ATERWYNNE LLP
ATTORNEYS AT LAW

Suite 1800
222 S.W. Columbia
Portland, OR 97201-6618
503-226-1191
Fax 503-226-0079
www.aterwynne.com

September 2, 2005

VIA EMAIL AND US MAIL

Filing Center
Oregon Public Utility Commission
550 Capitol Street NE #215
PO Box 2148
Salem, OR 97308-2148

Re: UM 1129 – Idaho Power's Comments on the Commission's Authority to Order Tariffs Subject to Refund

Dear Sir or Madam:

Enclosed for filing in the above-referenced docket is Idaho Power Company's Comments on the Commission's Authority to Order Tariffs Subject to Refund. Please contact me with any questions.

Very truly yours,

Jessica A. Gorham

Enclosures

cc: UM 1129

CERTIFICATE OF SERVICE
UM 1129

I hereby certify that a true and correct copy of **IDAHO POWER'S COMMEN5TS ON THE COMMISSION'S AUTHORITY TO ORDER TARIFFS SUBJECT TO REFUND** was served via U.S. Mail on the following parties on September 2, 2005:

MICK BARANKO
DOUGLAS COUNTY FOREST PRODUCT
PO BOX 848
WINCHESTER OR 97495

R THOMAS BEACH
CROSSBORDER ENERGY
2560 NINTH ST, STE 316
BERKELEY CA 94710

LAURA BEANE
PACIFICORP
825 MULTNOMAH STE 800
PORTLAND OR 97232-2153

JACK BREEN
PUBLIC UTILITY COMMISSION
PO BOX 2148
SALEM OR 97308-2148

BRIAN COLE
SYMBIOTICS, LLC
PO BOX 1088
BAKER CITY OR 97814

BRUCE CRAIG
ASCENTERGY CORP
440 BENMAR DR STE 2230
HOUSTON TX 77060

CHRIS CROWLEY
COLUMBIA ENERGY PARTNERS
PO BOX 1000
LA CENTER WA 98629

DATA REQUEST RESPONSE CENTER
PACIFICORP
825 NE MULTNOMAH, SUITE 800
PORTLAND OR 97232

CAREL DE WINKEL
OREGON DEPARTMENT OF ENERGY
625 MARION STREET NE
SALEM OR 97301

CRAIG DEHART
MIDDLEFORK IRRIGATION DISTRICT
PO BOX 291
PARKDALE OR 97041

ELIZABETH DICKSON
HURLEY, LYNCH & RE, PC
747 SW MILL VIEW WAY
BEND OR 97702

JOHN M ERIKSSON
STOEL RIVES LLP
900 SW FIFTH AVENUE, SUITE 2600
PORTLAND OR 97204-1268

JAMES F FELL
STOEL RIVES LLP
900 SW 5TH AVE STE 2600
PORTLAND OR 97204-1268

THOMAS M GRIM
CABLE HUSTON BENEDICT ET AL
1001 SW FIFTH AVE STE 2000
PORTLAND OR 97204-1136

STEVEN C JOHNSON
CENTRAL OREGON IRRIGATION DISTRICT
2598 NORTH HIGHWAY 97
REDMOND OR 97756

` DOUG KUNS
PORTLAND GENERAL ELECTRIC
121 SW SALMON ST
1WTCO702
PORTLAND OR 97204

MONICA B MOEN
IDAHO POWER COMPANY
PO BOX 70
BOISE ID 83707-0070

JANET L PREWITT
DEPARTMENT OF JUSTICE
1162 COURT ST NE
SALEM OR 97301-4096

IRION SANGER
DAVISON VAN CLEVE
333 SW TAYLOR, STE 400
PORTLAND OR 97204

MARK TALLMAN
PACIFICORP
825 MULTNOMAH STE 800
PORTLAND OR 97232-2153

MICHAEL T WEIRICH
DEPARTMENT OF JUSTICE
REGULATED UTILITY & BUSINESS
SECTION
1162 COURT ST NE
SALEM OR 97301-4096

J RICHARD GEORGE
PORTLAND GENERAL ELECTRIC COMPANY
121 SW SALMON ST
PORTLAND OR 97204

DAVID HAWK
J R SIMPLOT COMPANY
PO BOX 27
BOISE ID 83707

BARTON L KLINE
IDAHO POWER COMPANY
PO BOX 70
BOISE ID 83707-0070

ALAN MEYER
WEYERHAEUSER COMPANY
698 12TH STREET, SUITE 220
SALEM OR 97301-4010

THOMAS H NELSON
THOMAS H NELSON & ASSOCIATES
825 NE MULTNOMAH STE 925
PORTLAND OR 97232

PETER J RICHARDSON
RICHARDSON & O'LEARY
PO BOX 7218
BOISE ID 83707

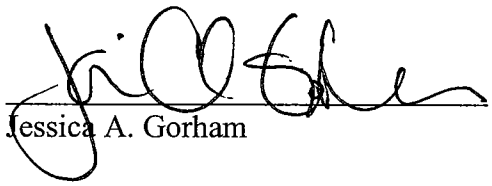
DONALD W SCHOENBECK
REGULATORY & COGENERATION
SERVICES INC
900 WASHINGTON ST STE 780
VANCOUVER WA 98660-3455

S BRADLEY VAN CLEVE
DAVISON VAN CLEVE PC
333 SW TAYLOR, STE 400
PORTLAND OR 97204

LINDA K WILLIAMS
KAFOURY & MCDOUGAL
10266 SW LANCASTER RD
PORTLAND OR 97219-6305

PAUL WOODIN
WESTERN WIND POWER
282 LARGENT LN
GOLDENDALE WA 98620

ATER WYNNE LLP



Jessica A. Gorham

BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

UM 1129 - PHASE II

In the Matter of PUBLIC UTILITY COMMISSION OF OREGON Staff's Investigation Relating to Electric Utility Purchases from Qualifying Facilities	IDAHO POWER COMPANY'S COMMENTS ON THE COMMISSION'S AUTHORITY TO ORDER TARIFFS SUBJECT TO REFUND

I. INTRODUCTION

On May 13, 2005, the Public Utility Commission of Oregon (the "Commission") issued its order adopting the avoided cost rates and standard contract forms for Qualifying Facilities ("QFs") under the Public Utility Regulatory Policies Act ("PURPA")[1] in the revised tariffs of Idaho Power Company ("Idaho Power"), Pacific Power & Light ("PacifiCorp"), and Portland General Electric ("PGE") (collectively, the "Companies"). However, because of remaining concerns over the propriety of the rates, the Commission tentatively ordered that the rates be adopted "subject to refund," and further ordered the Companies to include provisions in their standard contracts acknowledging the possible refund. In issuing its order, the Commission specifically acknowledged that there remains a question as to its authority to approve the rates subject to refund.

In fact, the Commission has no authority to adopt the avoided cost rates subject to refund, or to order language allowing a possible refund in the Companies' standard contracts. The mandated language and the proposed refund fatally conflict with PURPA and are inconsistent with state law. Accordingly, Idaho Power asks the Commission to reconsider its tentative decision to adopt the Companies' avoided cost rates subject to refund.

[1] 16 U.S.C. § 824a-3.

II. BACKGROUND

In Docket UM 1129, the Commission investigated electric utility purchases from QFs under PURPA—evaluating specific policies and procedures in order to determine whether the Commission's goals relating to PURPA could be more effectively implemented. Based on this investigation, the Commission issued Order No. 05-584 (the "Order") on May 13, 2005. In the Order, the Commission directed the Companies to file standard contract forms and revised tariffs to implement the Commission's decision. The Order provides that the tariffs will be effective thirty days from the filing date, unless suspended by the Commission. After consultation with the Commission Staff ("Staff"), the Companies made their compliance filings on July 12, 2005, and the matter was set to come before the Commission at its August 2, 2005 Public Meeting.

In its July 25, 2005 report ("Staff Report"), Staff issued its recommendations regarding the Companies' compliance filings. Staff stated that it believed that the Companies' filings "generally implement the Commission decision" but noted that there remained "continued issues" as to two specific issues and "widespread interest of other parties in these issues."[2] For these reasons, Staff recommended that the Commission conduct hearings regarding the tariff filings. However, Staff also noted that the parties generally agreed that the proposed tariffs and standard contracts were "far superior" to the existing rates and practices, and, for this reason, did not recommend "a suspension that would require the parties that have sought the relief fostered by UM 1129 to continue to wait to avail themselves of the changes until the completion of the investigations."[3] Accordingly, Staff recommended that the avoided cost rates contained in the proposed tariffs be adopted "subject to possible refund" under ORS 757.215.[4] Staff explained the contemplated refund as follows:

> For the current filings, if the Commission orders higher avoided cost rates at the end of the investigation, then QF would be paid the additional amount (with

[2] *Staff Report*, Appendix A to Order No. 05-899, p. 2.

[3] *Id.*, p. 3.

[4] *Id.*, p. 4.

> interest at the utility's authorized rate of return). In the case of a lower avoided cost rate, the QF would not be required to return amounts to the company.[5]

In addition, Staff recommended that the Commission direct the utilities to include a provision in the standard contracts acknowledging that the rates contained in the agreement were subject to refund, as follows:

> The seller and Idaho Power Company, Pacific Power & Light, and Portland General Electric Company acknowledge that the rates, terms and conditions specified in this agreement and the related tariffs are being investigated by the Oregon Public Utility Commission. Upon a decision by the Oregon Public Utility Commission in the investigation, the Idaho Power Company Pacific Power & Light, and Portland General Electric Company will notify the seller within ten calendar days. If the rates resulting from the investigation are higher than the rates in effect during the initial period, the Idaho Power Company, Pacific Power & Light, and Portland General Electric Company will refund, with interest, the difference to the seller. The seller shall have thirty calendar days from the effective date of the revised standard contract and tariffs complying with the Commission's order to amend this agreement if the seller so chooses to adopt the revised standard contract and/or the revised rates, terms, and conditions in the tariff approved by the Oregon Public Utility Commission as a result of the investigation.[6]

At the August 2, 2005 Public Meeting, the Commission adopted Staff's recommendations, allowing the filing to go into effect subject to possible refund, and ordering the Companies to include in their standard contracts the proposed contract language regarding a possible refund.[7] However, the Commission specifically noted the parties' questions as to whether the filings could properly be ordered into effect subject to refund, and ordered that the issue be separately addressed at the outset of the investigation.[8]

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[5] *Id.*, p. 2.

[6] *Id...*

[7] The Commission did order a slight modification to the contract language. Order No. 05-899, p. 2.

[8] *Id.*

III. DISCUSSION

A. PURPA AND FERC REGULATIONS PRECLUDE THE COMMISSION'S CONDITIONAL APPROVAL SUBJECT TO REFUND

In 1978, Congress enacted PURPA as part of a package of legislation to combat the nationwide energy crisis resulting from skyrocketing oil prices in the early 1970s, and the shortage of natural gas in 1977.[9] Section 210(a) of PURPA directs the Federal Energy Regulatory Commission ("FERC") to promulgate rules to encourage the development of alternative sources of power, including rules requiring utilities to offer to buy electricity from qualifying cogeneration and small power production facilities—QFs.[10] In so doing, PURPA specifically directs FERC "and not the states, to prescribe rules governing QF rates."[11] In accordance with its mandate, FERC prescribed the rules for setting QF rates and directed the states to implement these rules.[12] Significantly, there is nothing in PURPA or the FERC regulations that allow a state commission to condition approvals or otherwise revisit rates once they are adopted. On the contrary, when presented with this question, the courts have found that such conditional rate approvals are prohibited.

For example, in *Smith Cogeneration Management, Inc. v. Corp. Comm'n*,[13] the Appellant, Smith, challenged a rule of the Oklahoma Corporation Commission (the "Corporation Commission") requiring utilities to include in each QF contract a provision stating "that the Commission may, after proper notice and hearing, change the terms and otherwise finalize experimental purchase tariffs and special contracts."[14] This rule served to allow the Corporation Commission to alter the terms of QF contracts days, months or years after the parties had entered

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[9] *Federal Energy Regulatory Commission v. Mississippi*, 456 U.S. 742, 102 S.Ct. 2126 (1982).

[10] *Id.*

[11] *Connecticut Light & Power Co.*, 70 FERC ¶ 61,012, 61,027 (1995) (citing 16 USC § 824a-3(a)-(b)).

[12] *See* 16 USC § 824a-3(f).

[13] 863 P.2d 1227, (Ok. 1993).

[14] *Id*. at 1230, fn3.

into the agreements.[15] Smith argued that the rule directly conflicted with PURPA regulations and was therefore preempted. The Appellee utility defended the rule, arguing that it was required under state and federal law – specifically pointing to the state law that required the Corporation Commission to conduct a detailed rate investigation every five years.[16]

The Oklahoma Supreme Court found the rule preempted. Specifically, the court held that "[r]equiring QFs and electric utilities to include a notice provision allowing reconsideration of established avoided costs conflicts with PURPA and FERC regulations."[17] In the court's view, allowing reconsideration would impose, contrary to Congress's intent, "traditional utility-type ratemaking concepts on sales by qualifying facilities to utilities."[18] The court noted that under the controlling law, the Corporation Commission "is required to set avoided costs for the duration of the proposed contract—even if the avoided costs are estimated."[19] And, after the Commission estimates these costs, nothing in "the FERC regulations authorize[] or encourage[] a recalculation of estimated avoided costs."[20]

The Oregon Court of Appeals recently followed the opinion in *Smith*[21] in determining that the Oregon Public Utility Commissioner possesses "no post-approval authority to modify

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[15] *Id.*

[16] *Id.* at 1237-1238.

[17] *Id*. at 1241.

[18] *Id*.

[19] *Id.*

[20] *Id*. at 1238.

[21] Indeed, courts nationwide have followed the *Smith* opinion. For example, in *Freehold Cogeneration Associates, l.P. v. Board of Regulatory Commissioners*, the Third Circuit Court of Appeals held that PURPA prevented the relevant New Jersey commission from modifying terms of approved contracts between QFs and utilities. The Third Circuit held that after the commission approved "the power purchase agreement . . . on the ground that the rates were consistent with avoided cost, any action or order by the [commission] to reconsider its approval or to deny the passage of those rates to [the utility's] consumers under purported state authority was preempted by federal law." 44 F.3d 1178, 1194. Also, in *Agrilectric Power Partners, Ltd. v. Entergy Gulf States, Inc.*, the Fifth Circuit cited *Smith* and *Freehold* with approval, but acknowledged a difference when the parties voluntarily contracted around restrictions. 207 F.3d 301, 303 (2000). Specifically, when the utility and QF deliberately and voluntarily made the price variable through a "regulatory-out" price adjustment clause, the court allowed these agreed-upon changes. *Id*. At 304, fn5. The Fifth Circuit juxtaposed this situation with the "direct and invasive regulatory control" exercised in *Smith* and *Freehold*. *Id*.

prices" in a utility-QF contract.[22] In *Oregon Trail*, the utility and the QF had mutually agreed to contractual language providing that the contract prices were "subject to modification, to the extent the Oregon Public Utility Commissioner, or his successor, may modify the agreed payments upon a finding that such payments are contrary to public policy."[23] The court determined that the parties included this provision early in PURPA's history, gambling on how PURPA would be interpreted--the utility believing that PURPA would be interpreted to authorize state regulators to modify prices in existing contracts and the QF believing the opposite and expecting that the language would be ineffective under PURPA.[24] The utility guessed wrong; the Court of Appeals found as follows: "it is well-settled that . . . PURPA precludes a regulator's exercise of post-contractual, utility-type price modification authority."[25]

Instead of conditioning or deferring approval, the state possesses an "absolute duty" to definitively determine rates at the outset.[26] This determination provides the certainty necessary for both the utility and the QF.[27] In fact, FERC has repeatedly highlighted the need for certainty in QF rates.[28] In refusing to revisit estimations of avoided cost, FERC noted that, in the long run, "'overestimations' and 'underestimations' will balance out."[29]

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[22] *See Oregon Trail Electric Consumers Cooperative, Inc. v. Co-Gen Co.*, 168 Or.App. 466, 482 (2000).

[23] *Id*. at 469.

[24] *Id.* at 480.

[25] Oregon Trail Electric Consumers Cooperative also argued that the contract language discussed above provided the Commissioner with independent, contractual authority to modify the price. *Id.* at 483. Co-Gen argued that PURPA precludes flexible contract pricing and requires that the costs be definitively "*calculated at the time the obligation is incurred*." *Id.* (citations omitted). The court did not address this issue because it relied upon a rejected interpretation of contract law. *Id.*

[26] *See GPU Industrial Intervenors v. Pennsylvania Public Utility Comm'n*, 156 Pa. Cmwlth. 626, 635-6 (1993) (holding that without this factual determination on the record, the state commission "cannot fulfill its duty under PURPA and the federal and state regulations implementing it. . .").

[27] FERC has also specifically acknowledged that this policy preference for certainty may benefit the utility.

[28] *See, e.g. Consumers Energy Co.*, 89 FERC ¶ 61,138, 61,397 (1999) (identifying the general reluctance to impose rate changes retroactively).

[29] *New York State Electric & Gas Companies*, 71 FERC ¶ 61,027, 1995 WL 216781, *15.

[31] 70 FERC at 61,030.

Additionally, even if the Commission *could* legally make retroactive adjustments to the avoided cost rates after they had been incorporated into contracts, the asymmetric nature of the Commission's proposed "refund" violates federal law. In *Connecticut Light & Power*, FERC stated that if state law or policy requires the parties to enter into contracts "that are in excess of avoided cost, those contracts will be considered to be void ab initio."[31] Yet the Commission's proposed mechanism contemplates that if the Commission were to find that the rates at issue were above avoided cost, the contract at issue would remain in force. Specifically, it must be noted that in proposing its "refund mechanism", the Commission has stated that it will order "refunds" the QFs should its investigation determine that the rates paid to the QFs were too low. However, should the Commission determine that the rates paid by the utilities to the QFs were above avoided cost, no refund to the utility would be ordered. Therefore, even assuming that PURPA authorized the Commission to retroactively modify prices after approval, this asymmetrical mechanism would be impermissible.

In short, PURPA and FERC regulations require the Commission to adopt rates for QFs set at the avoided cost and preclude the Commission from retroactively modifying the rates contained in signed contracts between the utilities and QFs. In issuing an order of tentative approval and requiring contractual language contemplating a subsequent. asymmetrical recalculation, the Commission engaged in preempted activities that subject the QF contracts to utility-type rate regulation.

B. THE COMMISSION'S ORDER EXCEEDS ITS OWN STATUTORY AUTHORITY

Even ignoring PURPA, FERC regulations, and relevant case law, and assuming that the tentative order is not preempted, the Commission lacks the authority to approve QF rates subject to refund as a matter of state law. In adopting the Companies' tariffs and standard contracts, the Commission states that they are subject to refund pursuant to ORS 757.215(4). However, that statute—on its face—is inapplicable to QF transactions under PURPA. ORS 757.215(4) allows the Commission to adopt tariffs for services provided by utilities to its customers, subject to a

refund by the utility if the Commission later determines that the rates paid by the utility customers parties were too high. The statute – which implements classic utility-type rate regulation--cannot be said to apply to the situation contemplated by the Commission here, where it adopts rates pursuant to delegated authority under PURPA, and later determines that the utility should have paid more to a third party.

Indeed, the statutes implementing the Commission's delegated authority under PURPA are not found in Chapter 767, but rather in Chapter 758, at ORS 758.505 through 758.555. Consistent with the controlling FERC rules, the Oregon statutes do not allow for conditional approvals or subsequent rate modification. ORS 758.525(1) simply requires the Commission to "review[] and approve[]" the prices. The Commission's proposal to retroactively modify the approved prices, and to order additional payments including interest, impermissibly exceeds this statutory authority.[32]

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[32] *See Planned Parenthood Ass'n, Inc. v. Dep't of Human Resources*, 297 Or. 562, 565 (1984) (holding that state agency or commission acting under delegated authority must undertake actions through the "procedures prescribed by statute or regulation").

IV. CONCLUSION

Considering the foregoing, Idaho Power asks that the Commission reconsider the legality and propriety of approving the rates subject to a possible refund.

Dated this 2nd day of September, 2005.

ATER WYNNE, LLP

By: /s/ Lisa F. Rackner

Lisa F. Rackner
E-mail: lfr@aterwynne.com
Nathan A. Karman
E-mail: nak@aterwynne.com
222 SW Columbia, Suite 1800
Portland, OR 97201
Telephone: (503) 226-8693
FAX: (503) 226-0079

IDAHO POWER COMPANY

By: Barton L. Kline, ISB #1526
Senior Attorney
P.O. Box 70
Boise, Idaho 83707
E-mail: bkline@idahopower.com

Attorneys for Idaho Power Company