

**BEFORE THE PUBLIC UTILITY COMMISSION  
OF OREGON**

**DR 10, UE 88, UM 989**

In the Matters of

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

**OPENING MEMORANDUM OF  
PORTLAND GENERAL ELECTRIC  
COMPANY REGARDING PHASE I  
SCOPE**

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

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

**I. INTRODUCTION**

The courts have concluded that the final orders in dockets DR 10, UE 88 and UM 989 included legal errors. Therefore, the matters are remanded to the Public Utility Commission ("Commission") for further proceedings. The remand orders and the Commission's duty to set just and reasonable rates for Portland General Electric Company ("PGE") determine the scope of this consolidated proceeding. The inquiry is not ministerial.

**II. THE REMAND ORDERS**

The two remand orders differ. The remand by the Court of Appeals in DR 10 and UE 88 requires the Commission to hold "further proceedings" to implement the judgment of the Court of Appeals. The remand by the Circuit Court is more specific. The orders should therefore be analyzed separately.

**A. THE REMAND ORDERS IN DR 10 AND UE 88**

These remand orders do not require the Commission to order any refund or rate reductions. Historically, the Commission has taken the position that it does not have the

power to order refunds or rate reductions for past errors, except in those situations where a statute so allows. Nothing in the opinion of the Court of Appeals contradicts the Commission's historic position. It is at least arguable that the opinion does not permit any such refunds or rate reductions.<sup>1</sup>

If the remand in UE 88 does not permit or require a refund, what further proceedings does that remand contemplate? We contend that it would require the Commission to set rates prospectively by a process free of the error identified by the Court of Appeals. As it turned out, by the time the remand came down, the Commission had already done so. The Commission argued these points to the Circuit Court in defense of URP's appeal from the order in UM 989. Although the Circuit Court rejected these points in its decision in UM 989, the Commission has appealed that decision to the Court of Appeals. The Court of Appeals may yet confirm the Commission's position. In any event, the remand in DR 10 and UE 88 do not contradict the Commission's position.

**B. THE REMAND ORDER IN UM 989**

This remand order is more specific, Judge Lipscomb's remand of the final order in UM 989 requires the Commission to exercise its discretion to determine just and

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<sup>1</sup> This is true for two reasons. First, in the appeals from UE 88, there was no challenge to the Commission's finding that the rates it put into effect were just and reasonable. Neither the Circuit Court nor the Court of Appeals held that the rates were unjust or unreasonable. The Commission's conclusion in UE 88 that the rates were just and reasonable has not been overturned and should therefore be regarded as final. Although the Court of Appeals identified an error in the Commission's process, that does not mean the result of that process is necessarily overturned. The Commission and the courts sometimes make errors along the way in a proceeding, yet the final order of the Commission or the final judgment of a court may still be valid.

Second, the question whether there should be a refund as a result of legal error was raised in UE 88. The complaint filed by the Utility Reform Project in the Circuit Court demanded that the court order a refund. The Circuit Court did not do so, and neither did the Court of Appeals. Since URP has already asked the courts to order that relief, and since the courts declined to do so, the principle of issue preclusion, formerly known as *res judicata*, prevents that issue from being raised again.

reasonable rates. The Circuit Court's opinion concluded that the Commission had authority to identify past legal errors and issue refunds to "fix" any excess charges.<sup>2</sup>

Judge Lipscomb recognized that the scope of these remanded proceedings would not be a ministerial calculation of the return on the Trojan investment. Judge Lipscomb said:

"\* \* \* [A]t the Commission you [PGE] can argue \* \* \*, if you can't give us that [a return on the Trojan investment], you have to give us something else, because otherwise we aren't made whole \* \* \* And that's probably what you're going to do. \* \* \* And that may or may not result in any net rate relief \* \* \*." July 23, 2003 Hearing, Tr. at 177.

Judge Lipscomb also stated:

"I'm not prepared to buy off on that today, but I'm certainly not prepared to conclude that you can't argue on remand to the PUC that if you can't get a return on your investment, they need to put something else in your [rate] base for some other reason that \* \* \* allows you to have \* \* \* a rate of return that's economically viable for you to continue on as a successful utility company." July 23, 2003 Hearing, Tr. at 179.

### **C. THE COMMISSION'S RESPONSE TO THE REMAND ORDERS**

The Commission has consistently held that it lacks statutory authority to order refunds as URP seeks here. *See, e.g.*, UM 989, Order No. 02-227; UCB 13, Order No. 03-629. Accordingly, there is no Commission precedent directly on point. Nevertheless, it is clear from the court orders that the Commission now must exercise its broad ratemaking authority and discretion to determine just and reasonable rates.

The court decisions do not tell the Commission what the refund should be. Nor do they tell the Commission how to calculate a refund. They do not tell the Commission

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<sup>2</sup> The OPUC, PGE and URP have appealed the Final Judgment entered by Judge Lipscomb in 02C114884 on January 28, 2004 to the Oregon Court of Appeals. The parties in this docket reserve the right to pursue the appeal of the Final Judgment.

what ratemaking principles to use. They do not say what rates would be just and reasonable or what rate level would be unjust and unreasonable.

Indeed, the Court of Appeals decision did not find that rates were unjust and unreasonable at all. It simply concluded that ORS 757.355 "precludes the PUC from allowing rates \* \* \* that include a rate of return on" the Trojan investment balance. *Id.* at 714. It did not mandate a particular ratemaking methodology on remand. Like the Marion County Circuit Court, the Court of Appeals left the central ratemaking question to the Commission's discretion in these "further proceedings."

This view is entirely consistent with the traditional allocation of responsibilities between the Commission and the courts. The Commission has broad discretion when acting in its legislative rate-setting role, a principle the Oregon courts have embraced repeatedly: "rate-making is a purely legislative function, involving broad discretion in selecting policies and methods." *American Can Co. v. Lobdell*, 55 Or App 451, 463, 638 P2d 1152 (1982). The Commission "is not obliged to employ a single formula or combination of formulas to determine what are in each case just and reasonable." *Pacific Northwest Bell Telephone Co. v. Sabin*, 21 Or App 200, 224, 534 P2d 984 (1975). Indeed, the appellate provisions in the Oregon utility statutes specifically provide that the court may not substitute its judgment for that of the Commission on any finding of fact supported by substantial evidence. ORS 756.598(1).

The determination of just and reasonable rates cannot be accomplished through adjusting one specific cost item in the revenue requirement underlying the challenged rates as URP suggests. The Commission, Commission Staff and PGE have always recognized that the interpretation of ORS 757.355 would have far-reaching implications for the ratemaking decisions in UE 88.

In early 1993, PGE filed a request for declaratory ruling (Docket DR 10) that

sought an "early Commission expression of regulatory policy regarding the recovery of costs related to Trojan." *In re PGE* 1993 W L 221239, DR 10, Order No. 93-329 at \*1. PGE requested a declaratory ruling to "clarify the legal framework for a future rate proceeding." *In re PGE*, WL 374227, Order No. 93-1117 at \*8. The Commission stated that the ruling was important because it "establishes the rules within which a rate case will be conducted and the facts that must be proven for recovery to occur." Order No. 93-1117 at \*9. In adopting the Attorney General's opinion<sup>3</sup> that both a "return of" and "return on" the Trojan balance was within the Commission's authority, the Commission acknowledged that the "outcome [of the declaratory ruling proceeding] gives [PGE] information that will influence its behavior in a future rate case." *Id.* The Commission's decision in DR 10 adopting the Attorney General's opinion set the ground rules for the UE 88 rate case.

Determining just and reasonable rates in UE 88 under new ground rules will require the Commission to consider all aspects of the UE 88 order that would have been different. The bedrock nature of the DR 10 ruling and the Attorney General's opinion dictates that the Commission review several important issues directly affected by a change in the ground rules of UE 88. Similarly, the settlement approved by the Commission in UM 989 may need to be revisited in light of the new ground rules.

### **III. PRIOR COMMISSION DETERMINATIONS ARE AFFECTED BY THE COURTS' OPINIONS**

There are at least three separate determinations related to UE 88 rates that are affected by the Courts' Opinions. In response to the remand orders, the Commission needs to review first, the appropriate recovery period for the Trojan investment balance, second, the cost of capital effects of the utility's change of circumstances, and third, the application of the net benefits formula given that PGE is precluded from recovering the cost of capital

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<sup>3</sup> OP-6454.

represented by the Trojan investment balance. Other related issues may arise during the course of these proceedings.

**A. AMORTIZATION PERIOD**

The Commission has authority to determine and allow for depreciation of public utility property. ORS 757.140. Historically, the Commission ordered PGE to depreciate its investment in Trojan over a useful life assumed to end in 2011. In UE 88, the Commission allowed PGE to recover its undepreciated investment in Trojan over the remaining 17 year period, as well as a return on the undepreciated investment. Absent a return on PGE's investment in Trojan, the 17-year amortization period used in UE 88 means that PGE will not be made whole. An investment paid back tomorrow is far more valuable than the same sum paid back in equal parts over the next 17 years. In order to recover its full investment in Trojan without earning a return on Trojan, PGE would need to recover the entire balance immediately. There is nothing in ORS 757.140 that requires the Commission to delay recovery of an investment over a number of years, particularly when the useful life of the asset has ended. Thus, the Commission could set rates that provide for a much quicker amortization of the investment.<sup>4</sup>

In considering UE 88 rates, the Commission did not want to put PGE in a worse financial position than it would have been in if it had continued to operate Trojan. There is good reason for that view. It is the only way to encourage prudent management and responsible least cost planning. Absent a return on its investment, the determination in UE 88 to use a 17-year amortization period is not reasonable. It puts PGE in a significantly worse financial position than it would have been in if it had kept Trojan open. Accordingly,

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<sup>4</sup> The Court of Appeals recognized that the appropriate amortization period might be at issue if PGE were not allowed to recover a return on its undepreciated investment. The Court explicitly declined to address the question. *See* 154 Or App 702, 713 n.5, 962 P2d 744 (1998).

the Commission should revisit the question and determine the appropriate recovery period for PGE's Trojan investment balance.

The Commission has previously recognized that a change in the ground rules for UE 88 would require reconsideration of all affected ratemaking decisions in the docket. In Order No. 02-227, the Commission rejected URP's argument against the 2000 Trojan settlement in part because the Commission concluded that it lacked the statutory authority to order refunds. The Commission said that even if it did have such legal authority, it doubted whether "refunds and a reduction in the Trojan investment balance are in the public interest." UM 989, Order No. 02-227 at 10. In particular, the Commission recognized that the recovery period of Trojan could be changed if the ground rules for UE 88 were altered: "The Commission could determine that if Trojan should not have been included in rate base, PGE should have recovered the entire Trojan balance immediately instead of over 17 years, as provided in Order No. 95-322." *Id.* at 10-11. This reflects just one ratemaking decision in UE 88 – the recovery period for the Trojan investment – directly affected by the court decisions.

## **B. COST OF CAPITAL**

Central to the ratemaking decisions in UE 88 was a determination of PGE's cost of capital. The Court of Appeals' decision rejecting recovery of the return on PGE's investment in Trojan has dramatically changed the circumstances. Therefore, the Commission should revisit cost of capital.

The Court of Appeals decision potentially affects both the cost of equity and the cost of debt. A utility's return on investment (both debt and equity) must be commensurate with the return on investments in other enterprises having corresponding risks. ORS 756.040(1)(a). With respect to equity, the Commission should consider whether

exclusion of any "return on" the \$340 million Trojan balance<sup>5</sup> over a 17-year period changed the company's risk profile and, therefore, the enterprises with which PGE's allowed return on investment should be comparable. PGE submits that it did. With respect to debt, an important consideration in a utility's debt ratings is the regulatory environment in which it operates. The Commission should consider whether the legal rulings would increase PGE's cost of debt.

The Commission's decision concerning cost of capital must be revisited for a second reason. Utility return on investment must be sufficient to ensure confidence in the financial integrity of the utility, allowing the utility to maintain its credit and attract capital. ORS 756.040(1)(b). The Commission should consider whether it needs to increase the approved rate of return on investment in UE 88 to meet these standards after eliminating the \$340 million Trojan balance from the rate base. Again, PGE submits that it does.

### **C. APPLICATION OF NET BENEFITS**

The Commission used a net benefits test to identify the point at which PGE ratepayers were indifferent between the option of continued operation of Trojan and the option of Trojan closure. The closure scenario assumed a return on PGE's undepreciated Trojan investment. Determining how the Commission would have treated the undepreciated balance under the framework of the Court of Appeals' opinion and over what timeframe PGE would have been allowed to recover that balance are essential to the application of the net benefits test to the decision to close Trojan.

In considering UE 88 rates, the Commission did not want to put customers in a worse financial position than they would have been in if PGE had continued to operate Trojan. But just as importantly, the Commission did not want to punish PGE or deter it from

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<sup>5</sup> The 1995 Trojan balance is sometimes identified as \$250.7 million. That represents the balance after including the effects of deferred taxes associated with Trojan. The pre-tax balance of \$340.2 million as of March 31, 1995 does not include the deferred taxes associated with Trojan.



making an otherwise economically sound decision to close the plant. The parties need to revisit application of the net benefits test.

#### **D. RATEMAKING**

By identifying these specific prior determinations, PGE does not mean to suggest that these remand proceedings should be purely mathematical exercises. The Commission is exercising its legislative ratemaking function. It can and must consider these specific determinations and perhaps others in light of the public interest, providing appropriate incentives for utilities to act for the long term benefit of customers. The Commission must strike the appropriate balance between the interests of utility investors and the interests of customers. It must also determine the appropriate ratemaking policies to adopt given the new legal rules handed down by the courts.

#### **IV. RATE PERIOD**

The Commission will need to determine the time period affected by the Courts' opinions. There are only two rate orders that have been challenged. The UE 88 rates in Order 95-322 were in effect from April 1 through November 28, 1995. The rates implementing the UM 989 settlement were in effect from October 1, 2000 through September 30, 2001.

#### **V. UM 989**

The parties should present evidence concerning the impact of the above issues (and any other UE 88 ratemaking issues included in this docket) on the settlement approved in UM 989. In addition, the parties may present evidence relevant to determining whether the rates approved in Order Nos. 00-601 and 02-227 were just and reasonable.

#### **VI. PROCEDURAL MATTERS**

PGE assumes the burden of proof on this remand with respect to showing that rates consistent with the ratemaking changes proposed by PGE would have been just and

reasonable, as with any rate determination. ORS 757.210. Therefore, PGE suggests that it file opening testimony followed by a response from URP and intervenors Frank Gearhart, Kafoury Bros., LLC and Patricia Morgan. Subsequently, the staff should respond, followed by a reply from PGE.

PGE proposes that normal discovery rules apply, with data requests, written testimony and opportunity for depositions, a hearing with an opportunity for cross examination, and briefing to follow the hearing.<sup>6</sup>

## VII. IMPLEMENTATION

The final phase of these proceedings will require the Commission to determine the appropriate mechanism to implement the rate determinations it reaches. We agree with the ALJ that questions about the Commission's authority to order refunds can be deferred to this implementation stage. While PGE disputes that a refund or downward adjustment to future rates is appropriate or legal in these circumstances, should the Commission decide otherwise, it needs to determine the amount to be distributed, whether or not interest should be applied and, if so, how it should be calculated. Further, the

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<sup>6</sup> Indeed, URP has already initiated discovery with its request dated May 21, 2004.

Commission would need to identify the appropriate recipients of any adjustment and determine whether those should include former as well as current customers.

DATED this 3rd day of June, 2004.

PORTLAND GENERAL ELECTRIC  
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**CERTIFICATE OF SERVICE**

I hereby certify that on this day I served the foregoing **OPENING MEMORANDUM OF PORTLAND GENERAL ELECTRIC COMPANY REGARDING PHASE I SCOPE** by mailing a copy thereof in a sealed, first-class postage prepaid envelope, addressed to each party listed below and depositing in the U.S. mail at Portland, Oregon.

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DATED this 3rd day of June, 2004.

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