BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION

COMMISSION

In re the Matter of	)	DOCKET NOS. UE-991832/UE-020417
	)	
PACIFICORP d/b/a PACIFIC POWER & LIGHT COMPANY	)	BRIEF OF THE INDUSTRIAL CUSTOMERS OF NORTHWEST UTILITIES AND PUBLIC COUNSEL FOR AN ORDER ON RETROACTIVE RATEMAKING
	)	
Request for an Accounting Order Authorizing Deferral of Excess Net Power Costs	)	
	)	

INTRODUCTION

The Industrial Customers of Northwest Utilities ("ICNU") and the Public Counsel section of the Washington State Attorney General's Office ("Public Counsel") respectfully submit this Brief in the above-captioned Dockets requesting that the Washington Utilities and Transportation Commission ("WUTC" or the "Commission") determine as a matter of law that deferred accounting may only commence prospectively after entry of a Commission order that: 1) approves the creation of a deferred account; and 2) establishes an amortization mechanism describing to ratepayers how the costs may be recouped through tariffed rates. PacifiCorp (or the "Company") has requested that the Commission approve deferral of excess net power costs beginning June 1, 2002. Allowing recovery of costs in deferred accounts prior to Commission authorization of that deferral would violate Washington's prohibition against retroactive ratemaking, the filed rate doctrine, and the constitutional prohibition against deprivation of property without due process.

This Brief addresses only the narrow issue of application of the doctrine of retroactive ratemaking to deferred accounting, and does not address or waive any other

legal issues or arguments in this proceeding. Public Counsel and ICNU will argue later in this proceeding that PacifiCorp's five-year rate plan ("Rate Plan") prohibits any recovery of excess net power costs.

BACKGROUND

On November 24, 1999, PacifiCorp filed certain tariff revisions in Docket No. UE-991832 designed to increase general rates for electric service by approximately $25.8 million over two years. In June 2000, PacifiCorp, ICNU, Public Counsel and the other parties to the proceeding submitted two stipulations ("Stipulations") to the Commission resolving the contested issues in Docket No. UE-991832. The Stipulations proposed a five-year Rate Plan designed to provide rate stability for customers and allow PacifiCorp to gradually increase rates during the first three years of the Rate Plan. The five-year Rate Plan also allowed PacifiCorp to retain significant cost savings, including savings from the ScottishPower/PacifiCorp merger and the Company's transition plan. On August 9, 2000, the Commission approved the Stipulations. WUTC v. PacifiCorp, Docket No. UE-991832, Third Suppl. Order (Aug. 9, 2000) ("Third Supplemental Order"). PacifiCorp has increased rates twice pursuant to the terms of the Rate Plan (3% on January 1, 2001 and 3% on January 1, 2002). WUTC v. PacifiCorp, Docket No. UE-991832, Fourth Suppl. Order (Dec. 27, 2000); WUTC v. PacifiCorp, Docket No. UE-991832, Sixth Suppl. Order (Dec. 21, 2001).

On April 5, 2002, PacifiCorp filed a petition, assigned Docket No. UE-020417, for an order authorizing deferral of excess net power costs ("Application"). In the Application, the Company proposed to defer the difference between actual net power costs incurred each month and the level of power costs currently assumed in retail

rates to Washington customers. Application at 14. The Company proposed to begin to defer these amounts on June 1, 2002. Id. Since retail rates are set pursuant to the Rate Plan Stipulations, which do not identify the underlying level of power costs to be included, the Company proposed to use the monthly level of power costs submitted by the Company in its prefiled testimony in Docket No. UE-991832. Id. at 14, Appendix A. The deferrals would continue until the earlier of: 1) twelve months (through May 31, 2003); or 2) such time as the Commission approves a power cost adjustment mechanism or similar form of relief. Id. at 14-15. Based on its forecasts, PacifiCorp estimated the deferrals would total approximately $12.7 million over the twelve-month period. Id. at 15, Appendix A. PacifiCorp acknowledged that less-than-full recovery of these costs would be appropriate because the Rate Plan limits changes in the Company's rates through December 31, 2005. Id. at 12.

PacifiCorp did not propose a mechanism for recovering its deferred costs, but promised to do so in a separate filing no later than September 30, 2002. Id. at 13. The Company did mention possible forms of relief, such as a power cost adjustment mechanism, a temporary power cost surcharge, and a power cost offset against rate credits currently provided to Washington customers. Id. at 14.

On May 10, 2002, ICNU filed a petition for leave to intervene in Docket No. UE-020417. On July 12, 2002, the Commission issued an order consolidating the two dockets. WUTC v. PacifiCorp, Docket Nos. UE-991832/UE-020417, Order of Consolidation and Notice of Prehearing Conference at 2 (Aug. 6, 2002). The Commission granted ICNU's intervention on August 21, 2002. WUTC v. PacifiCorp, Docket Nos. UE-991832/UE-020417, Second Suppl. Order (Aug. 21, 2002).

ARGUMENT

Washington law precludes a utility from deferring any costs prior to the Commission's approval of the deferred account and the adoption of a cost recovery mechanism. Only affirmative Commission approval would legally permit PacifiCorp to commence deferrals, and even then the Company may only defer those amounts prospectively. Charging customers for costs deferred before these affirmative Commission actions would violate: 1) the common law prohibition against retroactive ratemaking embraced by the WUTC, the Washington courts, and the U.S. Supreme Court; 2) the filed rate doctrine, as codified at RCW § 80.28.050; and 3) the prohibitions in the Washington and United States Constitutions against deprivation of property without due process.

In general, the Commission must enter an order identifying the forward costs, if any, that should be recoverable by PacifiCorp *and* provide in the Company's tariffs the formula that will be applied to determine the amounts recoverable in order to avoid retroactive ratemaking. Nevertheless, if the Commission determines certain costs are appropriate for deferral and allows accounting of those costs without defining the precise formula or mechanism for that recovery, then deferred accounting should begin on the date of entry of that order, not on June 1, 2002, as PacifiCorp requests.

I. Recovery of Costs Deferred Prior to Commission Approval of the Deferred Account Would Violate Washington's Prohibition on Retroactive Ratemaking

Under Washington law, the Commission is charged with setting rates on a prospective basis. The Commission is empowered to order the just and reasonable rates "to be *thereafter* observed and in force." RCW § 80.28.020 (emphasis added); Re Puget

Sound Energy ("PSE"), Docket No. UE-010410, Order Denying Petition at 2 (Nov. 9, 2001). Washington courts and the Commission have interpreted this statutory mandate to set rates on a prospective basis as prohibiting retroactive ratemaking. Standard Oil Co. of Cal. v. Dep't of Pub. Works, 53 P.2d 318, 319, 185 Wash. 235, 238 (1936); Re PSE, Docket No. UE-010410, Order Denying Petition at 2. The Commission has recognized that basic ratemaking principles, including the ban on retroactive ratemaking, apply to deferred accounting. Re PSE, Docket No. UE-010410, Order Denying Petition at 2.

> The Commission has described retroactive ratemaking as follows:
>
> [Retroactive ratemaking involves] surcharges or ordered refunds applied to rates which had previously been paid, constituting an additional charge applied after the service was provided or consumed. The evil in retroactive ratemaking as thus understood is that the consumer has no opportunity prior to receiving or consuming the service to learn what the rate is or to participate in a proceeding by which the rate is set.

WUTC v. Puget Sound Power and Light Company ("PSP&L"), Docket No. U-81-41, Sixth Suppl. Order at 17-18 (Dec. 19, 1988). Prospective ratemaking embodies sound public policy and ensures that: 1) customers pay for their own service, not for past deficits or services rendered to other customers; 2) utilities cannot exploit the regulatory process to extract a guarantee, rather than an opportunity, for a fair rate of return; and 3) utilities retain incentives to manage their resources efficiently. Leonard Goodman, The Process of Ratemaking 166 (1998). The prohibition on retroactive ratemaking also protects the utility from returning its previously earned profits. Bd. of Commrs v. N.Y. Tel. Co., 271 U.S. 23, 31 (1926) ("N.Y. Tel. Co."). PacifiCorp's Application seeks to contravene the policy of prospective ratemaking by changing the past effect of the

Company's rates, contrary to the terms of the rates in effect at the time consumers used the electricity.

A. The Prohibition on Retroactive Ratemaking Ensures that Customers Do Not Pay For Past Services and Receive Advance Notice of All Rate Changes

Unless the Commission has established a deferred account or authorized an interim rate increase, customers have a right to assume that the rates in effect when they utilize their electric service are the final rates. Electric utilities are not permitted to reach back in time to alter the past by changing past rates charged to customers. Re PSE, Docket No. UE-010410, Order Denying Petition at 2. Similarly, future rates cannot be adjusted to allow the utility to recover the costs of past services. Id. Finally, retroactive deferred accounting and recovery will create disparate classes of ratepayers, including a class of new customers who will be charged to cover costs incurred by the Company prior to the date those customers began to receive service. In effect, those customers will be billed for the services that others received.[1/]

Under PacifiCorp's proposal, customers will end up paying more in future rates for service provided in June, July and August than the lawfully established rate in effect for those months. Essentially, PacifiCorp seeks to inappropriately impose costs on future ratepayers for the difference between the lawfully established rate and the amount, if any, that is deferred.

PacifiCorp may argue that rate recovery is not retroactive because no past bills would be changed; bills will only increase prospectively to reflect the deferred costs

[1/] Legal claims such customers may have against the Company or the Commission on this basis are beyond the scope of this Brief.

once the Commission approves the deferral and the recovery mechanism. In a previous case, the Commission dismissed this argument as mere "semantics." Re PSP&L, Cause No. U-79-73, Order at 3 (Dec. 31, 1979). The Commission rejected PSP&L's argument that past bills can "be made up on the basis of tariffs approved by the Commission. . . ." Id. Under PacifiCorp's proposal, future bills will rise based on excess costs incurred in providing *past* service, from June 1, 2002, forward to the date of entry of an order allowing such recovery, if any. This amounts to inappropriately charging future ratepayers for service provided to past ratepayers.

PacifiCorp's proposal does not provide customers with notice that their rates did not fully compensate the Company. Under PacifiCorp's proposal, customers are now being, and have been, provided service at a rate higher than their current charges, these higher costs to be surcharged on future bills. Customers have had no notice of the changes and have no way to learn exactly what the actual rate is, and no way to review and participate, via the Commission, in the proceeding by which the rate is set prior to PacifiCorp's requested date of initiating deferrals. Without notice of rates, customers cannot make decisions regarding their usage of the service, level of conservation, or otherwise respond to price signals. This is precisely the state of affairs the Commission has consistently prohibited. Re PSE, Docket No. UE-010410, Order Denying Petition at 2-3; Re PSP&L, Cause No. U-79-73, Order at 3; WUTC v. PSP&L, Docket No. 81-41, Sixth Suppl. Order at 18.

B. The Rule Against Retroactive Ratemaking Prevents Utilities From Using Future Rates as a Method to Ensure Stockholder Investments

The rule against retroactive ratemaking prohibits incorporation of past profits or losses into future rates and prevents "the Commission from authorizing or requiring a utility to adjust current rates to make up for past errors in projections." Re PSE, UE-010410, Order Denying Petition at 2 *quoting* Town of Norwood v. FERC, 53 F.3d 377, 381 (D.C. Cir. 1995). The rule provides the utility with an opportunity to earn its authorized rate of return, but prohibits the Commission from adjusting rates to guarantee any particular level of financial performance. Re GTE Northwest, Docket No. UT-910499, Sixth Suppl. Order at 6 (Feb. 11, 1994); N.Y. Tel. Co., 271 U.S. at 31. Retroactive ratemaking shifts the risk that the utility will not earn its authorized rate of return from the utility to customers. N.Y. Tel. Co., 271 U.S. at 31; Re PSE, UE-010410, Order Denying Petition at 2.

PacifiCorp seeks to defer excess power costs incurred, due to adverse market and weather conditions beginning June 1, 2002. In other words, PacifiCorp is effectively asking the Commission to put a mechanism in place that will adjust future rates to make up for past errors in projections and to guarantee PacifiCorp a specific level of financial performance. If utilities are authorized to commence deferrals prior to a Commission order, they will have less incentive to operate in an efficient and cost-effective manner. PacifiCorp could choose any past time period when the Company did not meet its authorized rate of return and request a deferred account for those costs that exceeded projections.

PacifiCorp's request is particularly egregious because the Company is requesting that Washington ratepayers make up the difference between past forecasts and past conditions without proposing a specific recovery methodology. Unlike power cost adjustment mechanisms or deferrals the Commission has historically approved, PacifiCorp's Application does not include a methodology that would guide or direct the Commission in determining rates. Instead of proposing a recovery methodology, PacifiCorp focuses solely on how to adjust its rates to pass on cost increases that have allegedly occurred since the Company's last rate case.

C. The Narrow Exceptions to the Rule Against Retroactive Ratemaking Do Not Apply in this Case

Washington courts and the Commission have created narrow exceptions to the rule against retroactive ratemaking, none of which apply in this case. Washington courts have allowed retroactive ratemaking when necessary as an exercise of the police power to "safeguard a vital interest of the people." Hearde v. City of Seattle, 611 P.2d 1375, 1377, 26 Wash. App. 219, 222 (1980). In addition, the Commission has found that incorporating an element of historical cost as a component of a cost adjustment mechanism does not make a rate retroactive. WUTC v. PSP&L, Cause No. U-81-41, Sixth Suppl. Order at 18. Finally, the Commission has also allowed recovery of past expenses on "rare occasions . . . where doing so [was] consistent with the public interest and sound regulatory theory." Id. at 19.

PacifiCorp's current request violates the prohibition against retroactive ratemaking and does not fall under any of the narrow exceptions created by the courts or the Commission. PacifiCorp has not alleged that deferral is necessary to safeguard a vital

interest of the people. Furthermore, the Commission already determined PacifiCorp's appropriate level of power cost recovery in the Company's last general rate case. It is not consistent with the public interest and sound regulatory theory to increase that level of recovery through deferred accounting.

The Commission previously authorized Avista Corporation ("Avista") to defer amounts incurred prior to the date of the Commission order approving the deferral; however, the unique circumstances in those proceedings do not apply to PacifiCorp's request. On June 22, 2000, Avista requested authorization to defer certain power costs effective July 1, 2000. Re Avista, Docket No. UE-000972, Order Granting Deferral Of Power Cost Expenses Pending Demonstration of Prudence (Aug. 9, 2000). The Commission approved Avista's request on August 9, 2000. Id. The Commission issued this order over the objections of Public Counsel and ICNU, but made its approval subject to a number of conditions, including a determination that recovery of the costs through a deferral mechanism was appropriate. Id. In other words, in approving Avista's deferral, the WUTC explicitly reserved judgment on whether deferred accounting was an appropriate cost-recovery mechanism. In doing so, the Commission allowed the parties the opportunity to argue whether deferred accounting constitutes retroactive ratemaking at a later point in the proceeding.

The Commission ultimately authorized Avista to recover a portion of the deferred costs by approving a series of complex, multi-party settlements that resolved a general rate case, a request for interim rate relief, and the prudence review of the deferred costs. Re Avista, Docket Nos. UE-011514/UE-011595, Fourth Suppl. Order (March 4, 2002); Re Avista, Docket No. UE-011595, Fifth Suppl. Order (June 18, 2002). These

settlements resolved a wide variety of issues, some of which were related to Avista's deferred costs and others that were not.

As a result of these settlements, however, the parties never litigated, and the Commission never considered, the retroactive ratemaking issue. Instead, the parties that opposed Avista's recovery of the deferred amounts reserved their arguments in order to support the comprehensive settlement. The Commission should not penalize the parties who compromised their positions in favor of settling a wide range of issues by treating the Avista proceeding as precedent. The Commission has recognized that, except when expressly provided, orders accepting settlement agreements do not "constitute precedent for any purpose except the principles that the Commission encourages parties to disputes before it to consider settlements." WUTC v. Int'l Pac., Inc., Docket No. UT-911482, Ninth Suppl. Order (Jan. 23, 1995); WUTC v. US Ecology, Docket Nos. UR-950619/UR-950620, Sixth Suppl. Order at 6 (Dec. 6, 1995). To deviate from this policy in this proceeding will discourage settlement in the future. Thus, the Commission's action in the Avista proceeding should have no bearing on PacifiCorp's request.

II. Deferral Prior to Commission Approval Would Violate the Filed Rate Doctrine, Codified at RCW § 80.28.050

The filed rate doctrine declares that the only lawful rate a regulated entity may charge is the filed rate approved by the Commission. Ark. La. Gas Co. v Hall, 453 U.S. 571, 577 (1981) ("Arkansas Gas"); Tex. & Pac. Ry. v. Abilene Cotton Oil Co., 204 U.S. 426 (1907). Under the filed rate doctrine, "[n]o court may substitute its own judgment on reasonableness for the judgment of the Commission," and, "[e]xcept where

the Commission permits a waiver, no regulated seller of [energy] may collect a rate other than the one filed with the Commission." Arkansas Gas, 453 U.S. at 577.

Washington law incorporates the filed rate doctrine into the regulatory process. Utilities must file with the Commission tariffs "showing *all rates and charges* made, established or enforced, or to be charged or enforced." RCW § 80.28.050 (emphasis added). As the Washington Supreme Court has noted, the filed rate doctrine serves two purposes: 1) to preserve the Commission's primary jurisdiction to determine the reasonableness of rates; and 2) to ensure that regulated entities charge "only those rates approved by the [Commission]." Tenore v. AT&T Wireless Servs., 962 P.2d 104, 108, 136 Wash. 2d 322, 331-32 (1998).

PacifiCorp filed its request to establish a deferred account on April 5, 2002, proposing to begin deferring excess power costs as of June 1, 2002. Application at 1. PacifiCorp's Application did not seek to change rates, but requested that the Commission approve a deferred account for the Company. PacifiCorp's request to commence deferrals does not create a new filed rate since the Commission has taken no action to alter PacifiCorp's rates or permit deferrals; therefore, the lawfully established rate remains unchanged since the Commission last adjusted PacifiCorp's rates. Re PacifiCorp, Docket No. UE-991832, Sixth Suppl. Order (Dec. 21, 2001). Any rate increase based on costs incurred prior to a Commission order authorizing a deferred account would violate RCW § 80.28.050 and the filed rate doctrine.

The rationale of the filed rate doctrine can also be seen in Washington's requirement of statutory notice of tariff changes. Before any rate change may take effect, thirty days' notice of the changes must be given to the Commission and the public,

plainly stating the changes. RCW § 80.28.060. Customers are entitled to know the rates that they are being charged. PacifiCorp's proposal to collect deferred costs from June 1, 2002 until the time the Commission approves the deferral would contravene this basic principle of Washington law. Tenore, 962 P.2d 104 at 108, 136 Wash. 2d at 331-332; Arkansas Gas, 453 U.S. at 578-79.

III. Recovery of Cost Deferred Prior to Commission Approval Would Violate Customers' Right to Due Process

Setting rates too low for a utility to have an opportunity to earn a reasonable rate of return violates the Fifth and Fourteenth Amendments to the United States Constitution by depriving the utility of property without just compensation or due process of law. U.S. Const. amend. XIV § 1; N.Y. Tel. Co., 271 U.S. at 31. The Washington Constitution also incorporates due process protections. Wash. Const. art I § 3. Past profits in excess of the authorized rate of return cannot be used to justify confiscatory rates for the future. Los Angeles Gas Co. v. R.R. Comm'n, 289 U.S. 287, 313 (1933). By the same token, past losses (or earning below the authorized rate) cannot be used to justify a retroactive rate increase. Galveston Elec. Co. v. Galveston, 258 U.S. 388, 395 (1922). To impose such a rate increase would deprive customers of their property (money) in violation of due process, just as the confiscatory rates would deprive the utility of its property. As one court put it, "The commission has the authority to determine the rate *to be charged* . . . . It may not, however, redetermine rates already established and paid without depriving the utility (or the consumer if the rates were originally too low) of his property without due process." State ex rel. Util. Consumers

Council of Mo., Inc. v. Pub. Serv. Comm'n, 585 S.W.2d 41, 58 (Mo. 1979); Re Cent. Vt. Pub. Serv. Corp., 473 A.2d 1155, 1158 (1984).

Notice and an opportunity to respond are essential components of due process. In the context of utility ratemaking, "due process requires that the basis advanced for the change be set out in sufficient detail to permit those affected to make a meaningful response." N. Cal. Power Agency v. Morton, 396 F. Supp. 1187, 1193 (D.D.C. 1975). Were the Commission to allow PacifiCorp to retroactively recover past excess net power costs prior to an order authorizing deferral, customers' due process rights would have been violated because they were denied notice and an opportunity to respond to PacifiCorp's Application. Morton, 396 F. Supp. at 1193; Util. Consumers Council of Mo., Inc., 585 S.W.2d at 58. The Commission should protect customers' due process rights by limiting any deferral to commencement on the date of the order authorizing deferrals and by evaluating the assumptions, data and conclusions advanced by PacifiCorp regarding the recovery mechanism.

CONCLUSION

A fundamental feature of the regulatory scheme framed by the Washington legislature, and consistently articulated by the Commission in its orders, is that customers must be able to determine the cost of electricity at the time of purchase. Washington law requiring ratemaking to be prospective, tariffs to be filed with the Commission, and only published rates to be charged all reflect the basic principle that current rates cannot be adjusted to incorporate past loses or profits. Likewise, PacifiCorp's lawfully established rates fully compensate the Company for the service it has provided and cannot be changed without Commission approval. The Commission

should not permit changes to the amount charged for service until such time as the Commission approves (if it does)[2/] a deferral account and recovery mechanism. Unless and until the Commission takes these affirmative measures, customers should legitimately assume that payments made for bills received "close the book" on their summer service. Deferring costs prior to Commission approval for past services is contrary to Washington law and WUTC precedent.

[2/] Public Counsel and ICNU will argue later in this proceeding that the Rate Plan prohibits any recovery of excess power costs by PacifiCorp.

WHEREFORE, ICNU and Public Counsel respectfully requests that the Commission issue an order stating that as a matter of law it may not allow PacifiCorp to account for and defer alleged excess net power costs until, and unless, the Commission approves a deferral account and establishes an appropriate recovery mechanism to be reflected in tariffed rates.

Dated this 27th day of August, 2002.

Respectfully submitted,

DAVISON VAN CLEVE, P.C.

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that I have this day served the foregoing Brief of the Industrial Customers of Northwest Utilities and Public Counsel for an Order on Retroactive Ratemaking upon each party on the official service lists by causing the same to be mailed, postage-prepaid, through the U.S. Mail. Dated at Portland, Oregon, this 27th day of August, 2002.

_\s\Margaret A. Roth_____
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