IN THE SUPREME COURT OF THE STATE OF OREGON

FRANK GEARHART; PATRICIA MORGAN; KAFOURY BROTHERS, INC.,

Petitioners,
Petitioners on Review

and,

UTILITY REFORM PROJECT

Petitioner,

v.

PUBLIC UTILITY COMMISSION OF OREGON and PORTLAND GENERAL ELECTRIC COMPANY,

Respondents,
Respondents on Review,

FRANK GEARHART; PATRICIA MORGAN; KAFOURY BROTHERS, INC.,

Petitioners,
Petitioners on Review,

and,

UTILITY REFORM PROJECT,

Petitioner,

v.

PUBLIC UTILITY COMMISSION OF OREGON and PORTLAND GENERAL ELECTRIC COMPANY,

Respondents,
Respondents on Review.

Continued…

Public Utility Commission of Oregon
Nos. 08487; 09093

Court of Appeals No. A140317

Supreme Court No. S061517 (Control)

FRANK GEARHART; PATRICIA MORGAN; KAFOURY BROTHERS, INC.,

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Respondents,
Respondents on Review,

Continued…

BRIEF ON THE MERITS OF RESPONDENT ON REVIEW PUBLIC UTILITY COMMISSION OF OREGON

Judicial Review of the Final Order of the Public Utility Commission of Oregon

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BRIEF ON THE MERITS OF RESPONDENT ON REVIEW PUBLIC UTILITY COMMISSION OF OREGON

INTRODUCTION

This case—a protracted saga that now spans two decades—arises from a rate order that the PUC issued after PGE retired its Trojan Nuclear Power Plant in 1993. Because of costly and recurrent maintenance and repair problems, PGE decommissioned Trojan that year, 17 years after it had opened and well before the utility had recovered its initial investment in it. In 1995, the PUC issued a rate order that allowed PGE to recover most of its remaining investment in the retired plant and to earn a return on that investment. Groups representing utility consumers challenged that order and, in 1998, the Court of Appeals held that the PUC had correctly allowed PGE to recover the principal amount of its investment, but had erroneously allowed the utility also to earn a profit on the retired facility. Further litigation and appeals (including one foray to this court) has focused on whether customers who had paid rates set by the erroneous order between the years 1995 and 2000 were owed a remedy, and, if so, what that remedy should be. That litigation established that the PUC should address those questions on remand.

And that is what the PUC has done. In the order now on review, the PUC analyzed the effects of the erroneous 1995 rate order and required PGE to issue a refund to customers. The 106-page order, and the proceedings that led to it,

represent a comprehensive and exhaustive effort by the commission to accurately analyze the effect the order had on PGE's customers, to return the parties to the position they would have occupied had the PUC not made the mistake, and to bring an end to twenty years of litigation.

QUESTIONS PRESENTED AND PROPOSED RULES OF LAW

First Question Presented

To determine the extent to which PGE's customers were harmed by its erroneous 1995 rate order, the PUC compared the rates that customers actually paid between 1995 and 2000 with the rates the PUC would have set if it had not erroneously allowed PGE to recover a profit. Was that a lawful way to measure the harm caused by the order?

First Proposed Rule of Law

The PUC lawfully measured the harm to PGE's customers by comparing the rates that customers actually paid with the rates the PUC would have set if it had not erroneously allowed PGE to recover a profit. The PUC's initial erroneous conclusion that PGE was entitled to recover a profit had directly influenced several of the factors that the PUC had used in 1995 to determine what rates were fair and reasonable. Determining the effect of its error thus required the PUC to examine how the error influenced its analysis and reconsider the rates it would have set in 1995 but for its error.

Second Question Presented

In reconsidering what rates it would have set in 1995 if it had not erroneously allowed PGE to earn a profit on its investment in Trojan, the PUC determined that it would have allowed PGE to recover only its undepreciated capital investment—*i.e.*, only the *principal*, without earning a profit—over ten years. Because money recovered in the future is worth less that the same amount of money in the present, the PUC also would have allowed sufficient interest so that PGE would recover the principal's full present value—*i.e.*, interest sufficient to reflect the "time value" of money. Is the assumption that PGE would have been entitled to interest on its Trojan investment consistent with the Court of Appeals' 1998 conclusion that PGE was not entitled to earn a "return on" its investment?

Second Proposed Rule of Law

The PUC's order complies with the Court of Appeals' 1998 holding. The Court of Appeals concluded that PGE could recover its principal investment but that ORS 757.355 prohibited PGE from earning a *profit* on that investment. The court did not hold that the statute precluded PGE from earning sufficient interest to cover the time value of the principal.

Third Question Presented

Did the PUC have authority to re-examine the rates it would have set and to order PGE to refund $33 million to customers?

Third Proposed Rule of Law

The PUC's inquiry and analysis into the rates it would have set in 1995 but for its error, and the refund it ordered to return the parties to the positions they would have been in but for the error, are within its authority under ORS 756.040 to "do all things necessary" to protect customers from "unjust and unreasonable exactions."

Fourth Question Presented

Did the PUC violate the rule against retroactive ratemaking by re-examining the rates it would have set in 1995 but for its error, or by ordering PGE to issue a refund to customers?

Fourth Proposed Rule of Law

The PUC may not engage in retroactive ratemaking by adjusting future rates in an attempt to "make up" for a utility's anticipated profits or losses in previous rate periods, but that is not what it did here. The PUC did not set future rates at all. Instead, it used its ratemaking authority and expertise to measure the harm caused by its erroneous 1995 order. In issuing a refund, it did not set rates, nor did it consider PGE's past profits or losses. Instead, it was redressing the harm caused by the PUC's own legal error in an order that was timely appealed and remanded.

SUMMARY OF ARGUMENT

The basic problem that the PUC confronted on remand was that in 1995 it had issued a rate order, based on a mistaken interpretation of ORS 757.355, that erroneously allowed PGE to recover a profit on its investment in the Trojan Nuclear Plant. The PUC's task on remand, therefore, was to determine whether PGE's customers were harmed by the 1995 rate order and, if so, what remedy the commission could provide. To determine the effect of the erroneous order on PGE's customers, the commission compared the rates that the customers *actually* paid under the 1995 order with the rates that the customers *would* have paid if the PUC had not mistakenly interpreted ORS 757.355 when it issued the order. The results of that comparison are dispositive of nearly all the issues before this court.

Two findings, in particular, are crucial. First, after identifying the ways that its erroneous interpretation of ORS 757.355 had affected its original rate analysis, the commission made a significant, if somewhat counter-intuitive, determination: If, back in 1995, the commission had correctly interpreted ORS 757.355 to prohibit PGE from earning a profit on its Trojan investment, PGE's customers actually would have paid somewhat *higher* rates during the period from April 1995 to September 2000. That is a reflection of the fact that the PUC's error had simultaneously influenced several different aspects of its 1995 rate analysis. The most obvious effect was to allow PGE to include

Trojan in its rate base and thus to recover a profit. But the error also affected the PUC's 1995 analysis in ways that favored PGE's customers – namely, by extending the time period over which PGE could recover its Trojan investment and by increasing the PUC's estimate of the costs of closing the plant. Correcting the error, therefore, would have required multiple adjustments—allowing PGE to recover only its principal without a profit, obviously, but also reducing the number of years over which PGE would recover the principal (and thus increasing initial rates), as well as reducing the PUC's estimate of the costs to ratepayers of shutting down the plant. The net effect of all of those adjustments on rates between 1995 and 2000 was essentially a wash. For that reason, the PUC concluded that inclusion of Trojan in rate base had not rendered the rates during the period from 1995 to 2000 unjust or unreasonable.

Second, the PUC found that although its erroneous interpretation of ORS 757.355 had not adversely affected the rates that PGE's customers paid between 1995 and 2000, the error *did* ultimately harm PGE's customers. In October 2000, PGE, PUC staff and the Citizen's Utility Board reached a settlement intended to resolve the Trojan dispute. Under that settlement, which the PUC approved, the parties agreed that PGE's entire remaining investment in Trojan would be offset against certain credits PGE owed to ratepayers; Trojan was thus removed from PGE's books and no longer factored in PGE's rates. That solved the issued prospectively, but it failed to account a particular

consequence of the erroneous 1995 order: Had it not been for the erroneous analysis in the 1995 rate order, the PUC would have issued a rate order permitting PGE to recover its Trojan costs more quickly than it had been. As a result, the amount of PGE's remaining unrecovered Trojan investment in October, 2000—when PGE, PUC staff, and CUB reached a settlement and agreed to offset that amount—was greater than it otherwise would have been. For that reason, the PUC concluded that PGE should be required to pay a $33 million refund to customers. The amount of that refund reflected the difference between PGE's remaining investment in Trojan when it entered the 2000 settlement and what that amount would have been if Trojan had been excluded from PGE's rate base originally.

In a nutshell, then, the PUC's order on remand *returns the utility and its customers to the position that each would have been in had the PUC not erroneously allowed PGE to recover a profit on Trojan to begin with.* The order thus comports with the PUC's fundamental statutory obligations to set fair and reasonable rates, balancing the needs of customers and the utility, and to protect customers from unjust and unreasonable exactions.

On review, both Utility Reform Project ("URP") and Class Action Plaintiffs ("CAPs") contend that the PUC exceeded its authority in issuing the order, but the various arguments they marshal in support of that proposition are without merit. Petitioners rely heavily on the assumption that the Court of

Appeals previously had held that the *rates* in effect between 1995 and 2000 were unlawful. As the Court of Appeals' majority opinion correctly concluded in this case, however, that is not accurate. In *Citizens' Utility Board of Oregon v. Public Utility Commission of Oregon*, 154 Or App 702, 962 P2d 744 (1998), *rev dismissed*, 355 Or 591, 158 P3d 822 (2002) ("*Trojan I*"), the Court of Appeals held that the PUC's rate *order* was unlawful in so far as it relied on the erroneous assumption that PGE was entitled to a return on its investment in Trojan. But it does not follow from that holding that the resulting *rates* were unlawful. To determine whether the erroneous order actually resulted in unjust and unreasonable rates, the PUC lawfully used its rate making authority to determine what rates would have been fair and reasonable if it had not allowed PGE to earn a profit on Trojan. As this court expressly recognized in *Dreyer v. PGE*, 341 Or 262, 142 P3d 210 (2006)("*Dreyer*"), that was an appropriate way for the PUC to determine the harm caused to customers by the erroneous order.

Nor did the PUC err by assuming on remand that PGE would have been entitled to earn interest for the purpose of enabling it to fully recover the value of the principal investment in Trojan. The Court of Appeals had concluded—in reversing the 1995 order— that PGE could recover the full value of its principal investment but that ORS 757.355 prohibited PGE from earning a *profit* on that investment. The court did not hold that the statute precluded PGE from earning sufficient interest to cover the time value of its initial investment. As a matter

of simple economics, money available now is worth more than the same amount of money in the future. Because PGE could not have recovered all of its principal immediately, and instead would have been required to recover it over 10 years, allowing interest would have been necessary to ensure that PGE obtained the full value of its principal investment.

The PUC may not engage in retroactive ratemaking, but that is not what it did here. The rule against retroactive ratemaking prohibits the PUC from attempting to make up for a utility's past profits or losses when it sets future rates. In this case, the PUC was not setting rates at all. Instead, it merely identified the rates that it would have set in 1995 had it correctly construed ORS 757.355, in order to craft a remedy that would put the parties in the same position that they would have occupied had the PUC correctly applied that statute. The order was thus a lawful exercise of the PUC's authority, and is entirely consistent with the directives from the Court of Appeals and this court. This court should affirm it.

STATEMENT OF MATERIAL FACTS

The order on review, PUC Order No. 08-487, is the culmination of a complex series of proceedings before the PUC, the circuit court, and the

appellate courts.[1] To provide necessary context for the arguments that follow, the PUC begins by setting forth the events and decisions that preceded Order No. 08-487, identifying what the order says, and describing the Court of Appeals decision affirming it.

A. Events and Decisions Preceding PUC Order No. 08-487

The litigation surrounding PGE's recovery of its investment in the Trojan has spanned twenty years and has been fought on multiple fronts. In addition to the Court of Appeals' decision under review, the litigation has resulted in three previous decisions: *Trojan I*, *Dreyer*, and *Utility Reform Project v. PUC*, 215 Or App 360, 170 P3d 1074 (2007)("*Trojan II*").

1. The closure of Trojan and the 1995 rate order

When PGE first opened Trojan in 1976, the PUC approved rates that allowed PGE to recover its capital investment in Trojan, plus a return on that investment, over the course of 35 years. That rate structure reflected the assumption that the plant would supply electricity well into the 21st century. But that did not happen; the plant repeatedly ran into costly maintenance and repair problems. Those problems were sufficiently expensive that PGE concluded that closing Trojan and purchasing electricity from other sources

[1] A detailed description of those proceedings is set forth by the Court of Appeals in its opinion. *Gearhart v. PUC*, 255 Or App 58, 65-79, 299 P3d 533 (2013). Except where otherwise indicated, the factual summary above is based on that description.

would be less expensive than continuing to operate it. In 1993, after only 17 years in service and before recovering much of its capital investment—approximately $288 million still remained outstanding—PGE closed the plant.[2]

When Trojan stopped, the rate dispute started. Immediately at issue was whether PGE was entitled to recover its remaining undepreciated investment. Resolution of that dispute centered on two statutes—ORS 757.355, which generally prohibits utilities from recovering the costs of property that is not currently being used to provide utility service, and ORS 757.140, which provides an exception to that general rule. Under ORS 757.140(2), the undepreciated investment in a retired plant may be recovered when the commission determines that retirement of the plant was "in the public interest."

PGE argued that under ORS 757.140(2), the undepreciated amount should remain in its rate base, which would allow PGE to continue to recover both a "return of" its Trojan investment (*i.e.*, recovery of the remaining investment principal as an expense) and a "return on" its Trojan investment (*i.e.*, earning a profit on the remaining Trojan investment balance). The

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[2] That figure, $288 million, reflected the net undepreciated balance minus deferred taxes and tax credits associated with Trojan. The *gross* undepreciated Trojan balance was $340.2 million. (AR at 5110 and at 5123—PGE/Commission Staff Exhibit 202).

Citizens' Utility Board of Oregon (CUB)[3] argued on behalf of consumers that ORS 757.355 barred PGE from earning a return *on* its Trojan investment, even if ORS 757.140(2) permitted it to recover its undepreciated principal in the plant. URP argued that ORS 757.355 barred PGE from including *any* aspect of its Trojan investment in its rates—principal or profit. The PUC, based on advice from the Attorney General,[4] ruled that if PGE could establish at a rate proceeding that closing the plant was indeed in the "public interest," then ORS 757.140(2) did permit the undepreciated balance to remain in the rate base. (Order 08-487 at 10-11).

A ratemaking proceeding then ensued, at which the PUC applied a "net benefits" test to decide whether the closure of Trojan was in fact in the public interest. To do that, the commission analyzed which option—closing the plant or continuing to operate it—was less expensive from the perspective of ratepayers. It thus compared *allowable* costs of continuing to operate the plant (*i.e.* prudently incurred costs that the PUC would allow to be passed on to ratepayers) with allowable costs of closing it. Importantly, the PUC assumed—

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[3] The voters created CUB through the initiative process to represent and advocate for the interests of utility consumers, to ensure that "public policies affecting the quality and price of utility services reflect their needs and interests." ORS 774.020.

[4] Atty Gen OP 6454 (June 8, 1992) (AR 313).

when it calculated the allowable cost of closure—that PGE would be allowed to earn a return on that investment, the cost of which would be passed on to ratepayers. *Id.* at 11.

Based on that assumption, the commission determined that the allowable costs of closing the plant exceeded the costs of continuing to operate it, by about $20 million. In addition, the commission determined that approximately $17.1 million dollars in capital expenses that PGE had already made to keep the ailing plant operating were not allowable and could not be passed on to customers. Subtracting those amounts from the $288 million that comprised the remaining undepreciated investment, the commission thus determined that the remainder— $250.7 million—represented the point at which customers were indifferent between the options of continuing to operate the plant and shutting it down.[5] In other words, the commission determined that if, after the plant closed, PGE were limited to recovering $250.7 million of its total remaining

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[5] URP claims that the PUC improperly increased the undepreciated amount from $250.7 million to $340.2 million during its reexamination of rates. (URP Brief pg. 48, pg 75). URP is mistaken. As noted above, *supra note* 2, the figures represent the two separate calculations appropriately used by the PUC in its 1995 rate order to determine the basis for the return of the Trojan investment balance and the basis for a return on that balance. PGE's actual, pre-tax Trojan balance the time of the 1995 rate order was $340.2 million, while $250.7 million represents the after-tax value. Disallowances to a utility's revenue requirement are routinely considered on an after-tax basis. This practice is widely used by regulatory agencies and is required to account for the effects of accelerated depreciation and other tax benefits.

investment, then, from the ratepayer's perspective the cost of the two options—keeping the plant open or closing it—would be the same. The commission thus found that closing the plant and allowing PGE to recover that amount, $250.7 million, was in the "public interest" under ORS 757.140(2). (Order 08-487 at 11).

The commission then issued a rate order that allowed PGE to include the $250.7 million in its rate base, thereby giving PGE the opportunity to earn a return on that amount. Instead of allowing PGE to recover all its undepreciated capital at once, which would cause a spike in rates, the PUC required PGE to recover the amount over an extended period—17 years—to ensure that rates were fair and reasonable. As would become significant later, the PUC's decision to require PGE to recover the investment over the course of 17 years was, again, predicated on the commission's assumption that PGE would be earning a return on the amount during that period. (Order 08-487 at 12).

Both CUB and URP appealed the PUC's decisions interpreting ORS 757.140(2) to allow PGE to include a portion of its undepreciated investment in Trojan in PGE's rate base.[6] On appeal, CUB continued to argue that ORS 757.355 barred PGE from earning a *return on* its Trojan investment,

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[6] The cases were initially heard in Marion County Circuit court, and resulted in conflicting rulings. The Court of Appeals consolidated the cases.

while URP continued to argue that ORS 757.355 barred PGE from recovering *any* of its investment.

2. *Trojan I*

In *Trojan I*, the Court of Appeals concluded that the PUC had erred in interpreting the governing statutes. The court agreed with the PUC that ORS 757.140(2) authorized rates that reimburse a utility for its *principal* investment in unused or retired property. But the court concluded that ORS 757.355[7] precluded the PUC from authorizing rates that included a return or profit on an undepreciated investment in such property. Because the court concluded that the "PUC erred in each of the orders," it remanded the "orders to the PUC for reconsideration. 154 Or App at 706, 717.

Following the Court of Appeals' decision in *Trojan I*, the PUC petitioned this court to review the decision, and this court granted that petition. 328 Or 464 (1999). Soon thereafter, however, PGE, CUB, and PUC staff entered a settlement agreement. Under that agreement, the parties agreed that Trojan would be removed from PGE's accounts by offsetting the remaining Trojan investment balance—at the time, approximately $180 million— and certain tax liabilities against certain credits owed to ratepayers. The PUC approved the

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[7] The legislature amended ORS 757.355 in 2003. Or Laws 2003, ch 202, § 2. All references to ORS 757.355 are to the statute as it existed before the amendment.

settlement in 2000. Thereafter, Trojan was not included in PGE's rate structure. This court then dismissed the petition for review. 335 Or 91 (2002).

3. *Dreyer*

The settlement eliminated Trojan from PGE's rates prospectively. But it did not attempt to assess or redress the damages that may have been incurred by customers who, for the previous five years—from 1995 to 2000—had been paying rates established under the erroneous order. For that reason, after the PUC approved the rates established by the settlement, CAPs filed a putative class action in circuit court against PGE. They sought to recover from PGE the "overcharges" incurred during 1995 to 2000. The circuit court certified the class and granted CAPs' summary judgment motion on two claims.

PGE then petitioned this court for a writ of mandamus. PGE argued, among other things, that the circuit court lacked jurisdiction over CAPs' claims because their resolution necessarily involved rate making, which is solely within the province of the PUC. In that regard, PGE argued that for CAPs to prevail, the jury would have to decide what "fair and reasonable" rates the PUC *would* have set if it had not made an error, and would then have to compare that rate to the one actually charged during the relevant period.

This court agreed that *one* legitimate way to decide the question of damages would be to consider the rates the PUC would have set if it had not made an error. But this court also held that it was not the only legitimate

approach. Alternatively, this court noted, the jury "could simply attempt to determine what part of the rates that the PUC had approved as 'fair and reasonable' in fact represented a return on PGE's investment in Trojan and, therefore, were unlawful under ORS 757.355 (1993)." *Dreyer*, 341 Or at 282. The court therefore rejected PGE's argument that plaintiffs' claims *necessarily* involved ratemaking, and that the circuit court was therefore without jurisdiction. *Id.*

Notwithstanding its conclusion that the law did not require dismissal of the CAPs' lawsuit, this court nonetheless ordered the circuit court to abate the proceedings. In doing so, this court explained that the PUC had *primary* jurisdiction over the matter and that it therefore was for the PUC, in the first instance, to address the issue of the 1995-2000 rates. This court explained that "the PUC proceeding that is underway thus has the potential for disposing of the central issue in these cases, *viz*., the issue whether plaintiffs have been injured (and, if they have been, the extent of the injury)" and that depending on how the PUC responds to the issues on remand, "some or all of plaintiff's claimed injuries may cease to exist." *Id.*

4. *Trojan II*

At around the same time that CAPs was pursuing its case in circuit court, URP was back before the PUC, challenging the rates set by the settlement. URP argued that the rates established by the settlement were unjust because

they did not account for rates paid from1995 to 2000, and that customers were entitled to a refund of any rate amounts collected during that period that included a return on PGE's investment in Trojan. The PUC doubted its authority to retrospectively adjust rates or order a refund but concluded that, in any event, the rates established by the settlement were just and reasonable. On appeal, however, the Marion County Circuit Court concluded that the PUC *did* have authority to retroactively adjust its rates. It remanded the case to the PUC with instructions to offset future rates or order refunds. The PUC appealed that decision.

In *Trojan II*, the Court of Appeals agreed with the PUC that the circuit had erred in determining, in the first instance, that the PUC necessarily had authority to order a refund. 215 Or App at 372-74. The court remanded the case to the PUC to consider the scope of its authority, and to decide what action, if any, should be undertaken as a result of that decision. *Id.* at 376. Relying on this court's decision in *Dreyer*, the Court of Appeals emphasized that the PUC had primary jurisdiction to decide whether and under what circumstances the PUC is authorized to order a refund or other remedy. *Id.*

B. PUC Order No. 08-487

After the decisions in *Dreyer* and *Trojan II*, both of which had cited the need for a uniform resolution from the PUC, the PUC consolidated the ongoing

Trojan proceedings. The PUC then issued a single, comprehensive order, No. 08-487, that addresses all the outstanding issues related to Trojan.

The PUC's review required reexamination of all of the issues that were affected by the inclusion of Trojan in the rate base, beginning with its determination of PGE's revenue requirement as of 1995. The order thus began with a review of the procedural history of the case, and an examination of the direction that the PUC had received from the courts in *Trojan I*, *Dreyer*, and *Trojan II*. (Order 08-487 at 8-17). In *Trojan I*, the PUC explained, the Court of Appeals had concluded that the rates in effect between 1995 and 2000 were based on the commission's erroneous interpretation of the ORS 757.355. Yet, the commission noted that the Court of Appeals, while holding that the commission thus had made a legal error in its rate order, had not deemed the resulting rates unjust and unreasonable and thus unlawful. *That* determination—whether the resulting rates were unjust and unreasonable—required the PUC to exercise its expertise and authority to determine what rate is fair and reasonable, and was thus committed to the commission's authority. *Id*. Consistently with *Dreyer* and *Trojan II*, the commission concluded, it was up to the PUC to determine (1) whether there was any harm to ratepayers from the 1995 order and, if so, to determine (2) what remedy it could provide to customers.

To address the first question—whether the 1995 order harmed customers—the PUC compared the actual rates that ratepayers paid from 1995 to 2000 with those that the PUC would have set if it had recognized that ORS 757.355 prohibited PGE from earning a return on Trojan. Determining what rates it would have set was not a simple task, because ratemaking decisions are not made in isolation, and individual rate elements are often interdependent. That was the case with Trojan and the erroneous assumption that PGE lawfully could recover a return on its investment. *Id.* at 65-67.

As noted above, in applying a "net benefit" test and weighing the cost of closing the plant, the PUC, in issuing its 1995 order, had assumed that closure costs would include allowing PGE to earn a profit. Further, the PUC's determination that PGE would recover the undepreciated investment over a period of 17 years was also predicated on the assumption that PGE would be earning a profit over that period. Because that erroneous assumption had affected each of those variables, the PUC could not determine what the rates would have been by simply subtracting the Trojan profit from the overall rates. Rather, the PUC was forced to reexamine how changing that assumption would have changed its analysis and affected the resulting rate. *Id*..

After a lengthy analysis, the PUC determined that its 1995 decision would have differed in three fundamental respects had it correctly interpreted ORS 757.355 to prohibit a return on investment in a retired plant:

- First, the PUC would not have allowed PGE to include Trojan in its rate base and would instead have allowed PGE to recover only its principal as an expense. In other words, PGE would have been allowed a "return of" its Trojan investment, but not "return on" that investment. The PUC had originally allowed PGE to include Trojan in its rate base, which entitled it to earn a profit on the undepreciated balance, at approximately 9% per year. PUC determined that it would not have allowed PGE to earn that profit, but instead it would only have allowed PGE to recover the principal. Because the principal was to be collected over time, PUC would have allowed interest, at a rate (7.09 %) reflecting the time value of money.[8]

- Second, the PUC would have reduced the length of time over which PGE would recover the principal. The PUC had originally determined that an appropriate balancing of the interests of the utility and the ratepayers required PGE to recover its Trojan investment over an extended period, 17 years. But that determination assumed that PGE would be earning a profit on its investment over that period. In re-examining the rates, the PUC determined that, if it had known that PGE was not entitled to earn a "return on" the Trojan investment, it would have been necessary to shorten the period over which the PGE would recover its investment to 10 years to maintain rates that were fair and reasonable for both customers and PGE. If it was not earning a profit, PGE faced substantial lost opportunity costs while it recovered its investment. Yet allowing PGE to recover all of its investment immediately would not be fair to consumers, because it

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[8] The PUC considered various approaches to measuring the "time value of money" and determined that under the circumstances the interest rate of a 10-year United States Treasury bonds—a risk-free, guaranteed growth rate—was the appropriate measure (Order at 08-487 at 73). The rate in 1994 was 7.09 percent. By comparison, the current 10-year Treasury Bond rate, as of the date of this filing, is 2.79 percent. U.S. Department of Treasury, available at http://www.treasury.gov/resource-center/data-chart-center/interest-rates/Pages/TextView.aspx?data=yield (last visited January 23, 2014). The difference demonstrates that the time value of a present sum of money depends on economic conditions.

> would result in rate shock. The commission determined that allowing PGE to recover the investment over 10 years, with enough interest to ensure that PGE recovered the full present value of its principal, would strike the appropriate balance between the needs of consumers and the utility.
>
> - Third, it would have changed the outcome of the net benefit test, which the PUC used to assess whether closing the plant was in the public interest. In performing that test originally, the PUC had assumed that Trojan would be included PGE's rate base, and that PGE would thus be earning a "return on" that investment. Based on that assumption, the cost of closing the plant was $20 million more than the cost of continued operation. The PUC thus determined that closure was in the public interest only if it "disallowed" PGE from recovering $20 million of the remaining investment—*i.e.*, subtracted from the amount of the Trojan balance that PGE was allowed to recover. For that reason, in the 1995 rate order the PUC had disallowed PGE from recovering $20 million remaining Trojan investment. But if the PUC had known that PGE was not entitled to earn a profit, that would have made the cost of closing the plant much less. Under that scenario, the cost of closing the plant would have been *less* than the cost of keeping it open. So, closing the plant would have been in the public interest *without* the $20 million disallowance. Stated differently, the PUC had disallowed $20 million from the amount PGE was entitled to recover only because it assumed that PGE would be earning a profit. If the PUC had understood that PGE was not entitled to earn a profit, PGE would have been entitled to recover that $20 million along with the rest of its Trojan investment.

Id. at 67-79.

Other elements of the ratemaking process would have remained unchanged. Each of the three changes described above, considered in isolation, would have had a different effect on the rates. Removing Trojan from PGE's rate base, obviously, would have driven the rates down because PGE could no longer earn a profit. But reducing the period over which the Trojan balance was

recovered would have had the opposite effect, causing more of the principal to be recovered each year. Similarly, changes in the "net benefit" test would have increased rates also, because the principal that PGE would have been allowed to recover would have been $20 million more.

The net result of all of those changes, the PUC determined, was that, had the PUC correctly applied the pertinent statutory provisions in its 1995 order, it would have deemed PGE's revenue requirement for 1995 to 2000 to be $4.03 million *higher* than it did. (Order 08-487 at 78-79). Utility rates for customers would therefore have been somewhat higher as well, in order to satisfy the higher revenue requirement. In other words, the PUC determined that its erroneous assumption in 1995 that PGE could recover a profit did not increase the rates PGE's customers paid between 1995 and 2000. Because the legal error identified in *Trojan I* actually caused a slight decrease in the rates paid during 1995 to 2000, there was no basis to conclude that the error had resulted in unjust or unreasonable rates during the period, or to conclude that customers who paid those rates during that time were harmed by the error. *Id.* at 79.

That did not mean that the erroneous order had no effect on customers, however. Had the PUC correctly applied ORS 757.355, as discussed above, PGE would have been recovering the Trojan principal more quickly than it did under the 1995 order that the PUC actually issued. That is important, because it means that—had the PUC applied the law correctly in 1995—by 2000, less of

PGE's principal would have remained unrecovered. More specifically, the commission determined that had it applied the law correctly in 1995, PGE's unamortized Trojan investment balance as of September 30, 2000, would have been $165.1 million, instead of the $180.5 million that actually remained by that date as a result of the erroneous rate order. That difference is significant, because the 2000 settlement between PGE, CUB, and PUC staff was predicated on the assumption that PGE still had $180.5 million in principal that it was entitled to recover. The settlement agreement effectively compensated PGE for that remaining unrecovered principal so that Trojan was off PGE's books and no longer factored in its rates at all. *Id.* at 81-83.

To return the parties to the position they would have been if the erroneous rate order had not been issued, therefore, required PGE to refund to ratepayers $15.4 million (the difference between the $165.1 million and $180.5 million balances described above), plus interest. The PUC concluded that it had authority under ORS 756.040 to remedy past mistakes in its own orders, even in the absence of a finding that the resulting rates were unjust, unreasonable or discriminatory. *Id.* at 87. The PUC found that its remedial authority is broad enough to allow it to order PGE to refund to customers the $15.4 million that PGE realized as a result of the PUC's adjustment of the time period for the return of its Trojan investment. The PUC ordered a refund of that excess, plus

interest at PGE's authorized rate of return for 2000 to the date of the refund order, for a total of $33.1 million.[9] *Id.* at 88.

C. The Court of Appeals Decision Affirming PUC Order No. 08-487

A divided panel of the court of appeals affirmed Order No. 08-487. Writing for the majority, Judge Nakamoto emphasized the broad discretion that the legislature has given to the PUC, and concluded that the PUC's order was consistent with the Court of Appeals' decisions in *Trojan I* and *Trojan II*. *Gearhart*, 255 Or App at 86-88. In particular, the court agreed with the PUC that *Trojan I* had not held that the 1995 *rates* were unlawful, and had held only that the PUC had erred in calculating those rates. The PUC thus had responded appropriately on remand:

> When confronted with a judicial determination that it had unlawfully required inclusion of a return on PGE's undepreciated Trojan investment, the PUC had authority and, indeed, had a duty, to determine whether the unlawful inclusion of that component in the rate base had the effect of rendering the rates unjust and unreasonable.

Id. at 84-85. The majority rejected the contention of URP and CAPs that the PUC's assumption that PGE would have been entitled to earn interest was inconsistent with ORS 757.355 or with the Court of Appeals' construction of that statute. *Id.* at 94-96. The majority also rejected the contentions that the

[9] PGE has since issued that refund. By the time it issued, the refund had grown to $37 million. PUC UM 1402 - Initial Utility Filing - Letter from Randall J. Dahlgren of PGE to the PUC, Oct. 22, 2010, p. 1.

PUC lacked authority to reexamine rates or to order PGE to issue a refund. *Id.* at 96-102.

Judge Schuman dissented. He agreed with the majority's analysis in its entirety, except for one central point. Judge Schuman explained that, in his view, *Trojan I* stood for the proposition that the *rates* under the 1995 rate order were unlawful, regardless of whether they were fair and reasonable, because they "include an unlawful return on Trojan." *Id.* at 107-108 (Schuman, J., dissenting). He thus concluded that the PUC had exceeded the scope of its authority on remand by reexamining whether the 1995-2000 rates were fair and reasonable. The only analysis in which the PUC should have engaged, in his view, was to determine how much of the "unlawful rates" was directly attributable to the inclusion of Trojan in PGE's rate base. *Id.*

ARGUMENT

In its order on remand, the PUC analyzed several interdependent economic variables and ultimately made two fundamental determinations about how its erroneous 1995 assumption—that PGE was entitled to a "return on" its Trojan investment—affected PGE's customers. The PUC first determined that the erroneous order had not actually caused any increase in customer's rates between 1995 and 2000 and that the rates in that period thus were lawful. Second, the PUC determined that the erroneous order did affect the assessment of Trojan's remaining undepreciated value in 2000, when PGE settled to

remove Trojan from its books. To remedy that, the PUC ordered PGE to refund $33 million to customers. As explained below, in making each of those decisions the PUC lawfully exercised its ratemaking authority and faithfully discharged its statutory duty to ensure that rates are fair and reasonable by balancing the interests of the customers and the utility.

A. On remand, the PUC lawfully focused on whether the actual 1995-2000 rates were fair and reasonable by comparing those rates with the rates that the PUC would have set had it not erroneously allowed PGE a return on its Trojan investment.

On remand, the PUC determined the extent to which the 1995-2000 rates were unjust and unreasonable by comparing the actual rates that ratepayers paid during that period with the rate that the PUC would have imposed had it not erroneously allowed PGE a return on its Trojan investment. Both URP and CAPs challenge the validity of that approach and the PUC's authority to engage in it. They claim that the PUC ignored directives from the Court of Appeals and needlessly complicated the analysis; according to them, as a matter of simple arithmetic any amount of the "unlawful" rates that was attributable to a profit on Trojan must be considered an "overpayment" for which ratepayers deserve a refund. Petitioners' arguments, however, fail to appreciate the complex nature of rate making and fail to recognize the distinction between a lawful rate order and an unlawful rate. As explained below, the PUC's approach was consistent with its duty to ensure that rates are just and

reasonable, consistent with *Trojan I* and *Dreyer*, and consistent with fundamental ratemaking principles. The approach that petitioners advocate, by contrast, is inconsistent with those principles.

1. The PUC's approach comports with fundamental ratemaking principles

a. Ratemaking principles require the PUC to set fair and reasonable rates while balancing the interests of utilities and customers.

The rates that public utilities charge for their services are regulated because utilities are natural monopolies. Ratemaking is a legislative function that is performed through a quasi-judicial process similar to a civil court proceeding. "The power to prescribe [rates], like the power to write laws, is legislative in character." *Valley & Siletz R.R. Co. v. Flagg*, 195 Or 683, 715, 247 P2d 639 (1952). Ratemaking requires the PUC to exercise discretion by balancing the interests of the utility investor and the customer. ORS 756.040(1). In balancing those interests, the PUC is required to set "fair and reasonable" rates–that is, rates that are sufficient to provide adequate revenue both for operating expenses and capital costs of the utility, plus a return to shareholders that is commensurate with similar enterprises and that will allow the utility to maintain its credit and attract capital. *Id.*

The ratemaking process allows the PUC to set just and reasonable rates based on a forecast of the utility's revenue needs. But it does not dictate a

particular or precise result. The factors involved in ratemaking are "so many and so variable that it is impossible to fix rates that will be mathematically correct or exactly applicable to all the new conditions that may arise even in the immediate future." *Hammond Lumber Co. v. Public Serv. Comm'n*, 96 Or 595, 609, 189 P 639 (1920).

For those reasons, the validity of a PUC rate determination rests on the reasonableness of the overall rates, not the theories or methodologies used or individual decisions made. If the total effect of the rate order is not unjust and unreasonable, "[t]he fact that the method employed to reach that result may contain infirmities is not then important." *Federal Power Comm'n v. Hope Natural Gas Co.*, 320 US 591, 602-03, 64 S Ct 281, 288, 88 L Ed 333 (1944). "It is the end result of an order of a regulatory authority which determines the question as to its validity and not the processes by which the authority reached the result." *Flagg*, 195 Or at 715.

Ultimately, rates are prohibited and unlawful only under three circumstances: (1) the rates are unjust and unreasonable, *id*.; *see also* ORS 756.040(1) (requiring the PUC to establish "fair and reasonable rates"); (2) the rates are unjustly discriminatory, *American Can*, 55 Or App 451, 462-63, 638 P2d 1152 (1982); *see also* ORS 757.310(2) (prohibiting utilities from charging discriminatory rates); or (3) the rates are confiscatory, *see*, *e.g.*, *Pacific Tel. & Tel. Co. v. Wallace*, 158 Or 210, 297, 75 P2d 942 (1938)

(holding that rate order imposed rates that were unconstitutionally confiscatory).

When the PUC has made a legal error in the process of its ratemaking the resulting rate may or may not be "unfair or unreasonable." Regardless, as this court has long recognized, when a reviewing court concludes that the PUC has committed a legal error in its rate order, the court will vacate the order and remand the matter back to the PUC to "start over" with a correct understanding of the law. *Hammond Lumber*, 96 Or at 603. The reviewing the court thus does not, and could not, attempt to ascertain or dictate what the "fair and reasonable" rate should have been but for the error. *Id.* Instead, consistently with its power to prescribe rates, that job is committed to the PUC.

b. The PUC's order is consistent with those principles, while the approach advocated by petitioners is inconsistent with them.

The above discussion reflects four particularly pertinent principles:

- The PUC has a fundamental statutory obligation and broad power to set rates that are fair and reasonable, balancing the interests of customers and utility;
- Because determining which rate is fair and reasonable requires weighing and harmonizing multiple, interdependent elements, changing any one element may require revisiting other elements to ensure that the resulting rate is just and reasonable;
- A rate order that contains a legal error does not necessarily render the resulting rate outside the range of what is fair and reasonable and thus lawful;

- If a reviewing court determines that a rate order contains a legal error, the court vacates the order; it remains up to the PUC to ascertain what rates would have been fair and reasonable.

The PUC's analysis on remand is consistent with each of those principles. To return parties to the position they would have been in, the PUC could not simply subtract and refund the amount attributable to the Trojan profit. It could not do that because it knew that the initial erroneous assumption that PGE could earn a return on its investment in Trojan affected multiple components in its analysis—it affected the rate of return on Trojan, application of the net benefit test, and the time period over which PGE would recover the investment. Determining the error's effect, in other words, required the PUC to reconsider all of the components of its analysis that were affected by the error, reset those components, and then determine anew what rates would have been fair and reasonable.

Conversely, the approach that petitioners advocate is flatly inconsistent with those principles. If, as petitioners suggest, the PUC had simply ignored the complexities of ratemaking and treated the Trojan profit as an "overpayment," it would have been effectively presuming that subtracting the "overpayment" from the actual rates would result in the correct, fair and reasonable rates. But, as the PUC's actual analysis reveals, that is not the case. In fact, the actual rates paid between 1995 and 2000 were fair and reasonable, despite the error. If the PUC had simply subtracted the "overpayment" from the

actual rates, the result would have been rates for 1995-2000 that were substantially lower than the rates that the PUC has since determined *were* actually fair and reasonable. That might sounds like an attractive solution from the perspective of customers, but it is not a solution consistent with ORS 756.040 and the PUC's statutory duty to set rates that are fair and reasonable, balancing the needs of both customers and the utility. Stripping the Trojan profit from those rates without revisiting all of the affected elements that went into determining the 1995 to 2000 rates in the first place thus ignores holistic nature of ratemaking and would have resulted in an unjust and unreasonable rate. [10]

Petitioners alternatively argue that it should not matter that the actual rates 1995 and 2000 were fair and reasonable because, even if they were fair and reasonable they were still unlawful. (CAPs at 12). Here, petitioners echo Judge Schuman's dissent.

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[10] Indeed, URP's arguments that the PUC should have simply stripped away the profit component is inconsistent with the testimony of its own expert witness. URP's witness, Jim Lazar, recognized the complexity of ratemaking and, in fact, advocated for a series of other rate adjustments. Lazar concluded that these adjustments, above and beyond the removal of the profit component, "would have been the logical result of a rate case in 1995 that followed the legal requirement to exclude Trojan from rate base." UPR/200, Lazar/7.

Judge Schuman relied on what he saw as an important distinction between (1) rates that result from including an unlawful element, such as a return on PGE's Trojan investment, in the rate determination, and (2) rates that result from assigning an incorrect weight to one or more of the many legal elements that the PUC does have discretion to consider. 255 Or App at 107-108. With respect to the latter kind of rates, Judge Schuman acknowledged that the resulting rates may still be lawful, and "it is the legality of the end result of the ratemaking process, and not the legality of each calculation or input used during that process, that controls." But the former kind of rate, Judge Schuman concluded, is inherently unlawful. In his view,

> "The PUC did not misuse its broad discretion; it had no discretion to misuse. The PUC failed to recognize that, and, as a result, the rates that it approved included a single specific and impermissible element—a rate base that unlawfully includes return on the unamortized balance of Trojan. The rates that derive from that inclusion are unlawful, not because they are unfair and unreasonable but because they include an unlawful return on Trojan."

Id. at 108-109. Respectfully, Judge Schuman's analysis is incorrect.

The problem with that line of reasoning is that it confuses two entirely different concepts: an *unlawful rate order* with an *unlawful rate*. When the PUC makes a legal mistake in its rate *analysis*—either misreading a statute or assigning a legally incorrect weight to a particular element in its analysis, or considering an element it should not have—the underlying *order* is unlawful

and subject to remand. But whether the utility or the customer affected by the unlawful order is owed a remedy depends on whether (or the extent to which) the resulting *rate* is unlawful. The *rate* is unlawful only it is discriminatory, confiscatory, or outside the range of fair and reasonable. If the rate is none of those things, that is, if it actually is the overall amount that would represent a fair and reasonable balancing of the interests of the customers and the utility had there been no legal error or erroneous statutory interpretation, then the rate itself is lawful.

The proposition that a rate *itself* may be fair and reasonable but nonetheless unlawful is based on a misconception of what a rate is. A rate is not a collection of isolated and aggregated charges, any one of which can be peeled away. The rate is the end result of an analysis—the *total* amount of money that, in PUC's estimation, represents a "fair and reasonable" rate as defined by the legislature, balancing the interests of *both* the utility investor and the customer.[11] ORS 756.040.

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[11] CAPs argue that it is possible for a rate to be unlawful even if it is fair and reasonable. They rely on *former* ORS 756.594, which, they contend, explicitly demonstrates that rates can be *either* "unreasonable *or* unlawful." But that statute shows no such thing. That statute provided that in a rate challenge, "the burden of proof is upon the party seeking to modify, vacate or set aside findings of fact, conclusions of law or the order to show by clear and satisfactory evidence that the *order* is unreasonable or unlawful." (Emphasis added). The statute thus actually supports the PUC's point: the *order* may be

Footnote continued…

The proposition that a rate *itself* may be fair and reasonable yet nonetheless unlawful also finds no support in case law. As the United States Supreme Court has explained, "If the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry * * * is at an end. The fact that the method employed to reach that result may contain infirmities is not then important." *Hope*, 320 US at 602. *See also*, *Flagg*, 195 Or at 715. The PUC is not aware of any case, in any jurisdiction, in which a rate was held to be fair and reasonable yet simultaneously was deemed unlawful.

Nor can the proposition that a rate may simultaneously be fair and reasonable and unlawful be squared with PUC's statutory duty to ensure fair and reasonable rates. If a rate is fair and reasonable, but the PUC were nonetheless to strip any supposedly "illegal" component without attempting to adjust related ratemaking decisions, then the resulting rate would *not* be fair and not reasonable. If a rate –whatever errors may have gone into it—is nonetheless the "right" rate because it is in fact fair and reasonable, then by definition neither party to the rate order can be said to harmed by the rate. For all those reasons, the distinction on which Judge Schuman relied, between

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(…continued)
either unlawful or unreasonable. But it does not follow that the *rate* can be both "fair and reasonable" and the rate still inherently unlawful.

errors in assigning "weight" to various components and errors that involve the unlawful inclusion of a particular component, is not a useful one.

In addition, Judge Schuman's characterization of the error as unlawfully including a return on PGE's Trojan investment in the 1995-2000 *rates* does not fully or accurately capture the true nature of the problem that the PUC needed to address on remand. If the problem was simply that a return on the Trojan investment was included in PGE's rates, then indeed the solution would have been to simply take it out and refund the difference. But the problem was more complex than that. As explained above, the PUC's erroneous 1995 assumption that PGE was entitled to a return on the Trojan investment affected several different components that informed and influenced the 1995 rate calculation. The most obvious effect of the error was to allow PGE to include Trojan in its rate base and thus to recover a profit. But the error also affected the PUC's 1995 analysis in ways that favored PGE's customers – namely, by extending the time period over which PGE could recover its Trojan investment and by increasing the PUC's estimate of the costs of closing the plant. If the PUC had simply stripped the profit from the overall rate that, at most, would have addressed *one* of issues but would have ignored the others. Such an approach is flatly at odds with the PUC's duty. The problem identified by the Court of Appeals in *Trojan I*, in other words, was with the PUC's rate *order*. That is why, having concluded that the rate order contained an error of law, the Court

of Appeals required the PUC to reconsider the *order* to determine the affect the error had on the rates charged to customers. [12]

2. The PUC's order is also consistent with *Trojan I* and *Dreyer*.

Petitioners also contend that by revisiting the rates it would have imposed, the PUC's order is inconsistent with directives from the Court of Appeals in *Trojan I* and inconsistent with this court's decision in *Dreyer*. But the PUC's order is entirely consistent with both opinions.

i. The PUC's order is consistent with *Trojan I*.

Both URP and CAPs contend that the PUC's order is inconsistent with *Trojan I* because, as they read the opinion, the Court of Appeals had conclusively held that the *rates* resulting from the erroneous 1995 rate order were unlawful. (URP Br at. 44; CAPs Br at 15-19, 24). As the Court of Appeals recognized in its majority opinion, however, that is not a correct reading of *Trojan I*.

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[12] For similar reasons, petitioners' various contentions that the PUC's reexamination of rates violated the principles of *res judicata*, claim preclusion, or "law of the case" also miss the mark. *See, e.g.*, URP Brief pp. 26-38. As explained above *Trojan I* did not hold that the rates charged during the 1995 2000 period were unlawful. In any case, the remand proceedings were not a re-litigation of matters that had already been decided, nor were they attempt to litigate matters that might plausibly have been raised and litigated earlier. They were an attempt to determine for the first time what rates *would* have been "fair and reasonable" had the PUC not erred in interpreting ORS 757.355. *That* issue was obviously not on anybody's radar in earlier proceedings – it only arose because of the Court of Appeal's decision in *Trojan I*.

In *Trojan I*, the Court of Appeals held that the PUC had erroneously interpreted ORS 757.355 by assuming that PGE could earn a profit on Trojan. The court thus concluded that the *rate order* was unlawful. But that does not necessarily mean that the resulting *rate* is unlawful. Rates are unlawful if they are unjust and unreasonable, unjustly discriminatory, or confiscatory. But the Court of Appeals did not conclude that the rates set by the 1995 order were any of those things. As the PUC's order correctly states, the *Trojan I* court "did not even address the lawfulness of the *rates* adopted in UE 88, much less determine conclusively that these *rates* were unlawful." (Order 08-487 at 25) (Emphasis added). The court remanded to the PUC for reconsideration in light of the court's legal interpretation. *Trojan I*, 154 Or App at 717. But nothing in *Trojan I* declared the rates "unlawful" or required the PUC, on remand, to simply subtract the "return on" undepreciated investment in Trojan from the rates.

The Court of Appeals in this case has concluded that *Trojan I* does not mean what petitioners contend that it means. *Gearhart*, 255 Or App at 88. This court should affirm the Court of Appeals' interpretation of its own opinion.

Petitioners misreading of *Trojan I* reflects their continued confusion about the difference between an *unlawful rate order* and an *unlawful rate*. As this court recognized in *Hammond Lumber*, the role of the reviewing court "is not to search for or disclose or declare this 'reasonable and just' rate or service,

but merely to determine whether the *order* of the commission is "unreasonable"—quite a different thing." *Id.* at 600 (emphasis added). This court thus emphasized the difference between reviewing the validity of a rate order and the validity of the resulting rate:

> The result of the reversal of the order of the commission is not to * * * ascertain the [reasonableness of a rate], but to leave it undisclosed, leaving the former rates to stand or requiring the commissioners to try over again to find it. In reviewing the order of the railroad commission the inquiry is not whether the rate, regulation, or service fixed by the commission is just and reasonable, but whether the order of the commission is unreasonable or unlawful.
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> * * * * *
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> The making of [rate] regulations is a legislative or administrative, and not a judicial, function. The reasonableness of such an order is, however, a judicial question. The court may review the orders of the commission, but only so far as to determine whether they are reasonable. The order may be vacated as unreasonable if it is contrary to some provision of the federal or state Constitution or laws, or if it is beyond the power granted the commission, or *if it is based on some mistake of law*, or if there is no evidence to support it, or if, having regard to the interest of both the public and the carrier, it is so arbitrary as to be beyond the exercise of a reasonable discretion and judgment * * *. In brief, the function of the court is, in a sense, to review the proceedings of the commission and to ascertain if it has violated any principle of law or gone beyond the scope of its duty in making the *order*.

Id., at 600-603 (emphasis added)(internal quotation marks omitted).

Consistently with *Hammond Lumber*, in *Trojan I* the Court of Appeals reviewed the PUC's 1995 rate *order* and held it to be based on a mistake of law. It thus remanded the case to the PUC, but not with any particular directive

about what the correct rate was or should have been. *That* determination the Court of Appeals appropriately left "undisclosed," leaving it for the commission to "try over again." *Id.* at 600.

ii. The PUC's order is consistent with *Dreyer*.

Petitioners also contend that the PUC's order is inconsistent with this court's decision in *Dreyer*. In particular, they contend that this court concluded that PGE's customers were entitled to "damages" and that the PUC's conclusion on remand that the 1995-2000 rates were fair and reasonable ignores that holding. Yet the PUC's order comports precisely with what this court held in *Dreyer*.

In *Dreyer*, this court specifically recognized that the PUC's task on remand was to determine whether customers were injured by its error in including Trojan in the rate base. *Dreyer*, 341 Or at 286-87. As envisioned by *Dreyer*, the PUC undertook that reconsideration, and examined whether customers were harmed by the error identified in *Trojan I*, "by determining what a 'fair and reasonable' rate would have been if the objectionable return on Trojan had been excluded and then comparing that rate to the one actually

charged during the relevant period * * *." *Dreyer* 341 Or at 282.[13] The PUC did exactly that.

Contrary to CAPs' claim, *Dreyer* did not conclude that the CAPs are entitled to "damages." Instead, *Dreyer* simply held that the PUC had the authority and the responsibility to decide what action, if any, was required by the joint remand. *See Dreyer*, 341 Or at 286 (concluding that the PUC has primary jurisdiction to determine what, if any, remedy it can offer to PGE ratepayers). Again, that is precisely what the PUC has done.

What is more, in *Dreyer* this court expressly assumed that the PUC would exercise its ratemaking authority in the remand proceedings. Indeed, it was because of that assumption that this court concluded that the PUC had "primary, if not sole, jurisdiction over one of the remedies contemplated in the remand: *revision of rates* to provide for recovery of unlawfully collected

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[13] As noted above, this court also concluded that another way to measure damages would be to "simply attempt to determine what part of the rates that the PUC had approved as "fair and reasonable" in fact represented a return on PGE's investment in Trojan and, therefore, were unlawful under ORS 757.355 (1993), as interpreted in [*Trojan I*]." 341 Or at 282. Respectfully, the PUC disagrees with that conclusion. As explained above, because of the multiple way the erroneous interpretation of ORS 757.355 affected the rate order, the only accurate way to measure damages was the approach that the PUC in fact used. Regardless, because the approach the PUC used was a valid way to measure damages, to affirm the PUC's order this court does not need to revisit the question as to whether there are other valid measures that might have been employed.

amounts." 341 Or at 285 (emphasis added). That conclusion is entirely consistent with—and in facts anticipates—the approach that the PUC took on remand. The PUC did not engage in ratemaking per se, nor did it retroactively revise rates, but it did use its ratemaking authority and expertise to determine the effect that its erroneous 1995 rate order had PGE's customers.

3. The PUC did not exceed the scope of its statutory authority by reexamining the rates it would have set but for the error.

Petitioners further contend that the PUC had no authority to engage in a in remand in a retrospective analysis of what the 1995 rates might have been had it applied ORS 757.355 correctly. (URP Br at 68-70; CAPs Br at 35-37). But the proceedings that the PUC conducted on remand, and the analysis it conducted, were squarely within its delegated authority.

Absent a court's instruction to the contrary, an agency has authority on remand to act in accordance with its delegated powers. *See* Richard J. Pierce, Jr., 3 *Administrative Law Treatise* § 18.1, 1679 (5th ed 2010) ("An agency usually has several options available to it when a court sets aside an agency action and remands the proceeding for further action not inconsistent with the court's decision.") Here, neither of the appellate decisions that preceded the PUC order on review (*Trojan I* or *II*) purported to limit the scope of the PUC's broad delegated powers on remand. Nor did this court suggest any such limitation on the PUC's authority in *Dreyer*. On the contrary, as already

explained, both the Court of Appeals in *Trojan II* and this court in *Dreyer* expressly anticipated that the PUC might engage in just the sort of retrospective analysis that it did.

The PUC has been delegated exceptionally broad authority not just to set rates but to protect ratepayers from "unjust and unreasonable exactions." ORS 756.040; *see Pacific Northwest Bell Tel. Co. v. Katz*, 116 Or App 302, 308-10, 841 P2d 652 (1992) (recognizing PUC remedial authority to order a refund). That power includes the authority to amend orders at any time, to reopen the evidentiary records when necessary, and to remedy legal errors in previous orders. *See* ORS 756.568 (The PUC may at any time rescind, suspend, or amend any PUC order); ORS 756.040 (providing authority to do all things necessary to protect customers); *Katz*, 116 Or App at 308-10.

The PUC acted within that broad delegated authority on remand. It considered evidence and issues that were directly relevant to the issues before it – namely, those issues that were directly tied to the PUC's task of determining the extent to which including the Trojan balance in the rate base improperly increased PGE's revenue requirements. Following the instructions in *Trojan I*, *Dreyer*, and *Trojan II* , the PUC focused on what rates it would have approved if it had correctly interpreted ORS 757.355. AR 5453 (Aug. 31, 2004). The PUC allowed the parties to present new evidence; but limited it to evidence was limited to evidence that existed on or before October 1, 2000. *Id.*, AR 6685.

The PUC also investigated the extent to which it could lawfully reexamine past rates and whether that constituted retroactive ratemaking. Order No. 07-157 at 9, AR 6156 (Apr. 19, 2007). Finally, the PUC addressed the 2000 settlement among PGE, PUC Staff, and CUB that removed the Trojan balance by offsetting a variety of customer credits.

B. The PUC lawfully determined on remand that it would have allowed PGE to earn interest sufficient to allow PGE to recover over ten years an amount equivalent to the full value of its principal.

When the commission reconsidered the rates it would have set if it had known that PGE was prohibited from earning a return on Trojan, the commission determined that it would have allowed PGE to recover only the amount of its principal, over ten years, with a sufficient interest rate to reflect the "time value" of that amount. Petitioners contend that allowing PGE to recover *any* amount beyond the principal conflicts with the holding in *Trojan I* that ORS 757.355 prohibits PGE from earning a "return on" Trojan. Petitioners thus read *Trojan I* as prohibiting PGE from recovering interest on any Trojan-related funds. (URP Br at 13-30). As the Court of Appeals explained in this case, however, petitioners oversimplify and misread that decision. There is no basis for this court to overrule the Court of Appeals' interpretation of its own opinion.

The "time value of money" refers to the principle that money available now is worth more than the same amount of money in the future. Allowing an

investor to earn an interest rate that accounts for the time value of money is different that allowing that investor a rate that provides a profit over time. A rate that is merely sufficient to protect the time value of money is the minimal rate necessary to prevent an investor from being *penalized* by being forced to recover the original amount an investment over a protracted period of time.

It is a basic and fundamental principle of accounting that money received over time has less value than money received now. For example, if PGE was owed $10 today and received that money today, it has received full payment. But if PGE was owed $10 today, but did not receive that money until 10 years from today, it would not have received full payment. The same is true if PGE was owed $10 today and received $1 per year for 10 years. *See, e.g., Thomas v. Senior and Disabled Services Div.*, 319 Or 520, 530, 878 P2d 1081 (1994); *Till v. SCS Credit Corp*., 541 US 465, 486-487, 124 S Ct 1951, 1965-66 (2004) ("a creditor receives the 'present value' of its claim only if the total amount of the deferred payments includes the amount of the underlying claim plus an appropriate amount of interest to compensate the creditor for the decreased value of the claim caused by the delayed payments").

Here, if the PUC had assumed, as petitioners contend it should have, that PGE was entitled to earn *no interest* at all, then requiring PGE to recover the investment over 10 years would have prevented PGE from recovering the whole present value (in 1995) of its principal. But, as the Court of Appeals held in

Trojan I, PGE was entitled under ORS 757.140(2) to recover the whole value of that principal. That being the case, the only alternative to allowing PGE interest over ten years would have been to allow PGE to recover its entire investment in Trojan *all at once*. But that, as the PUC determined, was not a fair and reasonable alternative, because it would have led to an immediate 30 percent increase in rates. (Order 08-427 at 70). Such a dramatic increase in rates—rate shock—would not be "fair and reasonable" from the standpoint of PGE's customers. It also would have failed to promote intergenerational equity by requiring one "generation" (one year) of customers to bear the entire undepreciated balance. The PUC concluded that the only reasonable and acceptable alternative, therefore, was to allow PGE to recover the principal over time. In the exercise of its ratemaking authority, the PUC determined that the appropriate amount of time to avoid rate shock, promote intergenerational equity, and provide fair and reasonable rates would be 10 years. Under ORS 757.140(2), PGE was entitled to earn interest over that time.[14]

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[14] Petitioners object to the PUC's assumption that it would have allowed PGE's Trojan expense to earn interest, but they do not appear to challenge to the particular rate of interest that the PUC determined was the most accurate measure of the time value of money. Nor could they. The PUC's decision in that regard was well within the ambit of their rate-making authority and is supported substantial evidence and substantial reasoning in the record. As the PUC explained in its order, and as noted above, *supra note* 8, the PUC used the 1994 rate of 10-year U.S. Treasury Bonds, which reflected the risk-free, guaranteed interest rate that was then available. (Order 08-487 at 73).

C. The PUC acted within the scope of its authority by ordering PGE to refund $33 million to customers

To return the parties to the position they would have occupied if the erroneous rate order had not been issued, the PUC ordered PGE to refund payers $15.4 million, plus interest. That amount represents the difference between the actual remaining unrecovered Trojan investment in 2000, when PGE settled the case with CUB and staff, and what that amount would have been if PUC had not issued the erroneous order. On review, CAPs argue that the PUC has no authority to order such a refund. (CAPs Br at 38-50). As explained below, however, the PUC has extremely broad authority to remedy past mistakes in its own orders. The remedy that the PUC ordered was within the scope of that authority.

ORS 756.040 gives the PUC the authority "to do all things necessary and convenient" to protect customers from "unjust and unreasonable exactions." That statute actually places on the agency an affirmative *obligation* to protect customers and the public from unlawful rates:

> 1) In addition to the powers and duties now or hereafter transferred to or vested in the Public Utility Commission, the commission shall represent the customers of any public utility or telecommunications utility and the public generally in all controversies respecting rates, valuations, service and all matters of which the commission has jurisdiction. In respect thereof *the commission shall make use of the jurisdiction and powers of the office to protect such customers, and the public generally, from unjust and unreasonable exactions and practices and to obtain for them adequate service at fair and reasonable rates.* * * *

> (2) The commission is vested with power and jurisdiction to supervise and regulate every public utility and telecommunications utility in this state, *and to do all things necessary and convenient in the exercise of such power and jurisdiction.*

ORS 756.040 (Emphasis added.) By its plain terms, the statute gives the PUC the power—and duty—to ensure that customers are not harmed by its rate orders. The power to issue a refund is well within the scope of that authority.

In arguing to the contrary, CAPs rely on *McPherson v. Pacific Power & Light*, 407 Or 433, 296 P2d 932 (1956), but that case is inapposite. In that case, ratepayers challenged a surcharge and the trial court dismissed the case. This court affirmed. It noted that the PUC has exclusive authority to determine whether rates are unjust and unreasonable, but that the legislature had not conferred on it the authority "to award any reparations, either for unreasonable or unjustly discriminatory rates, or for overcharges[.]" 207 Or at 449. CAPS contend that the *McPherson* stands for the proposition that the commission lacks the authority to issue refunds. For several reasons, however, that is not a fair reading of *McPherson*.

First, in *McPherson*, this court concluded that surcharges were established as lawful rates and that the commission had acted lawfully. Because the commission had awarded no reparations, this court's statements about reparations were dicta. Second, in any case, in *McPherson* the question of the commission's authority pursuant to ORS 756.040 was not even raised,

much less answered. Instead, this court discussed the commission's powers under statutes in Chapter 757.[15] Third, *McPherson* is about regulation of *railroads*; the availability of "reparations" in the context of railroad regulation has nothing to do with whether a *utility* regulator can order a refund. Furthermore, in *Dreyer*, this court —while cognizant of *McPherson*[16]— expressly acknowledged that the PUC had jurisdiction to determine whether it can authorize refunds in this case. 341 Or at 285-86. The process that the PUC followed on remand, and the refund it issued, is consistent with *Dreyer* and with the PUC's broad authority under ORS 756.040.

D. The PUC's order does not violate the rule against retroactive ratemaking.

Petitioners also contend that the PUC engaged in impermissible retroactive ratemaking by determining what rates it would have set but for its error. (CAPs Br at 38-41). But their arguments in that regard are based on a misconception of that rule.

The rule against retroactive ratemaking (which is not actually an administrative rule but rather a well-settled common law principle) is implicated only when the PUC sets *prospective rates*. *See Gearhart*, 255 Or

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[15] Notably, the Court of Appeals has since concluded that ORS 756.040 *does* provide statutory authority for the PUC to order refunds. *See Katz*, 116 Or App at 309-10.

[16] *See Dreyer*, 341 Or at 271 n.10 (*citing McPherson*).

App at 99 (explaining rule). The rule prohibits the PUC from attempting to adjust prospective rates in order to "make up" for mistaken estimates of a utility's revenue requirement in previous rate setting. If, for example, a utility had generated more revenue in a previous rate period than the PUC had expected it to generate when it set rates for that period, the PUC could not penalize the utility by lowering rates for the next rate period. Similarly, if the utility earned less than the PUC had predicted it would earn in the past rate period, the PUC may not penalize ratepayers by raising rates in a new rate period in order to make up for that mistaken estimate. When setting future rates, the PUC must focus on the costs and appropriate return for the prospective period and cannot adjust that determination for a utility's past profits or losses. *Id.*

The rule against retroactive ratemaking does not, however, prevent the PUC from doing what it did on remand in this case—using its rate making authority and expertise to address whether a legal error in previously established rates produced an injury that is capable of being remedied. The PUC did retroactively examine the rates in effect from 1995 to 2000, but the PUC did so only to determine the extent to which PGE's customers were injured by the PUC's past legal error in setting those rates. The PUC thus explicitly limited its examination to information in existence at the time of the initial rate decision. PUC did not incorporate PGE's past profits or losses in

setting future rates. In fact, the PUC did not set future rates at all. The PUC determination of the hypothetical rates it would have set thus did not implicate the rule against retroactive ratemaking.

Nor did the PUC's decision to order PGE to pay a refund violate the rule against retroactive ratemaking. In arguing to the contrary, CAPs contends that when the PUC orders a utility to return money collected by the utility under a previous rate order, it necessarily is retroactively reducing the rates it previously approved. But a PUC-ordered refund to customers is not the legal equivalent of a retroactive rate reduction. Again, retroactive ratemaking occurs when a regulator sets future rates in an attempt to "make up" for unanticipated profits or losses in previous rate periods. Here, the PUC did not order a refund in an attempt to "make up" for PGE's past profits or losses. The PUC issued a refund to "make up" for the effects of the commission's own legal error in a rate order that was timely appealed and then remanded by the Court of Appeals.

Admittedly, some jurisdictions broadly construe the rule against retroactive ratemaking as prohibiting any refunds to ratepayers under any circumstances. *See generally*, Stefan H. Krieger, *The Ghost of Regulation Past: Current Applications of the Rule Against Retroactive Ratemaking in Public Utility Proceedings*, U Ill L Rev 983, 1022–26 (1991) (describing jurisdictions taking such a view). Other jurisdictions, however, interpret the rule much more narrowly, allowing, for example, exceptions to remedy procedural mistakes,

address extraordinary losses or gains, or allow energy cost adjustment clauses. *Id*. at 1003-09; 1030-31.

This court has never had occasion to decide the scope of the rule against retroactive ratemaking in Oregon. The rule is one fashioned by the courts, and it should be construed in a manner that is consistent with the regulatory scheme in a particular jurisdiction. As the PUC explained in its order, Oregon's statutory scheme militates in favor of a narrow understanding of the rule. First and foremost, the legislature has granted extraordinarily broad authority and expressly charged the commission to do "everything necessary" to "protect * * * customers, and the public generally, from unjust and unreasonable exactions and practices and to obtain for them adequate service at fair and reasonable rates." ORS 756.040. If the commission *lacked* the authority to issue refunds when a timely appealed rate order held to be erroneous on judicial review, the commission's ability to protect customers would be substantially restricted. Conversely, nothing in the statutory scheme purports to limit the commission's remedial authority to prospective applications only. To that extent, Oregon's scheme differs from other jurisdictions whose statutes create such an express limitation.[17]

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[17] The California case relied on by petitioners, for example, involves a statutory scheme that expressly prohibits retroactive ratemaking. *See City of Los Angeles v. Pub. Util. Comm'n*, 497 P2d 785, 804 (Cal 1972) (holding that

Footnote continued…

Against the backdrop of Oregon's statutory scheme, CAPs' contention that the rule against retroactive ratemaking prohibits *any* refunds to ratepayers under *any* circumstances is untenable. Certainly, the rule prohibits the commission from setting future rates based on based on an evaluation of a utility's actual expenses or revenues. But when the courts have concluded that a rate order includes an error of law, the commission's broad authority to do "everything necessary" to protect customers from unjust and unreasonable exactions includes the power to issue a refund to return the parties to the position they would have occupied but for the commission's error.[18]

(...continued)
the legislature "has expressly prohibited the granting of reparations on the basis of unreasonableness, where, as here, there is an approved rate" (citing Cal. Public Utilities Coe § 734.

[18] CAPs also argue that the PUC, by concluding that it could order PGE to issue a refund and then ordering that remedy, erred by retrospectively applying a new rule to a pending matter. (CAPs Br at 59-61.) It contends that an agency may not make such an abrupt reversal in policy and then apply it in a pending case. That argument is unpreserved, and this court should not address it for that reason. ORAP 9.20(2); ORAP 5.45(1). In any case, it is without merit. The analysis and refund in Order No. 08-487 is not a policy change. It is rather an application of Court of Appeals precedent, *see Katz*, 116 Or App at 311, and consistent with the directives from the Court of Appeals in *Trojan I* and *II*, and with this court's stated expectation in *Dreyer*. Moreover, CAPs cannot identify any former rule on which it relied to its detriment.

E. The PUC's order is supported by substantial evidence and substantial reason.

The PUC's determinations about the rates that it would otherwise have charged, and thus about the effect of its 1995 error, are determinations that it made in the exercise of its ratemaking authority and expertise. This court's review of those determinations is thus exceedingly narrow. The court must affirm the determinations if they are supported by substantial evidence and substantial reason, and it may not second guess the PUC's policy decisions, or reweigh its balancing of the interests involved. ORS 756.610(1); ORS 183.482(7).

The factual determinations in Order No. 08-487 are amply supported by evidence in the record, and the basis for the Commissions conclusions are supported by detailed, comprehensive reasoning. As outlined above, the order is a thorough and exhaustive effort by the commission to accurately identify the effect of its 1995 error on PGE and its customers and to return the parties to the position they would have occupied had the PUC not made the error.

In arguing to the contrary, petitioners challenge a number of specific calculations and insinuate that the PUC was not acting in good faith. But their arguments betray a misunderstanding about what the PUC's order says and why.

The URP contends, for example, that the PUC's order does not really address the error identified in *Trojan I* but merely "puts different labels on the same post-closure profits" that the Court of Appeals ruled were unlawful. (URP Br at 44.) In particular, the URP contends that the PUC shortened the recovery period from 17 to 10 years for the purpose of indirectly "preserving for PGE the benefit of the unlawful [rate order]." *Id.* That is not accurate. The PUC's order specifically explains that the original decision to allow PGE to recover Trojan investment over 17 years was reasonable only because the commission assumed PGE would be earning a profit over that time. (Order 08-487 at 71-72). But if the investment is only earning interest sufficient to cover the time value of money, then it comes with a substantial opportunity cost, because PGE is not able to use the money to invest in something that will generate a profit. For that reason, the PUC determined that a 10-year recovery period, as opposed to the longer 17-period, would "equitably allocate the benefits and burdens." In other words, the PUC changed the recovery period not to in an effort to "put a new label on post-closure profits" but in a good faith attempt to carry out its statutory duty under ORS 756.040 to balance the needs of the customers and the utility. (Order 08-487 at 72).

URP suggests that the PUC's order "indirectly" permits PGE to realize a post-closure profit through accounting sleight-of-hand by "pretending" that costs charged to ratepayers were "deferred" to later years. (URP Br at 46-48).

The precise logic behind those contentions is difficult to discern, but they appear to be based on a basic misunderstanding about the commission's reasoning. Indeed, URP's argument appears to have been largely cut-and-pasted from an earlier brief responding to a ratemaking scenario proposed in 2005.[19] In that earlier phase of the remand proceedings, PGE and the PUC staff recommended the commission adopt ratemaking scenarios that removed the Trojan investment from rate base and placed it in a deferred account under ORS 757.259. URP objected to the proposals because, once placed in a deferred account, the investment would earn return "equal to PGE's authorized rate of return on investment, thus magically changing Trojan return on investment to return on the 'deferred' costs."[20] URP is apparently unaware that the PUC *rejected* those proposed scenarios and, instead, adopted one that neither allowed the Trojan investment to remain in rate base nor be placed in a deferred account. The scenario that the PUC did adopt is a straightforward attempt to compare the rates that were imposed with those that would have been imposed had the error not been made. The order does not "pretend" costs actually charged were deferred or engage in any other obfuscatory accounting.

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[19] Compare URP's Opening Brief at 47 and Reply Brief of URP, et al at 1 (Nov 30, 2005).

[20] Reply Brief of URP et al at 1 (Nov 30, 2005).

URP also challenges the PUC's use of electronic spreadsheets and calculations made with the formulas contained within them, claiming the spreadsheets were not part of the record and the recalculations using them constituted *ex parte* communications. (URP Brief p. 20; p 63-64). Contrary to URP's assertions, the spreadsheets and the electronic formulas used to recalculate the rates were contained in the record.

To make the calculations, the PUC used Excel spreadsheets contained in testimony filed by PGE and PUC staff and admitted into the record. AR 295, tab 102; AR 297, tab 6201 and 6202. Moreover, as URP acknowledges (URP Brief p. 20), the PUC's ALJs obtained electronic copies of those spreadsheets, with formulas intact, in a Bench Request issued July 24, 2008—two weeks after the final remand hearings were concluded on July 10, 2008 but prior to oral arguments held on September 4, 2008. AR 21 pp. 6913-6198. URP did not respond or object to either the Bench Request or the filing of the spreadsheets.

During its deliberations, the PUC used the Excel formulas to make new calculations based on its adopted ratemaking decisions. The two "Non-Record Spreadsheets" submitted by URP in an appendix to its brief reflect the results of those calculations, derived solely from information and equations contained in the record, and do not constitute evidence outside the record. The PUC fully explained these calculations in FN 267 on page 75 and FN 279 on page 79 in its order. Furthermore, because the calculations were performed by the

Commissioners, ALJs, and PUC advisory staff who did not appear as witnesses in the proceeding, there were no *ex parte* communications that needed to be noticed to the parties.[21]

URP makes a variety of contentions about the accuracy of the mathematical calculations in the order, but those challenges are similarly without foundation. For example, URP claims that the PUC made a math error in calculating interest on the $15.4 million that is due customers. (URP Br at 17 n 11, 23 n 18). URP contends the PUC's interest calculation short-changed customers by $2 million, and that the customers should receive $35.1 million instead of the ordered $33.1 million. URP is mistaken. The PUC applied 9.6 percent interest, compounded monthly, to the $15.4 million for the 96-month time period from October 1, 2000 to October 1, 2008. Order No. 08-847 at 88.

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[21] *See* OAR 860-001-340 (formerly OAR 860-012-0015) (describing *ex parte* communications). URP also claims that the headings in the spreadsheets demonstrate that the PUC itself regarded 7.09 percent interest rate as a "return on" Trojan because column in which interest was calculated is labeled as "return on." (App 3-4, third column from right). But they read far too much into that heading. The PUC used spreadsheets prepared by PGE and PUC Staff for testimony filed in an earlier phase of the remand proceeding to access the electronic formulas in order to complete its calculations. Because the spreadsheets essentially served as a calculator, the PUC did not modify existing column headings when it changed the growth rate to reflect calculate interest rather than a "return on" Trojan that had previously been calculated. But the labels used to describe interest are beside the point. ORS 757.355 prohibited the PUC from including Trojan in PGE's rate base and thereby allowing PGE to earn a profit. ORS 757.355 did not prohibit the PUC from allowing PGE to recover it capital investment with sufficient interest to cover the time value of money.

The formula for and result of that calculation is: $\$15.4M \times ((1+.096/12)^{(8\times12)})$ = $33.1M. That is the number the PUC used.

Finally, URP contends that the PUC arbitrarily allowed PGE to introduce new evidence on remand while excluding evidence offered by URP. As an example, URP contends that the PUC refused to consider PGE's earnings during 1995 to 2000, but "took off the blinders when PGE presented massive amounts of information that was not 'known at the time of the Commission's original decisions.'" (URP Br at 69.) Again, for reasons started above, the PUC's conducted a retrospective examination to determine what rates it would have approved had it correctly interpreted ORS 757.355. To properly complete that examination, the PUC limited the parties to presenting evidence that could have been presented at the time of the 1995 rate order. Contrary to URP's assertion, the restriction applied to *all* parties.

URP sought to introduce evidence relating to PGE's earnings after 1995, but the PUC properly held that was irrelevant and inadmissible. (Indeed, consideration of earnings from a subsequent rate period is precisely the kind of inquiry that the rule against retroactive ratemaking precludes.) Furthermore, URP's claim that the PUC allowed PGE to present "massive amounts" of "future facts" is not supported by the record. (URP Br at 69). In fact, the only supposedly inadmissible "future fact" that URP has ever identified is the Court of Appeal's decision in *Trojan I*, and in particular the court's conclusion that

ORS 757.355 precluded PGE from earning a profit on its Trojan investment.[22] That is not evidence, however; it is a legal conclusion—and the whole reason why the case was back on remand to begin with.

In sum, petitioners' repeated attempts to suggest that the remand proceedings, and the resulting order, are anything other than a good faith effort by the commission to correct the damage caused by the erroneous 1995 order are without foundation. On the contrary, the order is careful and exacting effort by the PUC to comply with its statutory duty and with the direction from the appellate courts. This court should affirm it.

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[22] URP thus argued,

> "The Court of Appeal's decision is a future fact. And that's what this entire proceeding is premised upon. But now the Commission, in using some unheard of time machine in a rate case, goes back and attempts to place itself in the position of being in the year 1995, except that it knows only one future fact, and that is that its decision is unlawful and has been held so by the courts of Oregon all the way through the appellate process with no opportunity for further appeal. It's a final, absolute final judgment. So allowing only one future fact without allowing other future facts is a fundamental denial of due process and logic as well. The only possible consequence of cognizance of this one future fact is to benefit Portland General Electric."

Opening Brief of URP at 30-31 (Nov 9, 2005)

CONCLUSION

This court should affirm the Court of Appeals' decision and affirm the PUC's order.

Respectfully submitted,

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NOTICE OF FILING AND PROOF OF SERVICE

I certify that on January 24, 2014, I directed the original Brief on the Merits of Respondent on Review Public Utility Commission of Oregon to be electronically filed with the Appellate Court Administrator, Appellate Records Section, and electronically served upon Linda K. Williams, attorney for petitioners on review Frank Gearhart, Kafoury Brothers Inc. and Patricia Morgan; Daniel W. Meek, attorney for petitioner on review Utility Reform Project; and upon James N. Westwood, attorney for respondent on review Portland General Electric Company, by using the court's electronic filing system.

CERTIFICATE OF COMPLIANCE WITH ORAP 5.05(2)(d)

I certify that (1) this brief complies with the word-count limitation in ORAP 5.05(2)(b) and (2) the word-count of this brief (as described in ORAP 5.05(2)(a)) is 15,538 words. I further certify that the size of the type in this brief is not smaller than 14 point for both the text of the brief and footnotes as required by ORAP 5.05(2)(b).

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