Colstrip owners to join in the sale. Both PGE and PSE participated. The winning bidder expressed a strong desire to obtain a controlling interest in the plant, something PGE could help supply in that sale.

PGE also recognized that whoever the buyer was would want to operate the plant as an exempt wholesale generator (EWG). An EWG markets power in the wholesale market and is not regulated by state Commissions, as PGE is. EWGs are highly competitive and guard their market information carefully. Co-ownership with an EWG did not seem advantageous to PGE. PGE also recognized that if it did not sell along with MPC and PSE, Colstrip would later attract a more limited number of potential bidders. PGE feared that the only interested party in the future would be the EWG. Thus the timing of the auction was key.

PGE also argues that the Commission should take into account several negative characteristics of the plant. Colstrip is a large resource with minimum output below which it cannot operate efficiently. That is, the plant has a must-run aspect. The nearby hydro-dominated market complicates matters because water can displace thermal units. Colstrip is also located in a remote area. Any significant change in transmission rates or rate design could result in major harm to the plant's economics, and the value of the plant's real estate is low because of its location. This weak value of the underlying site is in contrast to plants that have recently sold in New England, New York, and Southern California.

Another characteristic of Colstrip is the fact that it burns coal. The coal it burns is relatively clean, but the plant remains vulnerable to global concerns about carbon dioxide emissions and possible further tightening of the Clean Air Act in this country. Eventual decommissioning may present environmental issues not currently anticipated. PGE has negotiated a favorable cap on total environmental remediation liability as part of the sale.

PGE's Exhibit 301, Hager, is meant to show that if all commercial and industrial customers leave the system, PGE can continue to serve its native load without Colstrip. (PGE notes that after October 1, 2001, it will not have "native load customers." Instead, it will have customers obligated to buy from PGE and customers not obligated to buy from PGE. PGE assumes it would not supply those two groups in the same way.) If PGE sells Colstrip, residential customers will not be saddled with the costs from Colstrip. Even if Staff's load assumptions are correct, the wholesale market is vibrant and PGE argues that it can easily meet its load obligations as it currently does, with a combination of generation and wholesale power purchases.

Staff's Adjustments. PGE contends that much of Staff's methodology is flawed. Furthermore, PGE notes that it does not agree with any of Staff's proposed adjustments and that if any of the adjustments are adopted by the Commission, PGE will not go forward with the sale.

PGE enumerates several disagreements with Staff's methodology in evaluating the proposed sale. First, PGE maintains that Staff did not employ the correct methodology to decide whether the plant should be sold. According to PGE, Staff valued its forecasts for 26 years into the future as highly as its forecasts for tomorrow. PGE contends that forecasts of the near future are more likely to be accurate than those pertaining to the distant future. According to PGE, Staff's figure of a $71.3 million loss to ratepayers is simply a projection. Yet Staff's projections show that the sale of Colstrip does not become negative for customers until well into the second decade of the twenty-first century. PGE argues that the Commission should also recognize that Staff is not weighing its forecast against another uncertain forecast. Here the comparison is between a forecast and Global's firm offer.

PGE's emphasis on the near future is also based on the belief that customers have a short payback expectation. Staff recommends disapproval of the proposed sale on the basis that the next generation of customers and beyond will be better off if the Commission disapproves the sale. PGE contends that the choice is between a certain benefit now and possible detriments later.

According to PGE, the only sensitivity analysis Staff ran from its base case was for electricity natural and gas prices. PGE points out that the problems with relying on such analyses are: (1) different scenarios are not meaningful unless some probabilities are assigned to them (Staff did not); and (2) the analyses do not give a complete picture of potential reactions to changes in circumstances and do not take into account the feedback effect. PGE contends that the Commission should consider how likely it is that the world will be different from the base forecast, and in what direction. PGE argues that if Staff is wrong, its customers could suffer in the long run. PGE believes that a major flaw in all of Staff's analysis is that it is more likely to be wrong on the down side, the side that will harm consumers.

According to PGE, Staff wrongly states that PGE's approach to this case ignores ratepayer interests. PGE contends that the fair market value standard does not ignore the interests of ratepayers. On the contrary, it minimizes stranded costs and takes advantage of the market situation to obtain the best price a utility is likely to receive for its assets. The most striking fact that Staff ignores is the immediate rate reduction PGE is offering. PGE proposes to flow the benefits of the sale through to ratepayers. According to PGE, Staff's position denies current ratepayers the benefits of the sale by relying on its forecast of conditions to 2020 and beyond.

PGE also takes issue with Staff's analysis because it contains no carbon dioxide tax analysis. That is, PGE argues that Staff failed to consider the possibility of future significant environmental legislation affecting coal fired plants.

PGE further maintains that Staff's quantification of the capacity factor for the plant is problematic. The plant's actual history yields an average availability factor of 82 percent, lower than the national average. PGE believes that the national average is more appropriate, so it used an 84 percent AAF. Staff, on the other hand, used selected historic figures; Staff omits the four worst years of plant's performance and uses the four best, and its three-year average includes the two best years.

Staff's position on the life of coal plants raises similar concerns for PGE. Staff expects Colstrip to last between 70 and 100 years. Staff proposed no capital improvements to extend Colstrip's life beyond PGE's assumptions. PGE asked Staff for data on the specific plants that it relied upon to reach its conclusions. According to PGE, Staff has no knowledge of such basic data as estimated remaining lives, availability factors, history of capital expenditures, and outage history of those plants. PGE does not understand how Staff can take a position on the life of Colstrip without relevant background data. PGE urges the Commission to ignore testimony that cannot be supported.

Revenue Requirement Issues. PGE has three rate issues with Staff. First, PGE is concerned with Staff's approach to PGE's tracker filing. Staff proposes to track in a different level of power (258 average megawatts) than it tracks out (262 average megawatts). PGE proposes to track the same amount of power (262 average megawatts) in and out. PGE points out that the purpose of a tracker filing is to adjust a single aspect of a company's base rate without having to reexamine all elements of the rates. Staff's proposal to track in a different level of power than is tracked out upsets this balance.

Second, PGE expresses concern about the cost of replacement power. When Staff filed its testimony, PGE had not reached agreement with Global over purchase of power. Staff therefore used the average price forecast. PGE has entered into a contract for replacement power and proposes to use actual contract price rather than a proxy. Staff has since agreed to use the contract price, so this is no longer an issue.

Third, in terms of overall transition cost recovery, Staff and PGE do not disagree. The disagreement on this issue relates to rate of return on costs. PGE has proposed that its authorized overall rate of return apply to transition costs. Staff has proposed that the Commission set a rate of return when PGE applies to establish a balancing account for transition costs, and then recommends that the rate of return be lower than PGE's authorized cost of capital if the Commission sets a five-year amortization period. PGE disagrees with Staff for four reasons. First, a reduction in the interest rate for the transition cost deferred account penalizes PGE for attempting to implement SB 1149. Second, the interest rate for deferred amounts should be the same whether paid to PGE or its customers. Third, the Commission has never ruled that a utility's cost of capital should be lowered for ratemaking purposes to reflect decreased risk for short recovery periods. PGE submits that the risk of nonrecovery of transition costs may be higher than other utility costs. Finally, the amount customers pay for transition costs can be reduced by securitizing those costs rather than by unfairly reducing PGE's authorized rate of return.

In summary, PGE argues that Staff's analysis focuses on a faulty cost benefit analysis. PGE asserts that Staff's methodology is flawed, and Staff's approach is inconsistent with rulings of the Commission that the public interest standard is broader than the economic test.

Determining Fair Market Value. PGE notes that the Commission has recognized that price is a key determinant in property transfer cases. If price is the higher of market or book value, the Commission has approved sales in the past. The price in this case exceeds book value; PGE has shown by several different methodologies that the sale price is at market or better. PGE contends that to meet Staff's sale price plus adjustments, a bid of $267.6 million, or $904 per kW, would have been necessary, far higher than the top price of $667 per kW in Merrill Lynch's analysis. Merrill Lynch found the average price for fossil fuel plants to be $303 per kW, less than half the bid for Colstrip ($652 per kW).

Furthermore, because Colstrip was part of a major asset auction, PGE argues that the price represents fair market value. PGE maintains that the auction was conducted appropriately. Staff alleged various flaws but no specific instances of actual harm were cited.

Other Policy Issues: BPA. PGE argues that the sale of Colstrip does not change PGE's net requirements because Colstrip was never included in PGE's firm resource exhibit. PGE also notes that even assuming adverse treatment by BPA on all resources, PGE has 844 average megawatts (aMW) of net requirements as calculated by BPA. PGE argues that this is a theoretical issue only. Furthermore, PGE argues that Colstrip is not necessary for it to serve residential load.

Other Policy Issues: Penalty Provisions. The sale is structured in such a way that if PGE's sale is approved, MPC will receive an additional $35 million and PSE will receive an additional $20 million. PGE points out that PSE and MPC will both suffer penalties (that is, they will not receive the extra monies) if PGE does not close. PGE's contract does not include a penalty provision. Staff suggests that PGE should receive some of the $55 million owed to PSE and MPC, because if PGE closes, PSE and MPC will avoid their penalty deductions. PGE argues that Staff's position is baseless. Staff's proposed adjustment is based on the conclusion that PGE's share has intrinsic value greater than that of PSE and MPC.

ICNU's Position. ICNU believes the Commission should approve PGE's proposed sale of Colstrip. ICNU contends that the Commission should not second guess the market; the auction, ICNU argues, represents a fair market evaluation of the long term costs of Colstrip compared to its long term value.

ICNU maintains that the amount of gain and the treatment of the gain should be addressed in PGE's next rate case.

Finally, ICNU contends that PGE's application should be considered in the context of SB 1149. The bill does not require divestiture, but its preamble states that divestiture is the most effective means of stimulating competition. SB 1149 also requires the Commission to adopt policies “to eliminate barriers to the development of a competitive retail market structure.” SB 1149, section 6(1). ICNU takes the position that the Commission should take steps to encourage divestiture through incentives. Staff appears to assume that a utility must retain its resources and continue to plan to serve customers at a cost of service rate that is the same as the service it provides today. ICNU opposes this assumption. ICNU argues, in sum, that the market rather than integrated utilities will supply generation for many customers, and the question before the Commission is whether to allow PGE to take advantage of the opportunity to sell presented by the option of MPC restructuring.

ICNU points out disadvantages to the Commission’s second-guessing the market. Buyers will be discouraged from participating in future auctions of assets owned by Oregon utilities. Second, utilities will be discouraged from divesting generating assets. Both outcomes could chill the creation of a competitive retail market and implementation of SB 1149. Finally, PGE's potential stranded costs could increase if the market value of PGE's share of Colstrip proves to be lower in the future. As a result, the Commission’s decision could result in higher rates in the long term. ICNU believes PGE's sale of Colstrip is a reasonable attempt by PGE to take advantage of unique circumstances and mitigate stranded costs.

Discussion. ***General Overview.*** The parties raise three sets of interrelated issues: 1) whether the Commission should focus on short term benefits to ratepayers from the sale or on the possible long term effects of selling Colstrip; 2) the accuracy of Staff’s adjustments to PGE's base case; and 3) policy questions that arise only if the Commission approves the sale, such as BPA’s treatment of the sale and revenue requirement consequences of the sale. Because we do not approve the proposed sale, this order does not discuss the third set of issues. The first and second sets of issues are involved in the determination of how to apply the no harm standard that we have adopted for this case.

Staff’s analysis examines the effect of the Colstrip sale on PGE's customers over the remaining life of the plant. It is true, as PGE argues, that Staff’s analysis is based on projections. However, it is not true that Staff’s analysis fails to weight the trends it projects. Staff uses a weighted net present value analysis as its tool in evaluating the Colstrip sale.

It is also true, as PGE contends, that Staff’s case deals in uncertainties because it deals in projections. However, we are not persuaded that all projections are equally uncertain. Even without evaluating specifically each dollar claim the parties make to substantiate their cases, we can judge whether selling Colstrip meets the no harm to ratepayers standard of review.

Part of PGE's case is based on projections about the need for Colstrip. PGE assumes that it will not need Colstrip power to serve its loads or that if it does have unmeet need, it can purchase replacement power at no detriment to ratepayers. Staff's assumptions in that context are more conservative and more reasonable than PGE's. The likelihood is that Colstrip will be needed in the future. Replacement power markets are volatile. Colstrip has relatively low operating costs. Given these conservative assumptions, it is clear that the sale of Colstrip exposes PGE's ratepayers to the risk of increased cost.

We understand PGE's contention that the sale of the plant presents ratepayers with a benefit in the near term. However, this is an emerging market in an industry moving from regulation to competition. Our task is to prevent harm to ratepayers as that transition takes place. We conclude that, in view of the many uncertainties in the market and the questions that Staff has raised about the sale, we can best adhere to the no harm standard by focusing on the long term and disapproving the sale.

SB 1149, as ICNU and PGE point out, looks favorably on divestiture of utility generation assets. We do not mean this case to prejudge our decisions in other cases or in implementation of SB 1149 in general.

Staff's analysis shows that over the expected life of Colstrip, the sale would cause power related costs (and therefore rates) to be over $70 million higher than they would be without the sale. PGE's own analysis, corrected for two obvious errors (there will be no rate decrease in 1999 as a result of the sale, and customers do have to pay stranded costs), also shows that costs would be over $43 million higher than without the sale. Again, both figures support a finding that PGE cannot show no harm to ratepayers from the sale.

Specific Issues: Sensitivity Analysis. PGE criticizes Staff's sensitivity analysis. We are not convinced by PGE's argument. Sensitivity analysis is a tool to determine how an estimation method like cost/benefit analysis reacts to a range of alternative assumptions without regard to their appropriateness. Staff conducted such an analysis to consider alternative assumptions, assessing the robustness of the analysis and the change in results due to a variation in assumptions.

Staff used different scenarios involving high/low gas prices, immediate high/immediate low gas prices, and high/low electric prices. Staff's sensitivity analysis shows that only two of the six scenarios result in customers not being harmed through the sale of Colstrip: immediate low gas prices and low natural gas prices. We give little weight to the immediate low price scenario because such is not the case today. In UG 136, UG 137, and UG 138, we have dockets involving natural gas trackers from all three Oregon regulated utilities that raise rates due in part to increases in the cost of purchasing natural gas.[4]

[4] Staff asks the Commission to take official notice of these tracker dockets pursuant to OAR 860-014-0050(1)(e). That request is granted.

That leaves one scenario, the low natural gas price scenario, that shows a downside risk of denying the sale. Under that scenario, the foregone benefit is roughly $4 million.[5] Staff argues, and we agree, that this benefit pales in comparison to Staff's base case, which projects a detriment of approximately $70 million, and to the results of the other scenarios in Staff's sensitivity analysis, which show possible detriments from $23.5 million to $175 million.

Specific Issues: Colstrip's Relative [Dis]Advantage. PGE raises a number of issues with respect to Colstrip that do not directly address the numbers in Staff's adjustments to its base case but which could be seen as supporting a decision to sell Colstrip. For instance, PGE notes that Colstrip is a large, remote, and relatively inflexible generating resource and that the nearby abundant hydro market can displace thermal units from Colstrip. When we determined to include Colstrip in rate base, we viewed as a plus what PGE now argues is a drawback. In Order No. 87-1017, we found, at 7, what we still consider to be true:

> The plant can displace other generating plants which have higher variable costs. Colstrip 4's mine mouth location results in low operating costs. . . . Furthermore, the costs for purchased power may increase sharply because of adverse water conditions or large thermal outages. . . . The plant can allow greater flexibility in maintenance scheduling and energy dispatching.

Specific Issues: Qualitative Factors. PGE also argues generally, relying on our Trojan decision, that Staff's case is flawed because it fails to consider PGE's qualitative factors. Staff did consider these factors and determined that the contextual factors were not sufficient to overcome the loss to ratepayers if Commission approves the sale. When we distinguished between net benefits and the public interest in Order No. 93-1117, stating that a finding of public interest is potentially much more inclusive than the economic calculation that constitutes a determination of net benefits, we did not eliminate consideration of cost/benefit analysis in future cases.

Specific Issues: Need for Colstrip. We agree with Staff that Colstrip is needed to serve PGE's residential native load. PGE's assertion that it will be able to serve native load without Colstrip is based on unreasonable assumptions. PGE's analysis assumed 1998 loads, excluded all commercial and industrial customers, and assumed that PGE would receive 400 aMW of BPA power. The cost of service option provided in UE 102 and under SB 1149 does not preclude PGE from serving commercial and industrial customers, as PGE had assumed. Therefore, we find Staff's analysis on this issue more reasonable.

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[5] The source for the numbers in Staff's sensitivity analysis is Staff exhibit 100, Conway 25. The downside risk of denying the Colstrip sale application under the low natural gas prices scenario was estimated at $7.9 million in Staff testimony. Subsequent to PGE's signing a contract with Global, Staff used the replacement power contract price rather than market, thus lowering the downside risk to the $4 million figure used above.

Even assuming that PGE’s assumptions are correct, we have previously rejected the notion that resources and loads need to be in balance at any given point in time. For instance, in Order No. 87-034, at 8, we reasoned: “It is completely unreasonable to contend that at any given point in time, an electric utility’s generation resources must precisely match its customers’ loads and reserve obligations and that any generating capacity over that amount is excess capacity[.]”

Specific Issues: Fair Market Value. Additionally, we agree with Staff that the Colstrip sale price could represent fair market value and still harm ratepayers. That being said, we believe that Staff has raised serious questions about whether the price to be paid PGE represents fair market value. PGE contends that Staff’s imputed price of $904/kW for the Colstrip sale is far too high, citing comparable sales in the $650/kW range. PGE's own application, however, states that Edison Mission Energy purchased a coal fired generation plant for $955/kW on August 3, 1998. We note that Colstrip is an attractive coal resource. It is a low cost mine mouth generation plant with low sulfur and relatively high heat content coal. It is reasonable to assume that such a resource would be in the higher end of the sales price range. Moreover, we are concerned that as the auction is structured, the PGE sale would bring an additional $55 million to PSE and MPC. If this sum represents part of the value of PGE's Colstrip share, it should go to PGE and its ratepayers, not to other utilities.

Finally, we have concerns about the auction process. Colstrip has multiple owners, and various agendas are at work in this sale. The displaced $55 million in payments is one aspect of the auction that raises concerns. We share Staff’s concern that PSE and MPC may receive a windfall at the expense of PGE's customers, if PGE sells its share of Colstrip. Unfortunately, the only evidence in the record is the bundled prices Global pays to MPC and PSE for Colstrip 1, 2, 3, and 4, assuming PGE sells its share of Colstrip. There is no way for us to unravel those prices.

CONCLUSION AND RECOMMENDATIONS

We conclude that ratepayers would be harmed by the proposed Colstrip sale. The application should be denied.

We have discussed above our concerns regarding this specific asset sale proposal and our conclusion that PGE has not met its burden to demonstrate that the sale is consistent with the public interest. While we base our decision on these concerns, we note that it would be plausible for PGE to overcome our concerns by proposing one or more offsetting benefits. Therefore, we are willing to revisit our decision if PGE is able to identify and propose such added benefits. Conceptually, for PGE’s consideration in furthering this matter, added benefits might include, but are not limited to, the following:

1. A power purchase agreement or option that secures benefits for PGE’s customers that reasonably reflect continued ownership of the company’s share of the Colstrip facility.

2. Sharing with PGE's customers other benefits to mitigate the benefits lost through the sale of Colstrip, including benefits not associated with the sale.

3. Other items that would allow the Commission to determine that cost uncertainties have been addressed and statutory provisions met.

ORDER

IT IS ORDERED that the application of Portland General Electric Company to sell its ownership share of Colstrip is denied. The tariffs associated with this application, PGE's Advice 99-3, are permanently suspended.

Made, entered, and effective ________________________.

______________________________	______________________________
Ron Eachus Chairman	**Roger Hamilton** Commissioner
	______________________________
	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.

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