

1 **BEFORE THE PUBLIC UTILITY COMMISSION**
2 **OF OREGON**

3 UM 1121

4 In the Matter of OREGON ELECTRIC
5 UTILITY COMPANY, LLC, et al.,
6 Application for Authorization to Acquire
Portland General Electric Company

STAFF'S OPENING BRIEF

7 **INTRODUCTION**

8 On March 8, 2004, certain entities and private individuals (Applicants) filed a joint
9 application for an order from the Public Utility Commission of Oregon (Commission) approving
10 the entity known as Oregon Electric Utility Company's (OEUC) acquisition of the common
11 stock of Portland General Electric Company (PGE) from PGE's parent company, Enron
12 Corporation (Enron). Subsequently, the Applicants amended their application. The application,
13 as amended, is in the record, marked as OEUC/ 22 (Application). As shown by OEUC/22, the
14 individual Applicants consist of: OEUC; TPG Partners III, L.P; TPG Partners IV, L.P.;
15 Managing Members Gerald Grinstein, Tom Walsh, Peter Kohler, M.D., Duane McDougall, and
16 Robert Miller.

17 The TPG applicant is a private equity investment firm. OEUC/Exhibit 3/Davis/3. TPG,
18 as a private equity firm, generally invests in privately held companies rather than in the public
19 stock and bond markets. *Id.* TPG plans to hold its investment in PGE no longer than 12 years.
20 *Id.* at 12.

21 The Commission opened UM 1121 to consider the Application and several parties
22 intervened in the proceeding. After numerous prehearing conferences, settlement conferences,
23 the filing of several rounds of written testimony, and evidentiary hearings, ultimately the parties
24 were unable to reach agreement on the conditions necessary for the Commission to approve the
25 Application.

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1 **SUMMARY OF STAFF’S POSITION**

2 Staff recommends the Commission deny the Applicants’ Application as presented
3 because it does not meet the requirements of ORS 757.511. See Staff/800, Conway/3. However,
4 staff presented numerous conditions (including a rate credit proposal) which, taken as a package,
5 allowed staff to recommend the Commission approve the Application. See Staff/800, Conway/2;
6 Staff/801.

7 In this brief, staff will list each of its conditions, and to the extent necessary, explain its
8 purpose and how staff’s condition may differ from a similar one presented by the Applicants or
9 another party. Moreover, after further review of the presentations the Applicants and the
10 intervening parties made either at the evidentiary hearing or in their written testimony, staff is
11 amending certain of its conditions. Staff will identify in this brief those conditions which it is
12 modifying and explain the reason for the modification.

13 It is important to note that staff does not view its conditions as providing complete
14 protection against the harm each is intended to address. “Even where conditions have been
15 agreed to or recommended that address risks and harms of the transaction, these conditions serve
16 to mitigate rather than eliminate risk.” Staff/800, Conway/12-13. In other words, staff’s
17 conditions are imperfect - time will tell if they are in fact sufficient to protect PGE’s customers
18 and the public at large. The rate credit is set, in part, in recognition of the difficulty in foreseeing
19 and addressing the risks and harms inherent to this proposed acquisition. *Id.*

20 **APPLICATION OF ORS 757.511**

21 The Commission’s decision to approve or deny an application to acquire a utility is
22 governed by ORS 757.511. ORS 757.511(3) provides the standard the Commission should apply
23 when considering an application. ORS 757.511(3) states, in relevant part:

24 If the Commission determines that approval of the application will serve the public
25 utility’s customers in the public interest, the commission shall issue an order
26 granting the application. The commission may condition an order authorizing the
acquisition upon the applicant’s satisfactory performance or adherence to specific
requirements. The commission shall otherwise issue an order denying the

1 application. The applicant shall bear the burden of showing that granting the
2 application is in the public interest.

3 In its Order No. 01-778, the Commission set forth how it would apply ORS 757.511(3).

4 The Commission stated the statute requires a two-step assessment of whether the proposed
5 acquisition would (1) provide a “net benefit” to the utility’s customers, and (2) impose “no
6 harm” to the public at large. *See* Order 01-778 at 8, 11; Staff/100, Conway/3. In commenting on
7 these two standards, the Commission opined:

8 We do not believe that this [referring to the net benefit standard] is either rigid or
9 arbitrary... We do not intend to reduce the net benefit standard to economic
10 considerations as a matter of policy. We will consider the total set of concerns
11 presented by each merger application in determining how to assess a net
12 benefit... Because potential harm from merger transactions is often difficult to
13 verify, recent orders have required monetary terms as a way to demonstrate that
14 customers will receive a net benefit... We read this second step as setting a no harm
15 standard to the public at large... Therefore, in addition to finding a net benefit to the
16 utility’s customers, we must also find that the proposed transaction will not impose
17 a detriment on Oregon citizens as a whole.
18 Order 01-778 at 11.

19 An analysis of “net benefits” includes a review of both the positives (benefits) and
20 negatives (risks or harms) for customers. Simply stated, to find net benefits the Applicants must
21 show the acquisition’s expected overall benefits outweigh its expected risks and harms. *See also*
22 Staff/800, Conway/13.

23 In its written testimony, staff explained how it applied ORS 757.511 and the
24 Commission’s interpretation of the statute to the Application. Staff observed that in prior
25 acquisitions a finding of approval was accompanied by a series of conditions addressing such
26 matters as service quality, ring-fencing financial conditions and rate credits. Staff/100,
27 Conway/3-4. In this case, staff is proposing 38 conditions (Staff Conditions) to address the risks
28 and harms staff identified as accompanying the proposed acquisition. *See* Staff/801 and the
29 amendments to the conditions made in this Opening Brief.¹ Further, consistent with the
30 Commission’s observations in its Order 01-778 about the inherent difficulty of verifying the

¹ Staff is attaching to this Opening Brief a copy of its revised Conditions. *See* Attachment A.

1 potential harm of an acquisition, staff also recommends the Applicants provide a guaranteed (i.e.
2 no offsets for potential cost savings) rate credit to PGE’s customers in the amount of \$75 million
3 as a condition of approval. *See* Staff Condition 20.

4 Finally, while it is not in dispute, it is important for the Commission to note that the
5 Applicants have the burden in this case “of showing that granting the application is in the public
6 interest.” ORS 757.511(3). Thus, the Applicants have the burden of showing, consistent with
7 Order 01-778, the proposed acquisition will (1) provide a net benefit to PGE’s customers, and (2)
8 impose no harm to the public at large.

9 **STAFF’S CONDITIONS**

10 Staff’s conditions are structured to ensure (to the extent such an assurance is possible) the
11 Application satisfies ORS 757.511. Staff’s conditions re-impose and strengthen, where
12 appropriate, the existing relevant Enron conditions.² Staff also recommends new measures that
13 try to account for OEUC’s highly-leveraged nature and the challenges arising from the fact that
14 OEUC’s majority owners are a private equity investment firm that intends to re-sell its interest in
15 PGE.

16 In this section, staff will set out each of its recommended conditions in numerical order.
17 Staff will then explain, to the extent necessary, the condition’s meaning and its intended purpose.
18 Importantly, it appears to staff that many of its conditions are identical, or nearly so, to those the
19 Applicants propose. *See* Oregon Electric/501. Recognizing that the Applicants state their
20 conditions are offered as a “package” only, Oregon Electric/500, Davis/34, staff nonetheless
21 views those conditions that are common to both staff and the Applicants as essentially not being
22 in dispute. The following conditions fall into this category: 7-12, 14, 19, 23 and 24.

23 As stated in its Summary of Position, staff has also made changes to certain of its
24 conditions. These modifications arise from staff’s review of the last round of testimony

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² The Enron conditions do not automatically apply to OEUC. *See* Staff/100, Conway/21.

1 presented by the intervening parties, the testimony presented at the oral hearings, and from
2 staff's further consideration of its position in this case. Staff has changed the following
3 conditions from the wording set forth in Staff/801: 13, 15, 16, 17, 18, 22, 24, 25, 28, 29, 31
4 and 33. Staff will explain the reason for each change in this section.

5 In addition to amending some of its conditions, staff has also added certain conditions
6 after reviewing the intervenors' last round of testimony. The new conditions are as follows: 35,
7 36, 37 and 38.

8 Like the Applicants, staff views its conditions as a "package." However, certain of
9 staff's conditions are more important than others. For the Administrative Law Judges'
10 convenience, the disputed conditions which are most important to staff are as follows:
11 Conditions 16, 20, 25, and 27.

12 ***1. Stipulated Conditions***

13 Staff and OEUC, along with certain other parties to this docket, have stipulated to the
14 following six conditions ("Stipulated Conditions"). See Staff/801. Although OEUC and PGE
15 have agreed to the Stipulated Conditions, staff understands that OEUC and PGE's obligations are
16 subject to the Commission's approval of the Application and the closing of the transaction. See
17 *Id.* at 5. The Stipulated Conditions, at a minimum, constitute an agreement between staff and
18 OEUC regarding the wording of the six Stipulated Conditions. The Stipulated Conditions are
19 necessary conditions which, taken together with staff's additional recommended conditions,
20 allow staff to recommend the Commission approve the Application.

- 21 1. PGE and Oregon Electric shall maintain separate books and records. All PGE
22 and Oregon Electric financial books and records shall be kept in Portland,
23 Oregon.
- 24 2. Oregon Electric and PGE shall exclude from PGE's utility accounts all
25 goodwill resulting from this acquisition.
- 26 3. Oregon Electric and PGE shall exclude all costs and fees of the acquisition,
including, but not limited to, all costs and fees associated with gaining
regulatory approval before the Oregon Public Utility Commission, Nuclear

1 Regulatory Commission, Federal Energy Regulatory Commission, Federal
2 Trade Commission, Securities Exchange Commission, costs and fees associated
3 with forming Oregon Electric, and any banking or financial institution fees
4 associated with the creation of Oregon Electric and the financing and closing of
5 the Acquisition from PGE's utility accounts. Within 90 days following the
6 completion of the transaction, Oregon Electric will provide a preliminary
7 accounting of these costs. Oregon Electric and PGE agree to provide the
8 Commission a final accounting of these costs within 30 days following the
9 completion of the final accounting related to the transaction.

- 6 4. Unless such a disclosure is unlawful, Oregon Electric shall notify the
7 Commission of:
- 8 a. Its intention to transfer more than 5 % of PGE's retained earnings to
9 Oregon Electric over a six-month period, at least 60 days before such a
10 transfer begins.
 - 11 b. Its intention to declare a special dividend from PGE, at least 30 days
12 before declaring each such dividend.
 - 13 c. Its most recent quarterly common stock cash dividend payment from
14 PGE within 30 days after declaring each such dividend.
- 15 5. Subsequent to its purchase by Oregon Electric, PGE shall continue to perform
16 under the Service Quality Measures ("SQM"), as set forth in Stipulations for
17 PGE Service Quality Measures UM 814/UM 1121 dated July 13, 2004, for a
18 period of ten full calendar years after the date the current SQM is scheduled to
19 retire. Nothing in any provision of this Stipulation is intended to affect the
20 Commission's authority to directly administer the stated terms of the SQM.
21 Notwithstanding the provisions described in this paragraph, the parties have
22 agreed to replace the current R4 measurement with a CAIDI-related
23 measurement, and further that PGE will maintain records of outages longer than
24 three hours. In addition, PGE agrees to work with ICNU to evaluate and, if
25 necessary, develop additional service quality standards related to service to
26 industrial customers.
6. PGE and Oregon Electric shall maintain separate debt ratings and, if more than
\$5 million of preferred stock is outstanding, then PGE and Oregon Electric
shall maintain separate preferred stock ratings.

22 ***2. Additional Staff Conditions***

23 The following conditions are not contained in a stipulation. However, these are
24 necessary conditions, which taken together with the Stipulated Conditions, allow staff to
25 recommend the Commission approve the Application.

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1 Condition 7

2 Staff's Condition 7 is found at Staff/801, Conway/7. OEUC has proposed identical
3 language for this condition. *See Oregon Electric/501, Davis/2.*

4 The Commission or its agents may audit the accounts of Oregon Electric, its
5 affiliates, and any subsidiaries that are the bases for charges to PGE to determine
6 the reasonableness of allocation factors used by Oregon Electric to assign costs to
7 PGE and amounts subject to allocation or direct charges. Oregon Electric agrees to
cooperate fully with such Commission audits. (*See Staff/1100, Hathhorn/2, line 20
through Hathhorn/3, line 5.*)

8 Condition 8

9 Staff's Condition 8 is found at Staff/801, Conway/7. OEUC has proposed identical
10 language for this condition. *See Oregon Electric/501, Davis/2.*

11 Oregon Electric and its affiliates shall not allocate to or directly charge to PGE
12 expenses not authorized by the Commission to be so allocated or directly charged.
(*See Staff/1100, Hathhorn/3, lines 6-10.*)

13 Condition 9

14 Staff's Condition 9 is found at Staff/801, Conway/7. OEUC has proposed identical
15 language for this condition. *See Oregon Electric/501, Davis/2.*

16 PGE shall maintain its own accounting system. PGE and Oregon Electric shall
17 maintain separate books and records, both of which shall be kept in Portland,
Oregon. (*See Staff/1100, Hathhorn/3, lines 11-14.*)

18 Condition 10

19 Staff's Condition 10 is found at Staff/801, Conway/7-8. OEUC has proposed identical
20 language for this condition. *See Oregon Electric/501, Davis/2-3.*

21 If the Commission believes that Oregon Electric and/or PGE have violated any of
22 the conditions set forth herein, any conditions contained in other stipulations signed
23 by Oregon Electric and PGE, or any conditions imposed by the Commission in its
24 final order approving the Application (collectively, the "Conditions"), then the
Commission shall give Oregon Electric and PGE written notice of the violation.

25 a. If the violation is for failure to file any notice or report required by the
26 Conditions, and if Oregon Electric and/or PGE provide the notice or
report to the Commission within ten business days of the receipt of the
written notice, then the Commission shall take no action. Oregon

1 Electric or PGE may request, for cause, permission for extension of the
2 ten-day period. For any other violation of the Conditions, the
3 Commission must give Oregon Electric and PGE written notice of the
4 violation. If such failure is corrected within five business days of the
5 written notice, then the Commission shall take no action. Oregon
6 Electric or PGE may request, for cause, permission for extension of the
7 five-day period.

- 8
- 9 b. If Oregon Electric and/or PGE fail to file a notice or written report within the
10 time permitted in subparagraph a. above, or if Oregon Electric and/or PGE fail
11 to cure, within the time permitted above, a violation that does not relate to the
12 filing of a notice or report, then the Commission may open an investigation,
13 with an opportunity for Oregon Electric and/or PGE to request a hearing, to
14 determine the number and seriousness of the violations. If the Commission
15 determines after the investigation and hearing (if requested) that Oregon
16 Electric and/or PGE violated one or more of the Conditions, then the
17 Commission shall issue an Order stating the level of penalty it will seek.
18 Oregon Electric and/or PGE, as appropriate, may appeal such an order under
19 ORS 756.580. If the Commission's order is upheld on appeal, and the order
20 imposes penalties under a statute that further requires the Commission to file a
21 complaint in court, then the Commission may file a complaint in the
22 appropriate court seeking the penalties specified in the order, and Oregon
23 Electric and/or PGE shall file a responsive pleading agreeing to pay the
24 penalties. The Commission shall seek a penalty on only one of Oregon
25 Electric or PGE for the same violation.
- 26 c. The Commission shall not be bound by subsection (a) in the event the
Commission determines PGE and/or Oregon Electric has violated any of the
material conditions, contained herein, more than two times within a rolling
24-month period.
- d. PGE and/or Oregon Electric shall have the opportunity to demonstrate to the
Commission that subsection (c) should not apply on a case-by case basis.
(See Staff/800, Conway/8, line 3 through Conway/9, line 2.)

21 Condition 10 applies to the entire package of conditions and outlines the procedure that
22 the parties agree to follow when the Commission believes that Oregon Electric or PGE, or both,
23 have violated any of the conditions that are part of this transaction.

24 Condition 11

25 Staff's Condition 11 is found at Staff/801, Conway/8. OEUC has proposed identical
26 language for this condition. See Oregon Electric/501, Davis/3.

1 Oregon Electric shall maintain and provide the Commission unrestricted access to a
2 record of each instance in which TPG Applicants withhold their consent to a
3 decision of the PGE Board of Directors. The record shall detail the basis for the
4 decision, including any governing report or document that memorializes the
5 exercising of the consent rights and shall identify the persons involved in making
6 the TPG Applicant Consent Rights decision. Oregon Electric shall provide the
7 records to the Commission upon request. Nothing in this condition shall be
8 deemed to be a waiver of Oregon Electric's or PGE's right to seek protection of the
9 information. Nothing in this paragraph shall prevent the Commission from
10 disclosing to the public the number of times the TPG Applicants exercised their
11 consent rights within a certain period of time. (*See Staff/900, Morgan/18, line 22*
12 *through Morgan/19, line 2.*)

13 This Condition requires OEUC to maintain and provide (upon request) the Commission
14 with access to a record of instances in which OEUC withholds its consent to a decision of the
15 PGE Board. This Condition does not establish a time frame for which a record will be developed
16 by the Board. Staff notes that it expects the Board will develop a record in a timely manner as a
17 standard course of business. In the event the Commission seeks a more definite time frame for
18 access to such records, the Commission could consider requesting OEUC's Board to make such
19 a record available, within a specified time frame, upon request. If not such record exists in a
20 final form within the specified time frame, a draft record could be available and would be
21 provided to the Commission.

22 Condition 12

23 Staff's Condition 12 is found at Staff/801, Conway/8. OEUC has proposed identical
24 language for this condition. *See Oregon Electric/501, Davis/4.*

25 Oregon Electric and PGE shall maintain and provide the Commission unrestricted
26 access to all books and records of Oregon Electric and PGE that are reasonably
27 calculated to lead to information relating to PGE, including but not limited to,
28 Board of Directors' Minutes, Board Subcommittee Minutes, and other Board
29 Documents. (*See Staff/900, Morgan/18, line 35 through Morgan/19, line 5.*)³

30 ³In Staff/801, staff's conditions 12, 15, and 19 contain sentences that provide that nothing in the
31 condition shall be deemed a waiver of Oregon Electric's or PGE right to seek protection of the
32 information. In Oregon Electric/501, Oregon Electric language does not contain these sentences.
33 However, Oregon Electric includes a General Provision A that provides that nothing in the
34 conditions affects any party's rights to seek protection of information or documents under the
35 Commission normal rules unless expressly waived.

1 Condition 13

2 Staff's Condition 13 is found at Staff/801, Conway/9. After further review, staff has
3 decided to replace its Condition 13 with OEUC's Condition 13. See Oregon Electric/501,
4 Davis/4. Thus, staff amends its Condition 13 to read as follows:

5 PGE and Oregon Electric shall notify the Commission within 30 days of the
6 formation of any subsidiary. Such notice shall include a copy of the business plan
7 and capitalization strategy, as well as any planned or anticipated transactions of the
8 subsidiary with PGE or Oregon Electric as applicable.

8 Although both conditions are similar and provide for notification to the Commission
9 regarding the formation of any subsidiary, Oregon Electric's condition is more specific on the
10 type of information to be included in the notice and applies to both PGE and Oregon Electric.

11 Condition 14

12 Staff's Condition 14 is found at Staff/801, Conway/9. OEUC has proposed identical
13 language for this condition. See Oregon Electric/501, Davis/4.

14 Oregon Electric and PGE shall provide the Commission access to all books of
15 account, as well as all documents, data and records of their affiliated interests,
16 which pertain to transactions between PGE and all its affiliated interests, unless
17 such transactions are exempt under applicable laws or the Master Services
18 Agreement. (See Staff/1100, Hathhorn/4, lines 5-11.)

18 Condition 15

19 Staff's Condition 15 is found at Staff/801, Conway/9. After further review, staff has
20 decided to replace its Condition 15 with OEUC's Condition 15. See Oregon Electric/501,
21 Davis/4. Thus, staff amends its Condition 15 to read as follows:

22 ///

23 _____
24 Substantively, staff and the Applicants agree and it is merely a matter of form as to whether
25 condition 12, 15, and 19 contain an explicit recognition of Oregon Electric's or PGE's right to
26 seek protection of the information or whether a general provision is added that provides the same
protection for conditions 12, 15, and 19. For purposes of these specific conditions, staff supports
a general condition that provides: "Nothing in conditions 12, 15, and 19 shall be deemed a
waiver of OEUC's or PGE's right to seek protection of the information under the Commission's
normal rules."

1 In the event of a dispute between the Commission or Commission Staff and Oregon
2 Electric or PGE regarding a request made pursuant to the Acquisition Conditions,
3 the parties agree that an Administrative Law Judge (ALJ) shall resolve the dispute
4 as follows: (i) within ten (10) business days Oregon Electric or PGE shall deliver
5 to the ALJ the books and records responsive to the request and shall indicate the
6 basis for the objection; (ii) Staff may respond in writing and Oregon Electric and/or
7 PGE may reply to Staff's response; (iii) the ALJ shall review the documents in
8 private; and (iv) the ALJ shall issue a ruling determining whether the documents (a)
9 are reasonably calculated to lead to the discovery of relevant information, and, if
10 so, (b) whether the documents should receive the protection requested. The ALJ
11 shall use this standard whether or not the Commission or Commission Staff is
12 making the request in connection with an open docket. Nothing in this provision
13 shall affect the right of Oregon Electric or PGE to request that the Commission
14 treat the documents as exempt from disclosure to third parties under applicable law.

9 Although both conditions are similar, Oregon Electric's condition more accurately states
10 that the condition applies to disputes between the Commission or Commission Staff and Oregon
11 Electric or PGE.

12 Condition 16

13 Staff's Condition 16 is found at Staff/801, Conway/9. However, after further review,
14 staff has slightly revised this condition. The changes are shown in **bold** print:

15 PGE will not make any distributions to OEUC that would, or could reasonably be
16 expected to, cause the common equity portion of PGE's total capital structure to
17 fall below 48 percent. (See Staff/900, Morgan/19, line 7 through Morgan/20,
18 line 10.)

- 19 a. "Total capital structure" is defined as common equity, preferred
20 equity, and long-term debt.
21 b. "Long-term debt" is defined as (1) outstanding debt with an initial
22 term of more than one year plus the sum of committed and drawn
23 balances greater than \$150 million on any of PGE's unsecured
24 revolving lines of credit (Unsecured Revolvers) **less any balances**
25 **related to collateral or security provided to counterparties for**
26 **power supply and related agreements necessary to meet PGE's**
retail loads and other firm commitments consistent with those
activities recognized in rates; and (2) the sum of committed and
drawn balances on PGE's secured revolving lines of credit (Secured
Revolvers).
c. A "committed balance" is the sum of commitments used to support
any borrowing capacity or other purposes, such as a commercial paper
program.
d. A "drawn balance" is sum of amounts drawn against the Revolvers.
e. Hybrid securities (e.g. convertible debt) will be assigned to equity and
long-term debt based on the characteristics of the hybrid security. The

1 Commission, prior to their issuance, will determine the assignment of
2 the equity and debt characteristics.

3 Under the terms of the Application, OEUC will own 100% of PGE's stock. OEUC/22,
4 Oregon Electric/3, Davis/2-3. Condition 16 is basically designed to limit the ability of PGE to
5 make distributions to OEUC that could harm PGE's financial integrity. See Staff/900,
6 Morgan/19.

7 Condition 16 is a complicated measure, and is one which is critical for staff to
8 recommend that the Commission approve the Application. Condition 16 has its origins in a
9 similar condition the Commission imposed for Enron's acquisition of PGE. See Order No. 97-
10 196, Appendix A at 2 (Condition 6).⁴ Identical to Enron's Condition 6, staff's Condition 16 sets
11 an equity floor of 48% against which PGE could make a distribution to OEUC.

12 Staff modified the underlying Enron condition in several ways, both to improve upon it,
13 and to account for the unique circumstances accompanying this Application. Preliminarily, staff
14 observes that its Condition 16 is not as strong as Enron Condition 6 in one important aspect. In
15 discussing Enron's Condition 6 in its Order approving the Enron acquisition, the Commission
16 stated: "PGE must maintain the common equity portion of its capital structure at 48% or higher
17 unless the Commission approves a different level, and must notify the Commission of certain
18 dividends and distributions to Enron." Order 97-196 at 7. Staff interprets this language as
19 prohibiting PGE's equity ratio from falling below 48% *for any reason*.

20 Staff's Condition 16, on the other hand, only prohibits a *distribution* that would cause
21 PGE's equity ratio to fall below 48%. This provides more assurance to OEUC that Condition 16
22 would not be imposed in a rigid, inflexible manner, as requested by the Applicants. See Oregon
23 Electric/100, Davis/53. However, as a trade-off, staff added the phrase "or could reasonably be
24 expected to" in the first sentence of the condition. The phrase provides a safety-net that is

25 ⁴ Enron's Condition 6 provides: "PGE shall not make any distribution to Enron that would cause
26 PGE's equity capital to fall below 48% of the total PGE capital without Commission approval.
The Commission Staff, PGE and Enron may re-examine this minimum equity percentage as
financial conditions change, and may request that it be adjusted."

1 intended to preserve for the Commission the necessary discretion to review any distribution that
2 caused, *or contributed to*, PGE's equity ratio falling below 48%.

3 The following example illustrates how staff's language would work. Assume PGE issues
4 a dividend to OEUC that causes PGE's equity ratio to fall to exactly 48%, a circumstance
5 allowed under the condition. However, continuing with this example, PGE then incurs a debt,
6 asset write-down or loss (that would be reflected as a decrease in equity) arising from a potential,
7 but reasonably foreseeable, liability that in fact occurs. Inclusion of the additional debt would
8 then result in PGE's equity ratio falling below the 48% equity floor. This is the circumstance
9 that the Applicants are trying to preserve. *Id.* However, as a trade-off, staff's language would
10 allow the Commission in this example to look back to determine whether it was reasonably
11 foreseeable that PGE would in fact incur the potential debt before issuing the dividend that took
12 the equity ratio to the bottom of the 48% equity floor. If the Commission determined that the
13 event was reasonably foreseeable, the Commission could require remedial action as allowed by
14 Condition 10.

15 OEUC proposes its own Condition 16 which, while seemingly similar to staff's, is
16 actually quite different. *See Oregon Electric/501, Davis/4* (Condition 16). For the point
17 addressed above, OEUC would strike staff's "or reasonably could be expected to" clause, and in
18 its place insert "as determined in accordance with Generally Accepted Accounting Principles
19 ("GAAP")." *Id.* In support of its position, TPG's witness Wheeler points out that accountants
20 throughout the business world use the GAAP principles. *Oregon Electric/600, Wheeler/11.*
21 From this, Wheeler argues that GAAP represents an accepted precedent, while staff's language is
22 too vague and subjective to be useful. *Id.; see also PGE/400, Piro/8.*

23 Staff recognizes that GAAP is widely accepted in the business and accounting world.
24 Nonetheless, GAAP is not the best method for analyzing distributions made under Condition 16.
25 The chief problem with using GAAP is the one staff identifies in its example. GAAP would not
26 necessarily preclude OEUC from causing PGE to make a distribution that in itself is allowed by

1 Condition 16, but which, along with the impact of reasonably foreseeable liability, contributes to
2 PGE's equity ratio falling below the 48% floor. The Commission must have the authority and
3 discretion to review all factors that result in the 48% floor being breached. Further, the
4 Commission has experience with making "foreseeability" judgments in ratemaking and prudence
5 reviews.

6 Sections (a), (c) and (e) for both staff's and OEUC's Condition 16 are essentially
7 identical.

8 Staff and OEUC differ on their language for Section (b) of Condition 16. The primary
9 difference is over the treatment and inclusion of "revolvers" in the definition of long-term debt.
10 Simply stated, the 48% equity ratio compares the relationship between the amounts of equity and
11 long-term debt a company has. Thus, the more long-term debt a company has, the lower its
12 relative percentage of equity. As such, including revolvers as long-term debt in Condition 16
13 ultimately increases the amount of equity PGE must maintain in its capital structure before it
14 may issue dividends to OEUC.

15 By "revolver," staff is referring to PGE's secured and unsecured revolving lines of credit.
16 A "secured" revolver is a line of credit that is generally backed by first mortgage bonds. *See*
17 PGE/400, Piro/7. In the usual circumstance, PGE must obtain the Commission's approval before
18 creating a secured revolver. PGE does not have a secured revolver at the present time, and has
19 no current plans to acquire one. PGE/400, Piro/7. PGE states that it intends to acquire "a new,
20 three-year, \$250 million revolver" [not specified but presumably "unsecured"] to support its
21 short-term capital needs. PGE/400, Piro/5.

22 Staff's Section (b) would include as long-term debt the committed and drawn balances
23 greater than \$150 million for any of PGE's unsecured revolvers. As shown in the bold print,
24 staff is now proposing to accept OEUC's language in Section (b) that would exclude amounts
25 committed or drawn for purposes of providing credit in the wholesale power and fuels markets.
26 *See also* PGE/400, Piro/6. However, in agreeing to OEUC's language, staff is restricting the

1 exclusion to only collateral or security needed for regulated purposes. Staff is also proposing to
2 include as long-term debt the entire amount of PGE’s committed and drawn balances on secured
3 revolvers, since they are generally supported by first mortgage bonds.

4 Conversely, the Applicants propose to include in long-term debt only the amount of its
5 unsecured revolvers that is greater than \$250 million, calculated using a 12-month rolling
6 average. The Applicants also propose to exclude any amount of the secured revolvers. Oregon
7 Electric/501, Davis/4-5 (Condition 16).

8 The Applicants argue that revolvers are treated as short-term debt under GAAP.
9 PGE/400, Piro/5. Even so, the Applicants agree to include unsecured revolvers as long-term
10 debt, but only the amount greater than \$250 million on a 12-month rolling average. The problem
11 with the Applicants’ proposal is that, based upon PGE’s history with unsecured revolvers, it is
12 extremely unlikely that PGE would ever exceed the \$250 million rolling average threshold. *See*,
13 *e.g.*, PGE/400, Piro/4-5.

14 The Applicants remove secured revolvers entirely from their Condition 16. Instead, they
15 suggest the Commission reserve a decision on how to categorize the secured revolver until PGE
16 actually acquires one. PGE/400, Piro/7. PGE’s witness Piro recognizes that the Commission’s
17 most recent decision concerning a PGE secured revolver was to treat it as long-term debt. *See*
18 PGE/400, Piro/7, citing PUC Docket No. UF-4188.

19 In response, staff includes secured and unsecured revolvers in Condition 16 to help guard
20 against their possible questionable use. To start, the Commission has authority over long-term,
21 but not short-term, debt issuance. *See, e.g.*, ORS 757.415, ORS 757.480. Staff is concerned that
22 OEUC/PGE could rely on a revolver, which is short-term debt, to help finance utility plant
23 expenditures, which are expected to ultimately be refinanced with true long-term debt. Without
24 staff’s Condition 16 including revolvers as long-term debt, PGE could use the short-term
25 revolvers to pay for long-term utility-related expenditures, thus helping PGE to stay above the
26

1 48% equity floor, while using other internal funds for dividend payments to OEUC. Staff/200,
2 Morgan/28-29.

3 As to Section (d), the only difference between staff and OEUC is staff's inclusion of
4 secured revolvers within the definition of a "drawn balance." Resolution of Section (b) will also
5 resolve the dispute over Section (d)'s language.

6 Condition 17

7 Staff's Condition 17 is found at Staff/801, Conway/10. After further review, staff revises
8 this condition as follows (new language shown in **bold**, deleted language is shown in ~~strike-out~~):

9 **Oregon Electric agrees that the customers shall be held harmless if PGE's the**
10 ~~allowed~~ return on common equity and other costs of capital viewed on a stand-
11 alone basis will not rise as a result of Oregon Electric's ~~acquisition~~ **ownership** of
12 PGE. These capital costs refer to the costs of capital used for purposes of rate
13 setting, avoided cost calculations, affiliated interest transactions, least cost
14 planning, and other regulatory purposes. (*See Oregon Electric/501, Davis/5*)
15 ~~Staff/900, Morgan/20, lines 11-15.~~

16 With these changes, staff is accepting the Applicants' Condition 17. *See Oregon*
17 *Electric/501, Davis/5; see also Oregon Electric/600, Wheeler/5.*

18 Condition 18

19 Staff's Condition 18 is found at Staff/801, Conway/10. After further review, staff revises
20 its Condition 18 as follows (new language shown in **bold**, deleted language is shown in ~~strike-~~
21 ~~out~~):

22 **Oregon Electric agrees that the customers of PGE shall be held harmless if**
23 **PGE's revenue requirement, viewed on a stand-alone basis,** is higher due to
24 Oregon Electric's ownership of PGE. (~~See Staff/900, Morgan/20, lines 17-19.~~)
25 With these changes, staff is accepting OEUC's Condition 18. *See Oregon*
26 *Electric/501, Davis/5; see also Oregon Electric/600, Wheeler/5.*

27 Condition 19

28 Staff's Condition 19 is found at Staff/801, Conway/10. OEUC has proposed identical
29 language for this condition. *See Oregon Electric/501, Davis/5.*

30 Oregon Electric and PGE shall maintain (for a rolling five-year period) and provide
31 the Commission unrestricted access to all written information provided to stock or
32 bond rating analysts, which directly or indirectly pertains to PGE or any affiliate
33 that exercises influence or control over PGE. Such information includes, but is not

1 limited to, reports provided to, and presentations made to, stock and bond rating
2 analysts. For purposes of this condition, “written” information includes, but is not
3 limited to, any written and printed material, audio and videotapes, computer disks
4 and electronically-stored information.

5 Condition 20

6 Staff’s Condition 20 is found at Staff/801, Conway/10. After further review, staff revises
7 its Condition 20 as follows (new language is shown in **bold**, deleted language is shown in ~~strike-~~
8 ~~out~~):

9 Oregon Electric agrees to provide a guaranteed rate credit in the amount of \$75
10 million to PGE’s customers. The amount of this credit will be \$15 million per year
11 for 5 years beginning with ~~2005~~ **2006**. PGE shall establish a balancing account and
12 credit that account with the \$15 million annual credit, beginning on January 1, ~~2005~~
13 **2006** (~~or within 10 business days of the closing of the transaction~~), and each
14 subsequent January 1, through ~~2009~~ **2010**. The balancing account will accrue
15 interest on the unamortized balance at PGE’s authorized rate of return. Beginning
16 January 1, ~~2005~~ **2006**, PGE will amortize amounts in the balancing account on an
17 equal cents per kWh basis, as a credit to customers’ distribution rates. PGE will
18 exclude all effects of the rate credit from the company’s results of operations and
19 any rate review. (See Staff/800, Conway/9-~~14~~ **lines 14-12**.)

20 Staff’s changes result in having the rate credit commence on January 1, 2006 rather than
21 in January 2005 (or within 10 business days of the closing of the transaction). With these
22 modifications, staff basically adopts a similar proposal suggested by the Industrial Customers of
23 Northwest Utilities (ICNU). See ICNU/301. The changes improve staff’s condition because
24 implementing the rate credits in 2006, rather than 2005, would be administratively easier for the
25 Applicants and for the Commission to oversee. In addition, starting the rate credit in 2006 rather
26 than an earlier date should also serve to improve PGE’s and OEUC’s cash flow when it is most
leveraged.

Staff proposes the rate credit to account for the net risks and harms present in this
proposed acquisition and to produce net benefits for customers. Staff/800, Conway/10. As the
Commission recognized, it is admittedly difficult to determine the appropriate rate credit
amount: “Because potential harm from merger transactions is often difficult to verify, recent
orders have required monetary terms as a way to demonstrate that customers will receive a net

1 benefit.” Order 01-778 at 11. In other words, the process of setting the rate credit amount
2 frankly involves judgment, and it cannot be reduced to precise mathematical calculations.

3 In recommending its \$75 million rate credit, staff considered many factors. Staff
4 reviewed the Commission’s most recent ORS 757.511 proceedings, each of which included a
5 rate credit. Staff also assessed the risks and harms of the transaction against staff’s admittedly
6 strong, but not foolproof, conditions created to address those risks and harms. Further, staff
7 assessed any “loss” that may occur should the acquisition proceed. Calculation of the loss
8 involves an assessment of the benefits inherent under the current Enron conditions, as well as an
9 analysis of what may happen to PGE should the Commission deny the Application. Finally, staff
10 considered the alleged “benefits” of the acquisition.

11 To begin, staff witness Conway carefully reviewed each of the three prior Commission
12 acquisition proceedings. *See generally* Staff/800, Conway/10-11. In approving Enron’s
13 application to purchase PGE, the Commission approved a stipulation that included \$36 million in
14 rate credits (spread over four years). *Id.* (citing Order 97-196). Scottish Power agreed to pay
15 customers \$52 million in rate credits (also spread over four years). *Id.* (citing Order 99-616).
16 Finally, the Commission issued its Order 00-702, approving a stipulation under which Sierra
17 Pacific agreed to pay customers \$95 million in rate credits (spread over seven years). *Id.*

18 Staff readily acknowledges that each acquisition proceeding must be assessed on its own
19 merits. Clearly, it would not be correct, for example, to simply average the rate credits ordered
20 in these three prior proceedings to arrive at the appropriate amount for this docket. Nonetheless,
21 these prior proceedings provide useful guidance for how the parties and Commission in those
22 three cases viewed the notion of imposing rate credits to help “cover” risks and harms which are
23 not easily reduced to a monetary amount. In each circumstance, the parties and the Commission
24 agreed a rate credit in the many millions of dollars was required.

25 Staff’s rate credit is also based upon its assessment of the risks and harms underlying the
26 Applicants’ proposed acquisition. In a very real sense, each of staff’s 38 conditions is intended

1 to address a risk or harm related to this transaction. As stated, some conditions only mitigate the
2 concerns, however, and are unable to eliminate them entirely. *See* Staff/200, Morgan/31-32.
3 Again, staff’s rate credit and other conditions do not absolutely ensure or guarantee that the
4 acquisition would result in a net benefit to PGE’s customers. Indeed, reasonable people could
5 disagree whether, in hindsight, staff proposed sufficient conditions when recommending the
6 Commission approve Enron’s purchase of PGE. Staff here will highlight some of the more
7 worrisome concerns that remain despite a related condition.

8 Staff witness Morgan identified several potential risks and harms related to the financial
9 structure of this deal. Mr. Morgan testified at length about the risks surrounding the amount of
10 debt involved with this acquisition. OEUC needs approximately \$1.471 billion to purchase PGE.
11 OEUC/22, Exhibit/3, Davis/15. Of this amount, the TPG Applicants will provide \$525 million
12 in equity, and OEUC will borrow \$582 million of senior secured term loans, and \$125 million of
13 senior unsecured notes. OEUC/22, Exhibit/3, Davis/15; PGE/200, Tinker-Murray-Hager/5. Mr.
14 Morgan stated that he is concerned about the negative effects of the large amount of debt
15 inherent with this transaction.

16 One worry relates to “double-leverage.”⁵ Simply stated, double-leverage refers to a
17 company purchasing another company’s stock with borrowed funds. PGE/200, Tinker-Murray-
18 Hager/7. Here, OEUC proposes to buy PGE’s stock, in part, with borrowed money.

19 The concern with double leverage arises from the nature of debt itself. As is well-known,
20 borrowed money (debt) must be repaid, with interest. Staff/200, Morgan/25. PGE has its own
21 debt. *See* PGE/200, Tinker-Murray-Hager/4. Thus, when OEUC purchases PGE with debt,
22 OEUC has its own debt to service, and is “responsible” for PGE’s as well. The effect is best
23 seen when calculating the consolidated financial structure for the “combined” companies.

24

25

26 ⁵ “Leverage” refers to the amount of debt or preferred equity that exists in a company’s financial structure. Staff/200, Morgan/25.

1 Mr. Morgan provides an example in his testimony of the effect of double-leveraging on the
2 purchasing company's true financial structure. *See* Staff/200, Morgan/26-28.

3 As Mr. Morgan further explains, the double-leveraging proposed in this transaction could
4 negatively impact PGE. The transaction calls for PGE to make dividend payments to OEUC to
5 finance OEUC's debt payments. The amount of debt surrounding this deal places great pressure
6 on PGE to perform at a high level of efficiency to service it. Staff/900, Morgan/9-10. If PGE
7 were to have a poor financial performance, PGE could be forced to borrow on its line of credit to
8 fund its dividend to OEUC, which could result in credit rating companies lowering PGE's credit
9 rating. Staff/200, Morgan/28.

10 The highly-leveraged nature of the proposed acquisition has other negative effects.
11 Standard & Poor's, the credit-rating agency, has indicated it expects the highly leveraged nature
12 of the OEUC deal to decrease PGE's credit quality. Staff/200, Morgan/29. If PGE's credit
13 rating is lowered as expected because of this transaction, PGE's costs to obtain additional debt
14 would increase. Staff/200, Morgan/30, 50-51. An increased cost of debt is of special concern in
15 light of PGE's plans to make significant new capital expenditures for Port Westward. Customers
16 could face a \$1 million tab in additional costs for the Port Westward project due to PGE's
17 increased cost of debt arising from this transaction. Staff/900, Morgan/25. PGE's cost of debt is
18 also important because PGE has significant amounts of debt that it will be retiring by 2010.
19 Staff/900, Morgan/15.

20 PGE and the Applicants acknowledge Mr. Morgan's concerns about PGE's increased
21 cost of debt are valid. *See* PGE/100, Piro/21; Oregon Electric/200, Wheeler/15. Staff's
22 Conditions 25 and 27, to be discussed later, mitigate, but do not entirely satisfy, staff's concerns
23 with the level of debt inherent with this transaction.

24 Finally, Mr. Morgan outlines additional general concerns surrounding the transaction, not
25 the least of which is there are still no final financing contracts or operating agreements for staff
26 to review. *See* Staff/200, Morgan/46-51; Staff/900, Morgan/27.

1 Staff is also concerned that the financial pressures to service OEUC's debt will increase
2 the pressure on OEUC to make questionable cuts to PGE's costs. Depending on where the cuts
3 occur, PGE's service quality could be jeopardized. This is discussed further in staff's Conditions
4 22-24.

5 Staff also reviewed the Enron conditions to assess what PGE's customers would have to
6 forgo should the Commission approve this transaction. Staff determined that PGE's credit rating
7 has already gone down because of the activities of its owner, Enron. Staff/200, Morgan/31.
8 However, there is currently a ring-fencing condition that provides PGE's customers will not be
9 harmed due to Enron's ownership. *See* Staff/900, Morgan/24; *see also* Order 97-196, Appendix
10 A at 3 (Condition 7). As such, if Enron were to continue to own PGE, and PGE filed a petition
11 for new rates, staff would very likely recommend that PGE's shareholders, not PGE's customers,
12 absorb the increased costs arising from PGE's higher cost of debt which is due to Enron's
13 activities as PGE's owner. Staff estimates these increased costs would be \$5 to \$7 million per
14 year for many years to come. Staff/900, Morgan/24.

15 The final step in staff's analysis, used to arrive at its \$75 million recommended rate
16 credit, involved looking at any benefits arising from the proposed acquisition. Staff
17 acknowledges the benefits Applicants claim, such as: certainty of ownership and unified
18 shareholder support; accountability to customers and community; PGE having a first class board
19 of directors; thoughtful leadership; enhanced reliability and efficiency from investment in new
20 and existing utility resources; and safe and reliable efficient electric service. *See* Oregon
21 Electric/Exhibit 3/Davis/21-22. While these alleged benefits are certainly laudable, their value is
22 reduced because they are relatively nebulous in nature. Further, most of these benefits represent
23 a "given" in that the Commission expects PGE to have safe, reliable service (indeed, it is
24 required to do so by law), that it be accountable to the community, etc.

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1 Applicants also promise to direct Enron to award its promised indemnifications for
2 liabilities to PGE. TPG witness Davis explains at length the three categories of potential
3 liabilities facing PGE. *See* Oregon Electric/100, Davis/33-39; Oregon Electric/500, Davis/19-22.
4 The Applicants have negotiated certain indemnifications for these liabilities from Enron as part
5 of their agreement to purchase PGE. For the category known as “Control Group Liabilities,”
6 Enron agreed to indemnify the Applicants for liabilities incurred up to the purchase price (\$1.25
7 billion). Oregon Electric/100, Davis/35-36. For the other two categories of liabilities (Shared
8 Special Indemnification Matters and Non-shared Special Indemnification Matters), Enron agreed
9 to indemnify the Applicants for 90% and 100%, respectively, of the liabilities, up to a \$94
10 million cap. Oregon Electric/100, Davis/34-35. The Control Group Liabilities are “due to
11 Enron’s ownership.” Oregon Electric/500, Davis/19-20. However, Applicants assert that PGE is
12 solely responsible for the Shared Special Indemnification Matters. Oregon Electric/102, Davis/1.
13 By its Condition 21, the Applicants agree to direct Enron to pay the benefit of the indemnities
14 discussed in the Stock Purchase Agreement directly to PGE.

15 Staff recognizes that the Enron indemnifications represent a benefit of this transaction.
16 However, the benefit is not as great as it may appear. First, the Commission always retains the
17 right to deny PGE recovery in rates of the costs incurred for any of the liabilities. The
18 Commission may decide to disallow, or allow, such costs depending upon the circumstances
19 giving rise to any particular debt PGE incurs. Also, it is likely Enron would provide PGE the
20 indemnification for the Control Group Liabilities independent of the proposed sale to the
21 Applicants. *See* Enron/2, Bingham/3-4.

22 Further, part of the indemnifications’ value arises from the highly leveraged nature of the
23 transaction (which carries its own risks as discussed earlier). In other words, PGE, standing
24 alone, may be able to withstand a \$100 million write-off from a liability and still be viewed as a
25 low risk investment. However, because of the highly leveraged nature of this transaction, a
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1 \$100 million write-off to PGE may sharply reduce the consolidated equity ratio of OEUC and
2 PGE, with resulting impacts on PGE's perceived "riskiness." *See, e.g.,* Staff/200, Morgan/26-27.

3 Summarizing, staff took into account all of the various factors and concerns discussed
4 above to conclude that \$75 million in rate credits is required to produce, along with its other
5 recommended conditions, a net benefit for this transaction.

6 Condition 21

7 Staff's Condition 21 is found at Staff/801, Conway/11. After review, staff has decided to
8 accept the Applicants' language for this condition verbatim as follows:

9 To the extent that PGE incurs or suffers a loss that is subject to indemnification
10 under the Stock Purchase Agreement, Oregon Electric will direct Enron to pay the
11 benefit of such indemnity directly to PGE. *See* Oregon Electric/501, Davis/6.

12 Staff discussed immediately above in Condition 20 the issues giving rise to Condition 21.
13 Staff's only additional comment is to note the Applicants failed to provide the valuation data
14 underlying the potential liabilities for which the Applicants are offering the indemnifications.
15 *See* Staff/900, Morgan/6; Staff/200, Morgan/9 12. As such, while staff's Condition 21 provides
16 some protection, ensuring the indemnifications will flow to PGE and not OEUC, there still exist
17 risks surrounding the amount of the liabilities at issue.

17 Condition 22

18 Staff's Condition 22 is found at Staff/801, Conway/10. After further review, staff has
19 slightly revised this condition. The changes are shown in **bold** print:

20 Oregon Electric and PGE agree to submit a final "transition plan" to the
21 Commission within one year of closing. The plan shall detail, **through**
22 **benchmarking review and other analysis**, the areas where efficiencies and/or
23 cost-cutting efforts could occur, **identify process improvement plans**, and will
24 provide annual estimates of the expected savings. (*See* Staff/1000, Durrenberger/3,
25 lines 14-17.)

26 Currently, there is no certainty about how much the OEUC can save in decreasing PGE's
27 cost structure. *See* Staff/1000, Durrenberger/3. Although OEUC consultants have identified
28 potential cost savings, the amount of cost savings will not be known until a top-down review is

1 conducted by OEUC under oversight of the new Board of Directors. *See Id.* The Commission
2 should require OEUC to submit a final transition plan that details areas where efficiencies and
3 cost cutting efforts could occur.

4 Staff and OEUC agree on the first sentence of Condition 22, which provides that OEUC
5 will provide a final transition plan to the Commission within one year of closing. *See* Staff/801,
6 Conway/10; Oregon Electric/501, Davis/6. While OEUC has agreed to submit a final transition
7 plan to the Commission within one year of closing, OEUC’s proposed condition does not detail
8 what will be included in the submitted plan.

9 In its testimony, staff proposed language that would require the final transition plan to
10 detail the areas where efficiencies and cost-cutting efforts could occur, along with annual
11 estimates of expected savings. *See* Staff/801, Conway/10. Similarly, ICNU proposed a
12 condition that would subject PGE to a process improvement and benchmarking review. *See*
13 ICNU/301, Schoenbeck/5.

14 After reviewing ICNU’s testimony and proposed Condition 24 (*see* ICNU/301,
15 Schonebeck/5), staff modifies its Condition 22 to add language that provides more clarity and
16 substance to the requirements of the final transition plan. Namely, staff includes language that
17 provides that the plan will detail, *through benchmarking and other analysis*, the areas where
18 efficiencies and/or cost-cutting efforts could occur, *identify process improvement plans*, and will
19 provide annual estimates of the expected savings. Staff’s proposed Condition 22, as modified
20 based upon ICNU’s proposed language, should be adopted because it adds necessary substance
21 and detail to OEUC’s agreement to provide a final transition plan.

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1 Condition 23

2 Staff's Condition 23 is found at Staff/801, Conway/11. After further review, staff has
3 decided to replace its Condition 23 with OEUC Condition 23. See Oregon Electric/501, Davis/6-
4 7. Thus, staff amends its Condition 23 to as follows:

5 PGE agrees to the following with respect to its non-fuel operation and maintenance
6 (O&M) expenses and capital expenditures:

- 7 a. PGE shall file with its Results of Operations report an O&M expense
8 and capital expenditure update report (OMCE Update). Using
9 individual FERC accounts for O&M (*i.e.*, FERC Accounts 500
10 through 598 and 901 through 923), and Construction Work-in-
11 Progress (CWIP) costs by functional areas, the OMCE Update will
12 compare the actual O&M and capital expenditures for the most recent
13 past year with (a) the current year's budgeted O&M and capital
14 expenditures, and (b) the average of the preceding three calendar
15 years' actual O&M and capital expenditures. The OMCE Update will
16 also compare actual O&M costs by functional area for the most recent
17 past year to the last approved test year revenue requirement. The
18 OMCE Update will include a written narrative description of the
19 reasons for major variances between the compared accounts, including
20 accounting changes and the most recent organization chart for PGE. If
21 requested, PGE shall present the major findings of the OMCE Update
22 at a Commission meeting.
- 23 b. After completing and presenting its third OMCE Update, PGE may
24 petition the Commission to terminate this condition. The Commission
25 shall provide PGE and other interested parties an opportunity to be
26 heard with respect to the termination.

19 Condition 24

20 Staff's Condition 24 is found at Staff/801, Conway/11. After further review, staff has
21 revised this condition (new language is shown in **bold**, deleted language is shown in ~~strikeout~~):

22 Within the first seven years after closing, PGE agrees, if directed by the
23 Commission, to conduct an audit, at its shareholders' expense, using an
24 independent auditor approved by the Commission, ~~to review the company's O&M
25 and/or Capital construction plans and expenditures.~~ **The shareholders will bear
26 the expense of the audit up to \$400,000. This audit will include an
examination that includes, but is not limited to, the following areas:**

- **Strategic and operational planning;**
 - **Budgeting;**
 - **Capital expenditures;**
 - **O&M expenditures;**
 - **Measures of work planned and performed;**
 - **Maintenance planning, performance, and backlogs;**
 - **Performance measurement/Benchmarking; and**
 - **Comparative and trended expenditures and work performance.**
- (Staff/1000, Dirrenberger/5, lines 6-9.)

Staff is concerned with the potential risks that may occur when OEUC implements cost-cutting measures. *See* Staff/300, Durrenberger/6-9; *see also* Staff/1000, Durrenberger/4-5.

Staff's Condition allows the Commission to direct that OEUC hire an independent auditor to exam certain areas of PGE's operations.

OEUC has proposed a similar condition. *See* Oregon Electric/501, Davis/7. OEUC's condition provides that PGE agrees to an independent audit to review PGE's O&M, or capital construction plans and expenditures, or both, within the first seven years after closing, but no sooner than 2007, and that shareholders will bear the expense of the audit up to \$400,000. *See Id;* *see also* Oregon Electric/700, Mcdermott/13.

Staff's recommended Condition also provides for an audit, if directed by the Commission, within the first seven years after closing. However, staff's condition does not unnecessarily limit the possible audit to no sooner than 2007. After reviewing ICNU's testimony and proposed Condition 23 (*see* ICNU/301, Schonebeck/5), staff modifies its Condition 24 to add language that provides more clarity and substance to the requirements of the audit. In addition, Staff modifies its Condition 24 to reflect that shareholders will bear only the expense of an audit up to \$400,000.

Condition 25

Staff's Condition 25 is found at Staff/801, Conway/11. After review, staff has adopted language from ICNU's similar condition to clarify when the condition commences (new language is shown in **bold**, deleted language is shown in ~~strike-out~~). Staff has also decided to accept OEUC's request to eliminate the restriction that distributions first go to pay "direct"

1 operating expenses. *See Oregon Electric/600, Wheeler/15.* Staff’s revised Condition 25 reads as
2 follows:

3 **After closing,** ~~Each~~ PGE distribution to OEUC will be used by OEUC exclusively
4 to pay ~~direct~~ operating expenses and debt service for at least five years and until all
5 of the following conditions are met: (*See Staff/900, Morgan/21, line 9 through*
Morgan/22, line 5.)

- 6 a. The sum of the drawn balances of all PGE’s Secured Revolvers is zero
and there had not been a balance for three months; and
- 7 b. OEUC has paid down at least \$250 million of its outstanding debt as
8 compared to the level of outstanding debt at closing including the catch-
up dividend from PGE.

9 Condition 25 is known as the “cash flow sweep” or “cash sweep” provision and refers to
10 cash being “swept” from PGE to OEUC for a particular purpose. *See Staff/200, Morgan/19 at*
11 *footnote 11.* In this case, the condition is intended to ensure that all available cash not necessary
12 for operations or financing costs is used to liquidate OEUC’s debt. Without this provision, the
13 TPG equity investors would be able to receive dividends paid from PGE to OEUC that OEUC
14 could have otherwise used to pay down its debt. *Staff/200, Morgan/19.*

15 Condition 25 thus requires OEUC to use PGE’s dividend payments, for a period of five
16 years, only to pay operating expenses and debt service and until both (a) PGE’s secured revolver
17 has a zero balance for three months (to the extent one is created) and (b) OEUC has paid down at
18 least \$250 million of its outstanding debt at closing (which will be about \$707 million - *see*
19 *PGE/200, Tinker-Murray-Hager/5*).

20 OEUC has a similar Condition 25. *See Oregon Electric/501, Davis/7.* The only
21 substantive difference between staff’s and OEUC’s condition is found in Section (a). There,
22 OEUC eliminates any reference to a secured revolver, and instead inserts a requirement that the
23 rolling 12-month average of PGE’s unsecured revolvers be less than \$250 million. *Id.*

24 In staff’s opinion, PGE would only need to open a secured revolver account (as
25 contrasted with an unsecured revolver) if PGE’s financial performance was weak. *Staff/900,*
26 *Morgan/22.* As such, Staff requires a “zero” balance on a secured revolver (indicating a

1 financially strong PGE) before OEUC may use PGE’s dividends for other than paying operating
2 expenses and retiring debt.⁶

3 In response, OEUC argues that its condition is preferable merely because it better
4 preserves OEUC’s ability to “take advantage of least-cost financing opportunities and use its
5 revolvers to pay for necessary services.” Oregon Electric/600, Wheeler/16. The correct focus is
6 on the welfare of PGE’s customers, not on OEUC’s ability to take advantage of unspecified and
7 vague “financing opportunities.”

8 Condition 26

9 Staff’s Condition 26 is found at Staff/801, Conway/12 and it reads as follows:

10 No company, entity or person, other than PGE, shall use PGE’s regulated assets as
11 collateral for any loan, guarantee or other such use without prior expressed
12 Commission approval. (See Staff/900, Morgan/22, lines 7-21.)

13 Staff’s condition arises from ORS 757.480. That statute restricts a utility’s ability to
14 encumber its regulated assets without the Commission’s approval. Staff’s Condition 26 tailors
15 the statute to the concerns raised by the proposed acquisition by adding the phrase “guarantee, or
16 other such use.” Staff intends that its condition apply to prevent OEUC from any additional
17 borrowing against PGE’s dividend stream or from offering PGE’s assets as collateral for
18 borrowed funds provided by PGE’s regulated assets. See Staff/900, Morgan/22-23.

19 The Applicants do not offer a counter-proposal to Staff’s Condition 26. See Oregon
20 Electric/501, Davis/7.

21 Condition 27

22 Staff’s Condition 27 is found at Staff/801, Conway/12 and it provides as follows:

23 OEUC shall not re-leverage, i.e. increase the amount of its outstanding long-term
24 debt once such debt has been liquidated, if the increased debt would, or could
reasonably be expected to, bring the consolidated capital structure⁷ below 40%
common equity. (See Staff/900, Morgan/22, lines 23 through Morgan/23, line 6.)

25 ⁶ Staff notes that Mr. Morgan’s testimony erroneously discusses a \$50 million threshold for
unsecured and secured revolvers. As such, staff strikes the following passage from Mr.
26 Morgan’s testimony: Staff/900, Morgan/21, line 30 through Staff/900, Morgan/22, line 6.

⁷ In original language of the condition: The capital structure calculations refer to the OPUC
policy that does not include short-term debt in capital.

1 Condition 27 is meant to address the dangers surrounding OEUC’s highly leveraged
2 capital structure that were previously discussed under Condition 20. The condition prevents
3 OEUC from paying down its debt, which Condition 25 encourages, only to then immediately
4 incur the debt again. *See Staff/900, Morgan/23.*

5 OEUC’s Condition 27 is similar to staff’s condition, with two important differences.
6 First, OEUC substitutes its “GAAP” language for staff’s “or could reasonably be expected to”
7 phrase. *See Oregon Electric/501, Davis/8.* Staff previously explained the reason it prefers its
8 phrase to OEUC’s in its discussion under Condition 16. Staff incorporates that discussion here –
9 in summary, staff’s phrase preserves necessary authority for the Commission to review OEUC’s
10 decision to re-acquire debt after retiring it under Condition 25.

11 Second, OEUC’s Condition 27 lowers the equity threshold level for re-leveraging debt
12 from staff’s 40% to 30%. OEUC offers only vague justifications for lowering the bar for when it
13 can acquire debt after previously paying it off. OEUC says it would like to send a dividend to its
14 members at some point down the road. *Oregon Electric/600, Wheeler/17.* Staff understands and
15 does not oppose this general perspective that investors expect a return on their investment.
16 However, staff does not find OEUC’s statement persuasive for justifying a reduction of the
17 consolidated equity threshold for when debt can be re-acquired from staff’s 40% to OEUC’s
18 undeniably riskier 30%. Staff is also not convinced by OEUC’s dramatic, but unsupported,
19 claim that the difference between 30% and 40% may cause OEUC to prematurely divest its
20 interest in PGE. *See Oregon Electric/600, Wheeler/18.*

21 Condition 28

22 Staff’s Condition 28 is found at Staff/801, Conway/12. After further review, staff has
23 decided to adopt OEUC’s similar Condition 28, with minor changes, as follows (new language is
24 shown in **bold**, deleted language is shown in ~~strikeout~~):

25 **After closing, the TPG entities, in aggregate, TPG Applicants** will not allocate or
26 **direct bill OEUC for any goods, services, supplies or assets in excess of \$5 million**
per year in total until condition number 25 (cash sweep provision) has been
satisfied. (See Staff/900, Morgan/23, lines 8-10.)

1 The only changes from OEUC’s Condition 28 are the addition of the phrases “in
2 aggregate” and “in total.” These changes are meant to clarify that the sum of all allocations and
3 direct billings by “the TPG entities”⁸ to OEUC in a calendar year together do not total more than
4 \$5 million.

5 Condition 29

6 Staff’s Condition 29 is found at Staff/801, Conway/12. After further review, staff has
7 decided to replace its Condition 29 with OEUC’s Condition 29. *See Oregon Electric/501,*
8 *Davis/4.* Thus, staff amends its Condition 29 to read as follows:

9 PGE agrees to work in good faith with Staff and other interested parties to develop
10 and present to the Commission, within 270 days of the closing of the transaction, a
11 billing accuracy SQM consistent with Staff/702. At the time of the presentation to
12 the Commission, parties, including PGE, may present their views to the
13 Commission on the necessity for and content of the SQM.

14 OEUC’s proposed language provides that the parties will work in good faith to develop
15 and present a billing accuracy “Service Quality Measure” (SQM) to the Commission and notes
16 that the parties reserve their rights to present their views on the necessity and content of a billing
17 accuracy SQM.

18 Condition 30

19 Staff’s Condition 30 is found at Staff/801, Conway/12. OEUC does not offer a counter-
20 proposal to Staff’s Condition 30. *See Oregon Electric/501, Davis/8.* The condition reads as
21 follows:

22 Oregon Electric shall provide a report to the Commission, on a semiannual basis,
23 that details the date of each instance the TPG Applicants withheld their consent to a
24 decision of the PGE Board of Directors and names the Consent Right that was
25 triggered. (*See Staff/900, Morgan/25, lines 8-11.*)

26 This condition requires OEUC to report to the Commission, twice a year, the date and
Consent Rights triggered for each instance that the Applicants withheld their consent to a

⁸ By “TPG entities,” staff means each TPG entity that is an applicant, including the Tarrant Partners. *See Staff/801, Conway/12, footnote 2.*

1 decision of the PGE Board of Directors. This condition provides an obligation on the Applicants
2 to alert the Commission on a very broad level (simply the date and Consent Right triggered) of
3 use of the negative consent rights.

4 This condition assumes that the consent rights are triggered at the PGE Board level.
5 However, it may be that some of the decisions could come at the OEUC Board level. *See*
6 *generally* Application at Exhibit 7, pp. 1-3. OEUC/22, Exhibit/7. The operational decisions
7 impacting PGE’s customers should be made at the PGE Board level. However, in the event the
8 Commission seeks a broader report of triggered Consent Rights, the Commission could also
9 consider requesting OEUC to include negative Consent Rights triggered at the OEUC Board
10 level.

11 In Condition 11, staff and OEUC have agreed that OEUC will maintain a record when
12 Applicants use Consent Rights and provide such record to the Commission upon request.
13 Condition 30 affirmatively requires OEUC to report, semiannually, the date and Consent Right
14 triggered, if any, when Applicants use their negative Consent Rights.

15 The Applicants have claimed that a benefit of this transaction would be effective local
16 representation on the PGE Board. *See generally* Application, Exhibit 3, at 3. Oregon
17 Electric/100, Davis/57-58. However, the Applicants retain significant control over the actions of
18 the PGE Board through negative Consent Rights. *See* Application, OEUC/22, Exhibit/7. As
19 OEUC notes, many parties have expressed concern regarding transparency at OEUC. *See*
20 Oregon Electric/500, Davis/25. Staff’s proposed condition 30 increases transparency by
21 requiring OEUC to alert the Commission when Applicants exercise their consent rights. By
22 increasing transparency regarding the use of Consent Rights, Condition 30 also provides the
23 Commission with information that may be pertinent to judging the effectiveness of local
24 representation.

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1 Condition 31

2 Staff's Condition 31 is found at Staff/801, Conway/12-13. After further review, staff has
3 decided to replace its Condition 31 with OEUC's Condition 31. See Oregon Electric/501,
4 Davis/8. Thus, staff amends its Condition 31 to read as follows:

- 5 The following actions shall be reported to the Commission by TPG Applicants or
6 Oregon Electric, as appropriate, within 30 business days after their occurrence:
- 7 a. Any change of control of the General Partner of either of the TPG Applicants.
 - 8 b. Any change in the ownership interest in Oregon Electric or any of the TPG
9 funds investing in Oregon Electric.
 - 10 c. Any amendment to the terms and conditions of Oregon Electric's Operating
11 Agreement.
 - 12 d. Any amendment to the terms and conditions of the Limited Partnership
13 Agreement of either of the TPG Applicants.
 - 14 e. Any designation, appointment, election, removal or replacement of any
15 Member or Manager at Oregon Electric by a vote, approval or consent of a
16 majority of the Members.

17 Condition 32

18 Staff's Condition 32 is found at Staff/801, Conway/13. After further review, staff has
19 decided to replace its Condition 32 with OEUC's Condition 32. See Oregon Electric/501,
20 Davis/8. Thus, staff amends its Condition 29 to read as follows:

21 Beginning twelve months following the closing, Oregon Electric will prepare and
22 make available to the Commission and the public, on a quarterly and annual basis,
23 financial and operating disclosure reports that are equivalent in scope to that of
24 Form 10-Q and Form 10-K reports filed with the U.S. Securities and Exchange
25 Commission. (See Staff/900, Morgan/26, line 22 through Morgan/27, line 7).

26 OEUC's proposed language provides for some transparency and access to financial
information regarding Oregon Electric. Staff accepts OEUC's proposed language to replace its
proposed Condition 32.

27 Condition 33

28 Staff's Condition 33 is found at Staff/801, Conway/13. The Condition reads as follows
29 (as shown by the ~~strikeouts~~, staff has made two edits to correct punctuation and grammar):

30 Until the total consolidated debt at OEUC is less than 60% of total capital, Oregon
31 Electric and PGE shall not, without the prior consent of the Commission, directly
32 or indirectly permit any subsidiaries to, acquire, incorporate or otherwise organize

1 any subsidiary, or enter into substantially new lines of business, which were not in
existence as of the January 1, 2005. (See Staff/900, Morgan/27, lines 12-16.)

2 OEUC proposes a similar Condition 33. See Oregon Electric/501, Davis/8.

3 Both staff and OEUC agree the Commission should have adequate notice of any actions
4 taken by OEUC, PGE and their related subsidiaries to establish substantially new lines of
5 business. See Staff/900, Morgan/27; Staff/1100, Hathhorn/3; Oregon Electric/600, Wheeler/21.
6 The difference between the two conditions is (1) the percentage of consolidated debt below
7 which the condition does not apply (Oregon Electric proposes 70%, 60% for staff), and (2)
8 staff's condition requires the Commission's prior consent, while OEUC's merely requires prior
9 notice to the Commission.

10 OEUC asserts its more generous debt level "will not unnecessarily or unduly restrict
11 Oregon Electric's and PGE's ability to respond to evolving business opportunities." Oregon
12 Electric/600, Wheeler/21. Staff is not persuaded by OEUC's bald statement that staff's
13 condition would unduly restrict OEUC's or PGE's abilities to seize new business opportunities.
14 Further, OEUC's condition is nothing more than a reporting requirement. The risks inherent
15 with this transaction, discussed earlier, especially the amount of debt involved, make it prudent
16 for the Commission to keep control over the actions taken by the companies to expand into new
17 lines of business. Simply stated, staff's condition, requiring the Commission's prior consent,
18 preserves the Commission's authority, OEUC's does not.

19 Condition 34

20 Staff's Condition 34 is found at Staff/801, Conway/13. OEUC has proposed identical
21 language for this condition. See Oregon Electric/501, Davis/9.

22 The Applicants will file a Master Services Agreement, which includes agreed-upon
23 terms and conditions, no later than 30 days after a final order in UM 1121 is issued
approving the transaction. (See Staff/1100, Hathhorn/5, lines 3-15.)

24 **3. Additional Conditions**

25 In addition to staff's recommended conditions, staff has reviewed the parties' surrebuttal
26 testimony, which includes recommended conditions from other parties. While staff did not

1 recommend the conditions listed below, it has reviewed these conditions and agrees that these
2 conditions should be included in a package of conditions that would allow the Commission to
3 approve this transaction.

4 Condition 35

5 PGE will be operated as a corporate and legal entity separate from all of its
6 affiliates as defined by ORS 757.015. See ICNU/301, Schoenbeck/2.

7 Condition 36

8 PGE's revenue requirement shall not include more than 50% of the total fees and
9 costs of PGE's Board of Directors. This does not preclude any party from
10 advocating that ratepayers pay less than 50% of the total fees and costs of PGE's
11 Board of Directors. See ICNU/301, Schoenbeck/4.

12 Condition 37

13 Oregon Electric and PGE commit that a representative from each customer group
14 that is precertified to receive intervenor funding pursuant to OAR 860-012-0100
15 may attend no less than two (2) of the regular meetings of the PGE Board of
16 Directors per year. Attendance of customer groups of any more than two (2) of the
17 regular meetings of the PGE Board shall be allowed at the Board's discretion. At
18 each PGE Board meeting in which a representative of a customer group attends,
19 PGE shall permit each customer group to make a presentation to the Board. See
20 ICNU/301, Schoenbeck/4.

21 Condition 38

22 Oregon Electric and the City of Portland commit to make all reasonable efforts to
23 develop and obtain approval of a modern utility franchise between PGE and the
24 City of Portland within twelve months following the completion of the acquisition.
25 See COP/101, Anderson/3.

26
OTHER MATTERS

1. Likely Outcome should the Commission deny the Application

27 If the Commission does not grant the Applicants' petition to purchase PGE, the most
28 likely scenario is Enron would continue to own the company for a limited period of time.

29 Ultimately, should Enron not seek another buyer for the company, the most likely scenario is

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1 Enron would distribute PGE's stock to Enron's creditors and PGE would once again become a
2 publicly traded, stand-alone company.

3 Enron owns 100% of PGE's issued and outstanding common stock. Enron/1, Bingham/1.
4 Enron filed for Chapter 11 bankruptcy on December 2, 2001. *Id.* The case is currently pending
5 before the United States Bankruptcy Court for the Southern District of New York, Case No. 01-
6 16034(AJG) (Bankruptcy Court). *Id.* at 1-2. While PGE is not itself in bankruptcy, its stock is
7 a major Enron asset of the Enron bankruptcy estate and the shares will be disposed in the manner
8 approved by the Bankruptcy Court. *Id.*

9 The bankruptcy case is extremely complex, as shown by Staff/1400. However, Enron
10 witness Robert S. Bingham provides a good description of both the significant events in the
11 bankruptcy proceeding, as well as the likely future for PGE should the Commission reject the
12 Applicants' petition. Enron's sale of PGE is governed by a Plan approved by the Bankruptcy
13 Court. *Id.* Under the Plan, if the Commission does not approve the sale of PGE to OEUC,
14 Enron may still try to sell PGE to another buyer. If that occurs, then the prospective new buyer
15 would have to gain the Commission's approval for the sale under ORS 757.511.

16 If the Commission rejects the current Application, and if Enron does not sell PGE to
17 another buyer, then the Plan provides for the distribution of Enron's interest in PGE to Enron's
18 creditors. Enron/1, Bingham/4. The distribution of PGE's stock to Enron's creditors would
19 occur through a series of events which may take several years. *Id.* The Commission's authority
20 to oversee the process under ORS 757.511 depends on the mechanism used to distribute the
21 shares. An ORS 757.511 review would be triggered if the shares are distributed directly to
22 Enron's creditors, and one or more creditors receives shares totaling 5% or more of the voting
23 shares of PGE. *See* ORS 757.511, 757.015. It is possible that other mechanisms for distributing
24 the shares would also require the Commission's review. *See generally* Enron/1, Bingham/5-8.⁹

25 ⁹ ORS 757.511 could also be triggered if the PGE shares were initially held in a trust for
26 distribution to Enron's creditors. However, Enron's counsel Mike Morgan stated at the
evidentiary hearings that Enron no longer intends to use a trust to distribute PGE's shares. *See*
Transcript October 20, 2004 at pages 6 – 7 (Mike Morgan statement).

1 Mr. Bingham estimates that the conditions for the stock distribution to commence could occur as
2 early as the last half of 2005. Enron/2, Bingham/5.

3 Should PGE end up as a publicly traded, stand-alone company, the Enron conditions
4 would terminate. Similarly, staff's conditions necessary to recommend the Commission approve
5 the current Application would have no application to PGE as a stand-alone, publicly traded
6 company.

7 **2. The Commission should continue its current policy of viewing a utility's taxes on a stand-**
8 **alone basis**

9 The Commission should continue its current practice of viewing a utility's taxes on a
10 stand-alone basis because it reflects the costs of the utility's regulated operations. *See*
11 Staff/1200, Johnson/1; *see also* Staff/500, Johnson/2-3. The Commission, in addition to most, if
12 not all, other state commissions view a utility's taxes on a stand-alone basis, which protects the
13 utility from the business risks at the parent and subsidiary level. *See* Staff/1200, Johnson/1-2.

14 The Commission should not adopt a true-up mechanism (customers pay only what the
15 utility owes) for taxes because such a mechanism would likely raise PGE's costs due to a
16 probable loss in its currently available accelerated tax depreciation, the loss of which would
17 increase PGE's cost of service because customers would not receive the benefit of accumulated
18 deferred income taxes as a reduction to rate base. *See Id.* at 2-3; *see also* Staff/500, Johnson 2-4.
19 In addition, a true-up mechanism increases the risks that customers may be exposed to the
20 financial impacts (*i.e.* higher rates) of non-normalized weather and hydro conditions. *See Id.* at 3.

21 The Commission should not alter its current policy of viewing a utility's taxes on a stand-
22 alone basis. This policy correctly reflects the costs of the utility's regulated operations and
23 protects customers from potential business risks at the parent and subsidiary level. In addition, a
24 tax true-up mechanism would likely raise PGE's costs due to the loss of its currently available
25 accelerated tax depreciation and, therefore, potentially raise customer rates.

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1 **3. Unlawfulness of CUB's proposed "end game" condition**

2 CUB proposes a condition that gives the City of Portland (or other public entity
3 designated by the City) the option to buy all of PGE's assets, if TPG does not create a publicly-
4 traded corporation through a public stock offering. *See* CUB/300, Jenks-Brown/33; *See also*
5 CUB/325, Jenks-Brown/1 (language of CUB's proposed condition). The price of PGE would
6 apparently be determined through an arbitration process. *See Id.* at 34. In essence, CUB is
7 requesting that the Commission make a decision today about what will be best for PGE's
8 customers and the public generally at some unknown future time.

9 The Commission should not adopt CUB's proposed condition. Besides the serious policy
10 implications raised by making a decision today about what will be best in the future, ORS
11 757.511 does not allow the Commission to expand its authority to pick one possible purchaser
12 over another. For example, the Commission certainly could not require the Applicants to sell
13 PGE's assets to only ABC Corporation. ORS 757.511 allows the Commission to approve or
14 deny applications to acquire PGE but does not allow the Commission to eliminate otherwise
15 qualified future potential buyers.

16 The Commission's role is to provide rate and service regulation for customers of
17 investor-owned public utilities. *See* ORS 756.040; 757.005. While ORS 757.511 permits the
18 Commission to place conditions on the manner in which an applicant will operate a public utility
19 and provide net benefits to the utility's customers, absolutely nothing in the statute suggests that
20 the Commission has the authority to adopt a condition that favors one buyer and eliminates other
21 qualified – and potentially more advantageous - buyers.

22 If any future sale by the Applicant falls within ORS 757.511, or within any authority the
23 Commission has at the time, the Commission will use its authority to protect customers affected
24 by the proposed sale. However, there is nothing in ORS 757.511 that currently gives the

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1 Commission the authority to discriminate against potential qualified buyers and provide that any
2 future sale must be to a public entity only, if there is not a public stock offering.¹⁰

3 This Commission cannot, and should not, determine that it is in the best interests of
4 PGE's customers and the public generally that the City (or its designee) be given an option to
5 buy all of PGE's assets at some unknown future time, if TPG does not create a publicly-traded
6 company through a stock offering. CUB's proposed condition is unlawful and should be
7 rejected.

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19 ¹⁰ CUB's proposed condition also raises the question of whether this Commission can legally
20 bind future commissions and give a public entity a preferential option to buy PGE at the some
21 uncertain future time. CUB's request to bind a future Commission, at the expense of any other
22 qualified buyer, is contrary to the Commission's authority under ORS 756.568, which allows the
23 Commission to rescind, suspend or amend an order at any time. The only potential way that this
24 Commission could bind a future commission would be if the Commission entered into a contract
with a utility or customer group. There is nothing in ORS 757.511 that suggests the conditions
the Commission may impose on an application rise to the level of a contract that a future
Commission may not alter.

25 In addition, CUB's proposed condition raises the question of whether the Commission
26 would commit a regulatory taking by restraining the sale of PGE's assets. In this context, staff is
concerned with the reduction in market value of the public utility, which is certainly probable, if
the Commission limits the market for the resale of PGE.

1 **CONCLUSION**

2 For the reasons stated, staff asks the Commission to deny the Applicants' Application.
3 However, the Commission may find the Application, with staff's conditions, satisfies ORS
4 757.511.

5
6 DATED this _____ day of November 2004.

7 Respectfully submitted,

8 **HARDY MYERS**
9 Attorney General

10
11 _____
12 Michael T. Weirich, #82425
13 Jason W. Jones, #00059
14 Assistant Attorneys General
15 Of Attorneys for the Public Utility Commission
16 of Oregon
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STAFF'S CONDITIONS

(as revised)

1. PGE and Oregon Electric shall maintain separate books and records. All PGE and Oregon Electric financial books and records shall be kept in Portland, Oregon.
2. Oregon Electric and PGE shall exclude from PGE's utility accounts all goodwill resulting from this acquisition.
3. Oregon Electric and PGE shall exclude all costs and fees of the acquisition, including, but not limited to, all costs and fees associated with gaining regulatory approval before the Oregon Public Utility Commission, Nuclear Regulatory Commission, Federal Energy Regulatory Commission, Federal Trade Commission, Securities Exchange Commission, costs and fees associated with forming Oregon Electric, and any banking or financial institution fees associated with the creation of Oregon Electric and the financing and closing of the Acquisition from PGE's utility accounts. Within 90 days following the completion of the transaction, Oregon Electric will provide a preliminary accounting of these costs. Oregon Electric and PGE agree to provide the Commission a final accounting of these costs within 30 days following the completion of the final accounting related to the transaction.
4. Unless such a disclosure is unlawful, Oregon Electric shall notify the Commission of:
 - a. Its intention to transfer more than 5 % of PGE's retained earnings to Oregon Electric over a six-month period, at least 60 days before such a transfer begins.
 - b. Its intention to declare a special dividend from PGE, at least 30 days before declaring each such dividend.
 - c. Its most recent quarterly common stock cash dividend payment from PGE within 30 days after declaring each such dividend.
5. Subsequent to its purchase by Oregon Electric, PGE shall continue to perform under the Service Quality Measures ("SQM"), as set forth in Stipulations for PGE Service Quality Measures UM 814/UM 1121 dated July 13, 2004, for a period of ten full calendar years after the date the current SQM is scheduled to retire. Nothing in any provision of this Stipulation is intended to affect the Commission's authority to directly administer the stated terms of the SQM. Notwithstanding the provisions described in this paragraph, the parties have agreed to replace the current R4 measurement with a CAIDI-related measurement, and further that PGE will maintain records of outages longer than

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three hours. In addition, PGE agrees to work with ICNU to evaluate and, if necessary, develop additional service quality standards related to service to industrial customers.

6. PGE and Oregon Electric shall maintain separate debt ratings and, if more than \$5 million of preferred stock is outstanding, then PGE and Oregon Electric shall maintain separate preferred stock ratings.
7. The Commission or its agents may audit the accounts of Oregon Electric, its affiliates, and any subsidiaries that are the bases for charges to PGE to determine the reasonableness of allocation factors used by Oregon Electric to assign costs to PGE and amounts subject to allocation or direct charges. Oregon Electric agrees to cooperate fully with such Commission audits. (*See Staff/1100, Hathhorn/2, line 20 through Hathhorn/3, line 5.*)
8. Oregon Electric and its affiliates shall not allocate to or directly charge to PGE expenses not authorized by the Commission to be so allocated or directly charged. (*See Staff/1100, Hathhorn/3, lines 6-10.*)
9. PGE shall maintain its own accounting system. PGE and Oregon Electric shall maintain separate books and records, both of which shall be kept in Portland, Oregon. (*See Staff/1100, Hathhorn/3, lines 11-14.*)
10. If the Commission believes that Oregon Electric and/or PGE have violated any of the conditions set forth herein, any conditions contained in other stipulations signed by Oregon Electric and PGE, or any conditions imposed by the Commission in its final order approving the Application (collectively, the "Conditions"), then the Commission shall give Oregon Electric and PGE written notice of the violation.
 - a. If the violation is for failure to file any notice or report required by the Conditions, and if Oregon Electric and/or PGE provide the notice or report to the Commission within ten business days of the receipt of the written notice, then the Commission shall take no action. Oregon Electric or PGE may request, for cause, permission for extension of the ten-day period. For any other violation of the Conditions, the Commission must give Oregon Electric and PGE written notice of the violation. If such failure is corrected within five business days of the written notice, then the Commission shall take no action. Oregon Electric or PGE may request, for cause, permission for extension of the five-day period.
 - b. If Oregon Electric and/or PGE fail to file a notice or written report within the time permitted in subparagraph a. above, or if Oregon Electric and/or PGE fail to cure, within the time permitted above, a violation that does not relate to the filing of a notice or report, then the Commission may open an investigation, with an opportunity for Oregon Electric and/or PGE to request a hearing, to determine the number and seriousness of the violations. If the Commission determines after the investigation and hearing (if requested) that Oregon Electric and/or PGE violated one or more of the Conditions, then the

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Commission shall issue an Order stating the level of penalty it will seek. Oregon Electric and/or PGE, as appropriate, may appeal such an order under ORS 756.580. If the Commission's order is upheld on appeal, and the order imposes penalties under a statute that further requires the Commission to file a complaint in court, then the Commission may file a complaint in the appropriate court seeking the penalties specified in the order, and Oregon Electric and/or PGE shall file a responsive pleading agreeing to pay the penalties. The Commission shall seek a penalty on only one of Oregon Electric or PGE for the same violation.

- c. The Commission shall not be bound by subsection (a) in the event the Commission determines PGE and/or Oregon Electric has violated any of the material conditions, contained herein, more than two times within a rolling 24-month period.
 - d. PGE and/or Oregon Electric shall have the opportunity to demonstrate to the Commission that subsection (c) should not apply on a case-by case basis. (*See Staff/800, Conway/8, line 3 through Conway/9, line 2.*)
11. Oregon Electric shall maintain and provide the Commission unrestricted access to a record of each instance in which TPG Applicants withhold their consent to a decision of the PGE Board of Directors. The record shall detail the basis for the decision, including any governing report or document that memorializes the exercising of the consent rights and shall identify the persons involved in making the TPG Applicant Consent Rights decision. Oregon Electric shall provide the records to the Commission upon request. Nothing in this condition shall be deemed to be a waiver of Oregon Electric's or PGE's right to seek protection of the information. Nothing in this paragraph shall prevent the Commission from disclosing to the public the number of times the TPG Applicants exercised their consent rights within a certain period of time. (*See Staff/900, Morgan/18, line 22 through Morgan/19, line 2.*)
12. Oregon Electric and PGE shall maintain and provide the Commission unrestricted access to all books and records of Oregon Electric and PGE that are reasonably calculated to lead to information relating to PGE, including but not limited to, Board of Directors' Minutes, Board Subcommittee Minutes, and other Board Documents. (*See Staff/900, Morgan/18, line 35 through Morgan/19, line 5.*)¹

¹In Staff/801, staff's conditions 12, 15, and 19 contain sentences that provide that nothing in the condition shall be deemed a waiver of Oregon Electric's or PGE right to seek protection of the information. In Oregon Electric/501, Oregon Electric language does not contain these sentences. However, Oregon Electric includes a General Provision A that provides that nothing in the conditions affects any party's rights to seek protection of information or documents under the Commission normal rules unless expressly waived.

Substantively, staff and the Applicants agree and it is merely a matter of form as to whether condition 12, 15, and 19 contain an explicit recognition of Oregon Electric's or PGE's right to seek protection of the information or whether a general provision is added that provides the same protection for conditions 12, 15, and 19. For purposes of these specific conditions, staff supports a general condition that provides:

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13. PGE and Oregon Electric shall notify the Commission within 30 days of the formation of any subsidiary. Such notice shall include a copy of the business plan and capitalization strategy, as well as any planned or anticipated transactions of the subsidiary with PGE or Oregon Electric as applicable.
14. Oregon Electric and PGE shall provide the Commission access to all books of account, as well as all documents, data and records of their affiliated interests, which pertain to transactions between PGE and all its affiliated interests, unless such transactions are exempt under applicable laws or the Master Services Agreement. (*See Staff/1100, Hathhorn/4, lines 5-11.*)
15. In the event of a dispute between the Commission or Commission Staff and Oregon Electric or PGE regarding a request made pursuant to the Acquisition Conditions, the parties agree that an Administrative Law Judge (ALJ) shall resolve the dispute as follows: (i) within ten (10) business days Oregon Electric or PGE shall deliver to the ALJ the books and records responsive to the request and shall indicate the basis for the objection; (ii) Staff may respond in writing and Oregon Electric and/or PGE may reply to Staff's response; (iii) the ALJ shall review the documents in private; and (iv) the ALJ shall issue a ruling determining whether the documents (a) are reasonably calculated to lead to the discovery of relevant information, and, if so, (b) whether the documents should receive the protection requested. The ALJ shall use this standard whether or not the Commission or Commission Staff is making the request in connection with an open docket. Nothing in this provision shall affect the right of Oregon Electric or PGE to request that the Commission treat the documents as exempt from disclosure to third parties under applicable law.
16. PGE will not make any distributions to OEUC that would, or could reasonably be expected to, cause the common equity portion of PGE's total capital structure to fall below 48 percent. (*See Staff/900, Morgan/19, line 7 through Morgan/20, line 10.*)
 - a. "Total capital structure" is defined as common equity, preferred equity, and long-term debt.
 - b. "Long-term debt" is defined as (1) outstanding debt with an initial term of more than one year plus the sum of committed and drawn balances greater than \$150 million on any of PGE's unsecured revolving lines of credit (Unsecured Revolvers) less any balances related to collateral or security provided to counterparties for power supply and related agreements necessary to meet PGE's retail loads and other firm commitments consistent with those activities recognized in rates; and (2) the sum of committed and drawn balances on PGE's secured revolving lines of credit (Secured Revolvers).

"Nothing in conditions 12, 15, and 19 shall be deemed a waiver of OEUC's or PGE's right to seek protection of the information under the Commission's normal rules."

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- c. A “committed balance” is the sum of commitments used to support any borrowing capacity or other purposes, such as a commercial paper program.
 - d. A “drawn balance” is sum of amounts drawn against the Revolvers.
 - e. Hybrid securities (e.g. convertible debt) will be assigned to equity and long-term debt based on the characteristics of the hybrid security. The Commission, prior to their issuance, will determine the assignment of the equity and debt characteristics.
17. Oregon Electric agrees that the customers shall be held harmless if PGE’s return on common equity and other costs of capital viewed on a stand-alone basis will not rise as a result of Oregon Electric’s ownership of PGE. These capital costs refer to the costs of capital used for purposes of rate setting, avoided cost calculations, affiliated interest transactions, least cost planning, and other regulatory purposes. (*See Oregon Electric/501, Davis/5*).
18. Oregon Electric agrees that the customers of PGE shall be held harmless if PGE’s revenue requirement, viewed on a stand-alone basis, is higher due to Oregon Electric’s ownership of PGE.
19. Oregon Electric and PGE shall maintain (for a rolling five-year period) and provide the Commission unrestricted access to all written information provided to stock or bond rating analysts, which directly or indirectly pertains to PGE or any affiliate that exercises influence or control over PGE. Such information includes, but is not limited to, reports provided to, and presentations made to, stock and bond rating analysts. For purposes of this condition, “written” information includes, but is not limited to, any written and printed material, audio and videotapes, computer disks and electronically-stored information.
20. Oregon Electric agrees to provide a guaranteed rate credit in the amount of \$75 million to PGE’s customers. The amount of this credit will be \$15 million per year for 5 years beginning with 2006. PGE shall establish a balancing account and credit that account with the \$15 million annual credit, beginning on January 1, 2006, and each subsequent January 1, through 2010. The balancing account will accrue interest on the unamortized balance at PGE’s authorized rate of return. Beginning January 1, 2006, PGE will amortize amounts in the balancing account on an equal cents per kWh basis, as a credit to customers’ distribution rates. PGE will exclude all effects of the rate credit from the company’s results of operations and any rate review. (*See Staff/800, Conway/9-14*)
21. To the extent that PGE incurs or suffers a loss that is subject to indemnification under the Stock Purchase Agreement, Oregon Electric will direct Enron to pay the benefit of such indemnity directly to PGE.
22. Oregon Electric and PGE agree to submit a final “transition plan” to the Commission within one year of closing. The plan shall detail, through benchmarking review and other analysis, the areas where efficiencies and/or cost-cutting efforts could occur,

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identify process improvement plans, and will provide annual estimates of the expected savings. (*See Staff/1000, Durrenberger/3, lines 14-17.*)

23. PGE agrees to the following with respect to its non-fuel operation and maintenance (O&M) expenses and capital expenditures:

- a. PGE shall file with its Results of Operations report an O&M expense and capital expenditure update report (OMCE Update). Using individual FERC accounts for O&M (*i.e.*, FERC Accounts 500 through 598 and 901 through 923), and Construction Work-in-Progress (CWIP) costs by functional areas, the OMCE Update will compare the actual O&M and capital expenditures for the most recent past year with (a) the current year's budgeted O&M and capital expenditures, and (b) the average of the preceding three calendar years' actual O&M and capital expenditures. The OMCE Update will also compare actual O&M costs by functional area for the most recent past year to the last approved test year revenue requirement. The OMCE Update will include a written narrative description of the reasons for major variances between the compared accounts, including accounting changes and the most recent organization chart for PGE. If requested, PGE shall present the major findings of the OMCE Update at a Commission meeting.
- b. After completing and presenting its third OMCE Update, PGE may petition the Commission to terminate this condition. The Commission shall provide PGE and other interested parties an opportunity to be heard with respect to the termination.

24. Within the first seven years after closing, PGE agrees, if directed by the Commission, to conduct an audit, at its shareholders' expense, using an independent auditor approved by the Commission. The shareholders will bear the expense of the audit up to \$400,000. This audit will include an examination that includes, but is not limited to, the following areas:

- **Strategic and operational planning;**
- **Budgeting;**
- **Capital expenditures;**
- **O&M expenditures;**
- **Measures of work planned and performed;**
- **Maintenance planning, performance, and backlogs;**
- **Performance measurement/Benchmarking; and**
- **Comparative and trended expenditures and work performance.**

(*Staff/1000, Dirrenberger/5, lines 6-9.*)

25. After closing, each PGE distribution to OEUC will be used by OEUC exclusively to pay operating expenses and debt service for at least five years and until all of the following conditions are met: (*See Staff/900, Morgan/21, line 9 through Morgan/22, line 5.*)

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- a. The sum of the drawn balances of all PGE's Secured Revolvers is zero and there had not been a balance for three months; and
 - b. OEUC has paid down at least \$250 million of its outstanding debt as compared to the level of outstanding debt at closing including the catch-up dividend from PGE.
26. No company, entity or person, other than PGE, shall use PGE's regulated assets as collateral for any loan, guarantee or other such use without prior expressed Commission approval. (*See Staff/900, Morgan/22, lines 7-21.*)
27. OEUC shall not re-leverage, i.e. increase the amount of its outstanding long-term debt once such debt has been liquidated, if the increased debt would, or could reasonably be expected to, bring the consolidated capital structure below 40% common equity. (*See Staff/900, Morgan/22, lines 23 through Morgan/23, line 6.*)
28. After closing, the TPG entities, in aggregate, will not allocate or direct bill OEUC for any goods, services, supplies or assets in excess of \$5 million per year in total.
29. PGE agrees to work in good faith with Staff and other interested parties to develop and present to the Commission, within 270 days of the closing of the transaction, a billing accuracy SQM consistent with Staff/702. At the time of the presentation to the Commission, parties, including PGE, may present their views to the Commission on the necessity for and content of the SQM.
30. Oregon Electric shall provide a report to the Commission, on a semiannual basis, that details the date of each instance the TPG Applicants withheld their consent to a decision of the PGE Board of Directors and names the Consent Right that was triggered. (*See Staff/900, Morgan/25, lines 8-11.*)
31. The following actions shall be reported to the Commission by TPG Applicants or Oregon Electric, as appropriate, within 30 business days after their occurrence:
 - a. Any change of control of the General Partner of either of the TPG Applicants.
 - b. Any change in the ownership interest in Oregon Electric or any of the TPG funds investing in Oregon Electric.
 - c. Any amendment to the terms and conditions of Oregon Electric's Operating Agreement.
 - d. Any amendment to the terms and conditions of the Limited Partnership Agreement of either of the TPG Applicants.
 - e. Any designation, appointment, election, removal or replacement of any Member or Manager at Oregon Electric by a vote, approval or consent of a majority of the Members.

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32. The following actions shall be reported to the Commission by TPG Applicants or Oregon Electric, as appropriate, within 30 business days after their occurrence:
 - a. Any change of control of the General Partner of either of the TPG Applicants.
 - b. Any change in the ownership interest in Oregon Electric or any of the TPG funds investing in Oregon Electric.
 - c. Any amendment to the terms and conditions of Oregon Electric's Operating Agreement.
 - d. Any amendment to the terms and conditions of the Limited Partnership Agreement of either of the TPG Applicants.
 - e. Any designation, appointment, election, removal or replacement of any Member or Manager at Oregon Electric by a vote, approval or consent of a majority of the Members.
32. Beginning twelve months following the closing, Oregon Electric will prepare and make available to the Commission and the public, on a quarterly and annual basis, financial and operating disclosure reports that are equivalent in scope to that of Form 10-Q and Form 10-K reports filed with the U.S. Securities and Exchange Commission. (*See Staff/900, Morgan/26, line 22 through Morgan/27, line 7*).
33. Until the total consolidated debt at OEUC is less than 60% of total capital, Oregon Electric and PGE shall not, without the prior consent of the Commission, directly or indirectly permit any subsidiaries to, acquire, incorporate or otherwise organize any subsidiary, or enter into substantially new lines of business, which were not in existence as of January 1, 2005. (*See Staff/900, Morgan/27, lines 12-16.*)
34. The Applicants will file a Master Services Agreement, which includes agreed-upon terms and conditions, no later than 30 days after a final order in UM 1121 is issued approving the transaction. (*See Staff/1100, Hathhorn/5, lines 3-15.*)
35. PGE will be operated as a corporate and legal entity separate from all of its affiliates as defined by ORS 757.015. *See ICNU/301, Schoenbeck/2.*
36. PGE's revenue requirement shall not include more than 50% of the total fees and costs of PGE's Board of Directors. This does not preclude any party from advocating that ratepayers pay less than 50% of the total fees and costs of PGE's Board of Directors. *See ICNU/301, Schoenbeck/4.*
37. Oregon Electric and PGE commit that a representative from each customer group that is precertified to receive intervenor funding pursuant to OAR 860-012-0100 may attend no less than two (2) of the regular meetings of the PGE Board of Directors per year. Attendance of customer groups of any more than two (2) of the regular meetings of the PGE Board shall be allowed at the Board's discretion. At each PGE Board meeting in which a representative of a customer group attends, PGE shall permit each customer group to make a presentation to the Board. *See ICNU/301, Schoenbeck/4.*
38. Oregon Electric and the City of Portland commit to make all reasonable efforts to develop and obtain approval of a modern utility franchise between PGE and

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the City of Portland within twelve months following the completion of the acquisition.

See COP/101, Anderson/3.