

No. 44591-3

**COURT OF APPEALS, DIVISION II
OF THE STATE OF WASHINGTON**

PACIFICORP,

Petitioner,

v.

WASHINGTON UTILITIES AND TRANSPORTATION
COMMISSION,

Respondent.

BRIEF OF RESPONDENT

**WASHINGTON UTILITIES AND TRANSPORTATION
COMMISSION**

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TABLE OF CONTENTS

I. INTRODUCTION1

II. ISSUES PRESENTED2

III. STATEMENT OF THE CASE2

 A. Voters Approve the Energy Independence Act3

 B. PacifiCorp Files for a 20.9 Percent Rate Increase and
 Raises the Issue of Proper Rate Treatment of REC
 Revenues4

 C. Investigation and Public Hearings on the Rate Filing4

 D. Final Order 06 Increases Revenues to \$306,456,000
 and Confirms that REC Revenues Belong to
 Customers. PacifiCorp Does Not Seek Judicial
 Review6

 E. Order 10 Requires PacifiCorp to Return REC Proceeds
 to Customers, Starting With Test Period 2009 REC
 Revenues7

 F. Order 11 Confirms the Commission’s Prior Orders10

IV. ARGUMENT12

 A. Summary of Argument12

 B. Standard of Review13

 C. The Legislature Provided the Commission Broad Rate
 Setting Authority15

D.	The Commission Has Used A Variety of Techniques to Set Rates and Has on Numerous Cases Allowed Recovery of Actual Past Costs	17
1.	Techniques in setting general rates	17
2.	Techniques for addressing specific items	20
E.	Returning REC Revenues to Customers is Consistent With RCW 80.28.020	22
1.	Returning REC Revenues to customers is not retroactive ratemaking	23
2.	PacifiCorp’s definition of retroactive ratemaking contradicts rate treatment PacifiCorp requested and received in past cases, and it lacks the flexibility many courts and commissions use when applying the doctrine	24
3.	Even if the accounting for RECs were changed, that would not violate the retroactive ratemaking doctrine	26
F.	Returning REC Revenues to Customers is Consistent With RCW 80.28.080	30
1.	The Commission did not change a prior rate	31
2.	The Commission decisions PacifiCorp relies on do not apply.....	33
G.	PacifiCorp’s Interpretation Would Erode the Commission’s Ability to Regulate in the Public Interest ..	34
1.	<i>POWER II</i> supports the Commission’s decision ...	35
2.	PacifiCorp’s claims of harm are speculative	37

H.	The Commission’s Characterization of REC Revenues as Comparable to Property is Grounded in the Energy Independence Act	38
1.	PacifiCorp’s arguments that RECs are not “necessary or useful,” and are not depreciable, are overly restrictive and contradict the Company’s action in seeking property transfer authority for similar items.....	39
I.	The Commission Afforded PacifiCorp Due Process	43
1.	PacifiCorp has not sustained its burden to prove a due process violation	43
2.	PacifiCorp’s argument based on past filings and accounting records is barred. In any event, these items did not create a reasonable expectation that the Company can keep money that belongs to customers	44
3.	The cases the Company relies on for its “notice” theory do not prove a due process violation here	46
4.	Accepting PacifiCorp’s “notice” argument would adversely affect the Commission’s ability to address problems effectively.....	48
J.	The Commission is Justified in its Concern About Actual REC Revenues “Vastly Exceeding” Company Estimates and the Possibility of Untimely Disclosure	49
IV.	CONCLUSION	50

TABLE OF AUTHORITIES

Cases

<i>ARCO Prods. Co. v. Utils. & Transp. Comm'n</i> , 125 Wn.2d 805, 888 P.2d 728 (1995)	14, 15
<i>Re Cent. Vermont Pub. Serv. Corp.</i> , 473 A.2d 1155 (Vt. 1984)	34
<i>Citizens Action Coal. v. N. Ind. Pub. Serv. Co.</i> , 472 N.E.2d 938 (Ind. Ct. App. 1984), <i>aff'd on other grounds</i> , 485 N.E.2d 610 (Ind. 1985)	34
<i>Citizens Utils. Co. v. Ill. Commerce Comm'n</i> , 529 N.E.2d 510 (Ill. 1988)	28
<i>Cobra Roofing Servs., Inc. v. Dep't of Labor & Indus.</i> , 157 Wn.2d 90, 135 P.3d 913 (2006)	46
<i>Duquesne Light Co. v. Barasch</i> , 488 U.S. 299, 109 S. Ct. 609, 102 L. Ed. 2d 646 (1989)	16
<i>Farm Supply Distribs., Inc. v. Utils. & Transp. Comm'n</i> , 83 Wn.2d 446, 518 P.2d 1237 (1974)	17
<i>Hillis v. Dep't of Ecology</i> , 131 Wn.2d 373, 932 P.2d 139 (1997)	14
<i>Jensen v. Dep't of Ecology</i> , 101 Wn.2d 109, 685 P.2d 1068 (1984)	15
<i>Lewis Cnty. v. Pub. Emp't Relations Comm'n</i> , 31 Wn. App. 853, 644 P.2d 1231 (1982)	40, 44
<i>Mathews v. Eldridge</i> , 424 U.S. 319, 96 S. Ct. 893, 47 L.Ed.2d 18 (1976)	43, 44
<i>Mullane v. Cent. Hanover Bank & Trust Co.</i> , 339 U.S. 306, 70 S. Ct. 652, 94 L. Ed. 865 (1950)	43

<i>N. Car. ex rel. Utils. Comm'n v. Thornburg</i> , 353 S.E.2d 413 (N.C. 1987)	34
<i>Narragansett Elec. Co. v. Burke</i> , 415 A.2d 177 (R.I. 1980)	26
<i>Nat'l Rural Coop. Fin. Corp. v. Pub. Serv. Comm'n</i> , 528 N.E.2d 95 (Ind. Ct. App. 1988).....	34
<i>People's Org. for Wash. Energy Res. v. Utils. & Transp. Comm'n</i> , 101 Wn.2d 425, 679 P.2d 922 (1984) (<i>POWER I</i>)	36
<i>People's Org. for Wash. Energy Res. v. Utils. and Transp. Comm'n</i> , 104 Wn.2d 798, 711 P.2d 319 (1985) (<i>POWER II</i>)	1, 16-18, 34, 35, 37
<i>Permian Basin Area Rate Cases</i> , 390 U.S. 747, 20 L. Ed. 2d 312, 88 S. Ct. 1344 (1968).....	16, 37
<i>Pub. Util. Dist. No. 1 v. Dep't of Ecology</i> , 146 Wn.2d 778, 51 P.3d 744 (2002)	15
<i>Rios v. Dep't of Labor & Indus.</i> , 145 Wn.2d 483, 39 P.3d 961 (2002)	14
<i>Salzer v. Fed. Commc'ns Comm'n</i> , 778 F.2d 869 (D.C. Cir. 1985)	47
<i>Satellite Broad. Co. v. Fed. Commc'ns Comm'n</i> , 824 F.2d 1 (D.C. Cir. 1987)	46, 47
<i>Skagit Cnty. Pub. Hosp. Dist. No. 1 v. Dep't of Revenue</i> , 158 Wn. App. 426, 242 P.3d 909 (2010).....	15
<i>S. Union Gas Co. v. Tex. R.R. Comm'n</i> , 701 S.W.2d 277 (Tex. Ct. App. 1985), <i>disapproved on other grounds</i> , <i>Pub. Util. Comm'n of Tex. v. GTE-SW, Inc.</i> , 901 S.W.2d 401 (1995).....	29-30

<i>The Fishing Co. of Alaska, Inc. v. United States</i> , 195 F. Supp. 2d 1239 (W.D. Wash. 2002), <i>aff'd</i> , 333 F.3d 1045 (9 th Cir. 2003)	47, 48
<i>Turpen v. Okla. Corp. Comm'n</i> , 769 P.2d 1309 (Okla. 1988).....	26
<i>US WEST v. Utils. & Transp. Comm'n</i> , 134 Wn.2d 74, 949 P.2d 1337 (1997)	16
<i>Wash. Gas Light Co. v. Pub. Serv. Comm'n</i> , 450 A.2d 1187 (D.C. 1982)	29
<i>Wash. Indep. Tel. Ass'n v. Utils. & Transp. Comm'n</i> , 149 Wn.2d 17, 65 P.3d 319 (2003)	14
<i>Wash. Indep. Tel. Ass'n v. Utils. & Transp. Comm'n</i> , 110 Wn. App. 498, 41 P.3d 1212 (2002), <i>aff'd</i> , 149 Wn.2d 17, 65 P.3d 319 (2003)	14

Administrative Cases

<i>Re Application of PacifiCorp</i> , Docket UE-940466 (April 13, 1994) (“SO ₂ Docket”)	41
<i>Re Application of PacifiCorp</i> , Docket UP 260, Order 10-210, 2010 WL2406405 (Or. P.U.C., June 9, 2010)	41
<i>Re Application of Puget Sound Energy</i> , Docket UE-010410, 2001 WL 34797555 (UTC, Nov. 9, 2001) ...	33
<i>Re Petition of PacifiCorp</i> , Docket UE-020417, 2002 WL 32866434 (UTC, Sept. 2, 2002) ..	22
<i>Utils. & Transp. Comm'n v. Am. Water Res., Inc.</i> , Dockets UW-980072 et al., Initial Order (1998), <i>aff'd</i> , Final Order (1999)	33

<i>Utils. & Transp. Comm'n v. Avista Corp.,</i> Dockets UE-991606 & UG-991607, 204 Pub. Util. Rep. (PUR) 4 th 1 (2000)	20
<i>Utils. and Transp. Comm'n v. Olympic Pipeline Co.,</i> Docket TO-011472, 2002 WL 32862587 (UTC, Sept. 27, 2002)	27
<i>Utils. & Transp. Comm'n v. Pacific Power & Light Co.,</i> Cause U-78-52, 29 Pub. Util. Rep. (PUR) 4th 225 (1979)	36
<i>Utils. & Transp. Comm'n v. Pacific Power & Light Co.,</i> Causes U-82-12 & U-82-35, 51 Pub. Util. Rep. (PUR) 4th 158 (1983)	19, 48
<i>Utils. & Transp. Comm'n v. Pacific Power & Light Co.,</i> Docket U-84-65, 68 Pub. Util. Rep. (PUR) 4th 396 (1984)	19
<i>Utils. & Transp. Comm'n v. PacifiCorp,</i> Docket UE-061546, 257 Pub. Util. Rep. (PUR) 4th 380 (2007) ...	28
<i>Utils. & Transp. Comm'n v. PacifiCorp,</i> Docket UE-080220, 2008 WL 4572320 (UTC, Oct. 8, 2008)	21, 31, 39
<i>Utils. & Transp. Comm'n v. PacifiCorp,</i> Docket UE-090205, 2009 WL 4898823 (UTC, Dec. 16, 2009)	31, 32
<i>Utils. & Transp. Comm'n v. Puget Sound Power & Light Co.,</i> Cause U-78-21, Second Supp. Order (1979)	36
<i>Utils. & Transp. Comm'n v. Puget Sound Power & Light Co.,</i> Cause U-80-10, Fifth Supp. Order (1981)	36
<i>Utils. & Transp. Comm'n v. Puget Sound Power & Light Co.,</i> Docket U-81-41, 99 Pub. Util. Rep. (PUR) 4 th 305 (1988)	21, 23, 24

Statutes and Rules

40 C.F.R. Part 73	41
42 U.S.C. § 7651a(3)	41
42 U.S.C. § 7651b	41
Energy Independence Act	3, 5, 38-40, 42, 45
ORS § 757.480(1)a)	41
RCW 19.285	3
RCW 34.05	13
RCW 19.285.030(14)	38
RCW 19.285.030(13)	3
RCW 19.285.030(19)	10, 38
RCW 19.285.040(2)(a)	3, 38, 41
RCW 19.285.040(2)(a)(i)	3
RCW 19.285.040(2)(a)(ii)-(iii)	3
RCW 34.05.470(5)	10
RCW 34.05.570(1)(a)	14
RCW 34.05.570(3)(d)	15
RCW 34.05.570(3)(e)	15
RCW 34.05.570(3)(i)	14
RCW 80.04.130(1)	47
RCW 80.04.250	36

RCW 80.12	39, 41, 42
RCW 80.12.020	11, 41
RCW 80.12.020(1)	42
RCW 80.12.040	42
RCW 80.28.020	2, 13, 15, 22, 24, 35
RCW 80.28.080	2, 13, 30, 35
WAC 480-07-510	47
WAC 480-07-750(1)	21
WAC 480-100-203(4)	45

Session Laws

Laws of 1991, ch. 122 § 2	36
---------------------------------	----

Other Authority

Stefan H. Krieger, <i>The Ghost of Regulation Past: Current Applications of the Rule Against Retroactive Ratemaking in Public Utility Proceedings</i> , 1991 U. Ill. L. Rev. 983 (1991)	25
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I. INTRODUCTION

This case is before the Court on judicial review of a decision by the Utilities and Transportation Commission (Commission) in a case to determine Petitioner PacifiCorp's rates. After a hearing, the Commission required PacifiCorp to give its customers the benefits of revenues the Company received from its sale of Renewable Energy Credits (RECs).

The issue before the Court is not whether REC revenues should be credited to customers, who pay in rates the full cost of the resources that gave rise to those revenues; the Commission made that determination in its rate order, Final Order 06, and PacifiCorp did not seek judicial review. Rather, the issue is timing; PacifiCorp contends it is illegal for the Commission to provide customers a rate credit for REC revenues the Company received prior to the date of Final Order 06.

This Court has recognized the Commission's broad authority to set rates, and has not used the date of the rate order to limit that authority. For example, the Court upheld a Commission decision requiring customers to compensate a utility for its actual loss from abandoning a nuclear project before it generated any electricity. *People's Org. for Wash. Energy Res. v. Utils. & Transp. Comm'n*, 104 Wn.2d 798, 711 P.2d 319 (1985) (*POWER II*). That project was officially terminated nine months prior to the date of the Commission's order. *Id.* at 802 (October 8, 1982 - termination

agreement date) & at 804 (July 25, 1983 - order date).

PacifiCorp benefited from increased rates when the Commission exercised its authority in the same and similar circumstances. The Commission properly exercised its authority in this case as well, though at issue here is not a loss that results in increased rates for customers, but rather a gain from REC sales, resulting in rate credits for customers. However, that distinction is not dispositive. Returning REC revenues to customers is well within the Commission's range of lawful authority. The Court should affirm Commission Orders 10 and 11.

II. ISSUES PRESENTED

1. Though the Commission and all parties agree that ratepayers are entitled to a revenue credit for REC sales, does RCW 80.28.020 or RCW 80.28.080 bar the Commission from giving ratepayers any REC revenues PacifiCorp received before the date of the Commission's final order?
2. Did the Commission provide PacifiCorp with adequate process when the Company raised the issue of appropriate treatment of REC revenues, and the Commission afforded the Company an opportunity for two separate evidentiary hearings on REC-related issues, plus briefs and oral argument?

III. STATEMENT OF THE CASE

PacifiCorp is an electric utility regulated by the Commission. The Company provides electric service to customers in six Western states,

including customers in the south central and southeastern parts of Washington. AR at 2181, 4182.¹

A. Voters Approve the Energy Independence Act

In 2006, Washington voters approved the Energy Independence Act, RCW 19.285. The Act sets deadlines by which electric utilities must “use eligible renewable resources, or acquire equivalent renewable energy credits” [RECs], or any combination of them” to meet a prescribed percentage of the utility’s “load” (*i.e.*, the amount of electricity provided to its retail customers). RCW 19.285.040(2)(a) and .030(13) (definition of “load”). RECs are sometimes referred to as “Green Tags.” A market has developed for trading these rights.

The prescribed percentage increases over time. For example, for the period January 1, 2012, through December 31, 2015, PacifiCorp either must have actual renewable resources that serve three percent of load, or purchase RECs representing an equivalent amount of renewable resources, or have a combination of such resources and RECs totaling three percent of load. RCW 19.285.040(2)(a)(i). These percentages increase to nine and fifteen percent by 2016 and 2020, respectively. RCW 19.285.040(2)(a)(ii)-(iii).

¹ AR refers to the Administrative Record before the Commission.

B. PacifiCorp Files for a 20.9 Percent Rate Increase and Raises the Issue of Proper Rate Treatment of REC Revenues

On May 4, 2010, PacifiCorp filed with the Commission a request for a 20.9 percent rate increase. AR at 38, item 3. The Company wanted to increase the revenues it collects each year from its Washington customers by \$56,747,000, to \$328,512,000. AR at 38, items 4 & 2. The Company presented its case using the revenues, expenses and investment for calendar year 2009, the “test period.” AR at 27, ¶ 5. The test period represents a set of financial results from a particular year, corrected and adjusted for known changes, which forms a basis for determining appropriate new rates. The Commission suspended the effect of the proposed rate changes and set the matter for hearing. AR at 46-51.

In its direct case, PacifiCorp showed it received \$4.2 million from sales of RECs in 2009. But, in calculating its proposed new revenue level of \$328,512,000, the Company removed all \$4.2 million in REC revenue for rate-setting purposes. AR at 2675. PacifiCorp claimed it must save, or “bank,” all RECs during the first year the new rates would be in effect because the Company needed the RECs for itself. AR at 2584-85 & 3923 (referring to “Green Tags”).

C. Investigation and Public Hearings on the Rate Filing

The Commission’s staff, Public Counsel and intervenors investigated the Company’s rate case filing, including the Company’s

claims regarding REC revenues.² A Commission staff rate accountant, Mr. Foisy, testified that PacifiCorp had more RECs than it needed for compliance with the Energy Independence Act, and had excess RECs to sell. AR at 3924-25. Mr. Falkenburg, a witness for Intervenor Industrial Customers of Northwest Utilities, agreed, testifying that “the Company’s policy of not selling Washington allocated RECs would amount to simply wasting these important resources.” AR at 4639. He showed that PacifiCorp’s REC sales were increasing, and calculated PacifiCorp’s REC sales in the rate year would be \$4.87 million. AR at 4640.

Commission staff also recommended the Commission give the 2009 REC revenues to customers and order the PacifiCorp to defer REC revenues from January 1, 2010, forward, for ratepayer benefit. The Company would create a regulatory liability on its books for this purpose. AR at 3921-22. Mr. Foisy testified that REC revenues should be distributed “in an equitable manner to the ratepayers who have supported the assets that give rise to the REC revenues.” AR at 3920. He explained that the “ratepayers are paying rates based on the costs of these assets, which includes a return on PacifiCorp’s investment, plus all related operating expenses, and taxes.” *Id.* He concluded that “[i]t is entirely proper for those ratepayers to receive the benefits generated by these

² Public Counsel is a section of the Attorney General’s Office that advocates the interests of utility customers before the Commission.

assets....” AR at 3920-21.

On rebuttal, PacifiCorp reversed its earlier position, and proposed including \$4.8 million of REC revenues for rate setting purposes. AR at 2999. PacifiCorp testified that it “does not contest the premise” that “customers are generally entitled to a revenue credit for REC sales.” AR at 2399. PacifiCorp proposed using the \$4.8 million “as a basis for setting prospective REC revenue levels in rates,” but opposed giving customers any REC revenues it received prior to the date of the Commission’s rate order. AR at 2396.

D. Final Order 06 Increases Revenues to \$306,456,000 and Confirms that REC Revenues Belong to Customers. PacifiCorp Does Not Seek Judicial Review

On March 25, 2011, after conducting hearings and considering post-hearing briefs, the Commission issued Final Order 06, its final order setting rates for PacifiCorp. AR at 774-904. The Commission increased the Company’s total annual revenues to \$306,456,000. AR at 937, col. 6, line 20.³

Although the Commission did not believe the record was sufficient to make “all necessary determinations concerning the amount of RECs that should be returned to customers,” it made what it termed “fundamental determinations,” and called for further process on the

³ This figure is taken from PacifiCorp’s compliance filing, which includes approved updates and corrections to figures contained in Final Order 06.

amount of RECs to be returned to customers. AR at 844, ¶ 201.

The Commission found that this case was “only the second occasion upon which such revenues have been raised for consideration.” AR at 843, ¶ 199. The first occasion was an earlier order involving Puget Sound Energy, Inc. (Puget), in which the Commission determined that REC benefits should go to customers because they pay through rates all of the costs of the resources that give rise to the RECs AR at 843-44, ¶ 199.

The Commission went on to rule that “we adhere to the basic principles discussed in [the prior Puget order] that require the proceeds derived from REC revenues to be returned to customers ... in the form of bill credits, identified separately on customers’ monthly bills.” AR at 844, ¶ 202.

For RECs PacifiCorp would sell during the 12 months starting April 3, 2011 (the effective date of the new rates), the Commission required PacifiCorp to credit customers \$4.8 million in REC revenues, subject to a later true-up to actual REC revenues for that period. AR at 845, ¶¶ 204-05. PacifiCorp was also required to establish “a tracking for all REC proceeds received beginning January 1, 2009” AR at 844-45, ¶ 203. PacifiCorp did not seek judicial review of Final Order 06.

E. Order 10 Requires PacifiCorp to Return REC Proceeds to Customers, Starting With Test Period 2009 REC Revenues

The Commission held further proceedings to determine the amount

of REC revenues to be returned to customers. In its Prehearing Conference Order, the Commission noted its earlier conclusion that “REC benefits should go to PacifiCorp’s ratepayers.” AR at 1225, ¶ 1. The Commission provided the opportunity for testimony, hearing⁴ and briefs, and heard oral argument. *See* AR at 1225-28 and Tr. 843-955.

On August 23, 2012, the Commission issued Order 10, requiring PacifiCorp to return to customers the REC revenues the Company received from January 1, 2009 to April 3, 2011. AR at 1566-88; 1575 ¶ 26; 1586-87 ¶¶ 64, 65 (Findings of Fact), ¶¶ 69-71 (Conclusions of Law) & ¶ 74 (Order). The Commission credited the Company with \$657,755, the exact amount the parties agreed in a prior settlement was the amount of REC revenues included in prior rates. AR at 1572 ¶ 18, 1587 ¶ 74.

The Commission reasoned that REC sales “are comparable to utility property with respect to disposition of sales proceeds.” AR at 1574, ¶ 24. Accordingly, the Commission decided REC revenues should be distributed to customers apart from the general rate base/rate of return ratemaking formula. *Id.*

The Commission also addressed the Company’s “fairness” claims. First, the Commission noted that the issue of appropriate regulatory treatment of PacifiCorp’s REC revenues had not before been addressed by

⁴ In this phase of the case, the parties filed written testimony and exhibits, but waived hearing. *See* AR at 1268-69.

the Commission. AR at 1576, ¶ 28. Second, the Commission held that the Company “cannot rely on the absence of a filing of a deferred accounting petition by Staff or another party as a legal basis to give the Company free access to REC revenues.” AR at 1576, ¶ 29. As the Commission explained:

PacifiCorp’s decision not to proactively seek a Commission determination of the distribution of REC sale proceeds does not shield the Company from its obligations to its customers or preclude the Commission from determining the proper disposition of those proceeds, even if the sales occurred in the past. Had PacifiCorp sold a generating plant or corporate office building that was financed by ratepayers, the Commission would determine how the proceeds of that sale would be distributed, regardless of when the sale occurred. REC sales are no different.

AR at 1576-77, ¶ 30.

The Commission also noted that the actual REC revenues “vastly exceed” the estimates PacifiCorp offered in its rate case presentations (AR 1577, ¶ 31), which suggested the Company may have been trying to avoid a decision requiring the Company to return REC revenues to customers:

Fairness under these circumstances dictates that the Commission determine how to distribute the millions of dollars in PacifiCorp’s REC sales proceeds based on the nature of the RECs, rather than on whether the Company or another interested party previously filed a two-page document asking the Commission to do so.

Id. PacifiCorp underestimated its actual REC revenues by an average of

1,375 percent for 2009 and 2010.⁵ Though the Commission made no finding that PacifiCorp engaged in “intentional manipulation,” the Commission noted that “[r]equiring the Company to credit to customers all actual REC sale proceeds, without regard to whether a deferred accounting petition is filed, precludes such gamesmanship.” AR at 1577-78, ¶ 32.

F. Order 11 Confirms the Commission’s Prior Orders

PacifiCorp moved for reconsideration, to reopen the record, and for a stay of Order 10. On November 30, 2012, the Commission issued Order 11, addressing the Company’s arguments. AR at 1777-93.⁶ First, the Commission again rejected PacifiCorp’s argument that REC sales were not comparable to sales of utility property, citing the Commission’s prior Puget order on the subject; the Energy Independence Act’s definition of RECs in RCW 19.285.030(19); the federal Environmental Protection Agency’s characterization of RECs as a form of property; and PacifiCorp’s treatment of RECs as “utility property” in the state of

⁵ The Company’s 2009 estimated REC revenues were \$576,254 (AR at 5346, line 4); actuals were \$6,779,592 (AR at 1852, line 4, col. A, REDACTED version), or 1,176 percent of the Company’s 2009 estimate. The Company’s 2010 estimated REC revenues were \$657,775 (AR at 5345, line 20); actuals were \$10,346,961 (AR at 1852, line 4, col. B, REDACTED version) or 1,573 percent of the Company’s 2010 estimate. The average is 1,375 percent [(1,176 percent + 1,573 percent) ÷ 2].

⁶ Under RCW 34.05.470(5), an agency order denying reconsideration “is not subject to judicial review.” However, in Order 11, the Commission dealt with other issues as well, took official notice of certain facts and addressed those facts. Accordingly, it is appropriate for the Court to include Order 11 in its review.

Oregon, under a statute worded the same as Washington's transfer of property statute, RCW 80.12.020. AR at 1779-80, ¶¶ 6-10 & 1782-85, ¶¶ 13-19.

Next, the Commission rejected PacifiCorp's arguments regarding how it had accounted for REC revenues:

The Company does not offer, nor is the Commission aware of, any authority for the proposition that by establishing rates, the Commission is deemed to have approved the accounting treatment of a specific regulatory asset without any knowledge of the existence of that asset or how a company has accounted for it.

... As should be abundantly clear from Order 10 and the discussion in this order, the fact that a utility unilaterally accords a particular accounting treatment to REC sale proceeds is not equivalent to Commission acceptance or approval of such accounting.

AR at 1786, ¶ 21 & 1787, ¶ 25.

The Commission also rejected PacifiCorp's argument that the Commission should not have returned REC revenues to ratepayers without considering PacifiCorp's actual earned returns. As the Commission explained, REC revenues "belonged to ratepayers, and we continue to conclude that PacifiCorp is not entitled to use those ratepayer funds to increase the Company's realized rate of return." AR at 1790, ¶ 33.

One commissioner dissented. Commissioner Jones did not agree that REC sales were comparable to property sales. Nonetheless, he would

require PacifiCorp to credit ratepayers for all REC revenues from October 5, 2010, forward, rather than from March 25, 2011, the date of Commission Final Order 06. October 5, 2010, was the date Commission staff's testimony was filed, which included a proposal for distributing REC revenues to ratepayers. AR at 1793, ¶¶ 42-45.

PacifiCorp sought judicial review, but only for Commission Orders 10 and 11, not Final Order 06. This Court granted direct review. The Commission has not yet ordered PacifiCorp to return any of the \$17.3 million (AR at 1849, 1st ¶) REC revenues in controversy. That matter remains before the Commission for decision on the mechanism for returning that money to ratepayers and issues regarding calculation of interest on unpaid balances.

IV. ARGUMENT

A. Summary of Argument

This case presents the question whether the Commission is limited by law to treat the actual REC revenues presented in the rate case below exclusively as an estimate of future REC revenues, or whether the Commission has authority to evaluate the nature of those revenues and, if appropriate, credit them to the customers who pay all costs of the related resources through rates.

There are many examples where the Commission has used specific

actual amounts presented by a utility in setting rates, and PacifiCorp is among the utilities that have sought and received such treatment, which benefited the Company and its investors. The law does not bar the Commission from using actual REC revenues, though they benefit customers.

While the Commission's treatment of REC revenues in this case is consistent with the plain meaning of RCW 80.28.020 and .080, PacifiCorp says the Commission violated the "retroactive ratemaking" doctrine and the "filed rate" doctrine. Many courts and commissions have not applied either doctrine in such a way as to preclude the Commission action at issue here. They recognize the flexibility regulatory agencies have to address issues such as those presented in this case.

The Commission held extensive hearings on all REC-related issues in this case, fully satisfying any legitimate due process concerns. The date of the Commission's final order is not a constitutional restraint on the Commission's ability to return REC revenues to customers.

In sum, the Commission acted well within its broad statutory authority when it required PacifiCorp to credit ratepayers with the revenues the Company received from selling RECs, starting in 2009.

B. Standard of Review

When reviewing agency action, the Court applies the standards of

the Administrative Procedure Act, RCW 34.05, directly to the agency record. *Wash. Indep. Tel. Ass'n v. Utils. & Transp. Comm'n*, 149 Wn.2d 17, 24, 65 P.3d 319 (2003). PacifiCorp bears “the burden of demonstrating the invalidity of agency action.” RCW 34.05.570(1)(a). “Courts must give substantial deference to a regulatory agency’s judgment about how best to serve the public interest.” *Wash. Indep. Tel. Ass'n v. Utils. & Transp. Comm'n*, 110 Wn. App. 498, 516, 41 P.3d 1212 (2002), *aff'd*, 149 Wn.2d 17, 65 P.3d 319 (2003) (citation omitted).

Under the “arbitrary or capricious” standard, RCW 34.05.570(3)(i), PacifiCorp must demonstrate that the Commission’s decision was “willful and unreasoning Where there is room for two opinions, an action taken after due consideration is not arbitrary and capricious, even though a reviewing court may believe it to be erroneous.” *Hillis v. Dep't of Ecology*, 131 Wn.2d 373, 383, 932 P.2d 139 (1997) (citations omitted). “[N]either the existence of contradictory evidence nor the possibility of deriving conflicting conclusions from the evidence renders an agency decision arbitrary or capricious.” *Rios v. Dep't of Labor & Indus.*, 145 Wn.2d 483, 504, 39 P.3d 961 (2002) (citation omitted). The Court ““will not set aside a discretionary agency decision absent a clear showing of abuse.”” *ARCO Prods. Co. v. Utils. & Transp. Comm'n*, 125 Wn.2d 805, 812, 888 P.2d 728 (1995) (footnote omitted)

(quoting *Jensen v. Dep't of Ecology*, 102 Wn.2d 109, 113, 688 P.2d 1068 (1984)).

Under the error of law standard, the Court can grant relief from an agency order if the agency erroneously interpreted or applied the law. RCW 34.05.570(3)(d). The Court reviews questions of law *de novo*, but gives “great weight” to an agency’s interpretation of an ambiguous statute the agency administers. *Pub. Util. Dist. No. 1 v. Dep’t of Ecology*, 146 Wn.2d 778, 790, 51 P.3d 744 (2002) (citation omitted).

Under the substantial evidence standard, PacifiCorp must show that the Commission’s findings are unsupported by substantial evidence in the agency record. RCW 34.05.570(3)(e). Substantial evidence is “evidence sufficient to persuade a fair-minded person of the declared premise’s truth,” when the evidence is viewed “in the light most favorable to” the prevailing party. *Skagit Cnty. Pub. Hosp. Dist. No. 1 v. Dep’t of Revenue*, 158 Wn. App. 426, 435, 242 P.3d 909 (2010) (citations omitted).

C. The Legislature Provided the Commission Broad Rate Setting Authority

Pursuant to RCW 80.28.020, the Commission determines the just, reasonable, and sufficient rates to be charged by a utility, and “fix[es] the same by order.” Neither that section, nor any other statute or rule, prescribes a particular formula the Commission must use to set rates.

The Court has confirmed the Commission’s broad range of

discretion in setting rates: “within a fairly broad range, regulatory agencies exercise substantial discretion in selecting the appropriate rate-making methodology.” *US WEST v. Utils. & Transp. Comm’n*, 134 Wn.2d 74, 86, 949 P.2d 1337 (1997). The United States Supreme Court has observed that “the economic judgments required in rate proceedings are often hopelessly complex and do not admit of a single correct result.” *Duquesne Light Co. v. Barasch*, 488 U.S. 299, 314, 109 S. Ct. 609, 102 L. Ed. 2d 646 (1989).

This broad range of discretion involves balancing customer and investor interests. The Court determines “whether the order may reasonably be expected to maintain financial integrity, attract necessary capital, and fairly compensate investors for the risks they have assumed, and yet provide appropriate protection to the relevant public interests, both existing and foreseeable.” *POWER II*, 104 Wn.2d at 811-812, quoting *Permian Basin Area Rate Cases*, 390 U.S. 747, 792, 88 S. Ct. 1344, 20 L. Ed. 2d 312 (1968). The Court is “*not to supplant the Commission’s balance of these interests with one more to its liking, but instead to assure itself that the Commission has given reasoned consideration to each of the pertinent factors.*” *POWER II*, 104 Wn.2d at 812 (completing quote from *Permian Basin*, 390 U.S. at 792).

As the Court further emphasized: “[c]ourts should not interfere

with or substitute their judgment for a decision of the Commission when the Commission has acted within the sphere of its purpose, expertise and competence.” *POWER II*, 104 Wn.2d at 826 (quoting *Farm Supply Distribs., Inc. v. Utils. & Transp. Comm’n*, 83 Wn.2d 446, 448, 518 P.2d 1237 (1974)).

D. The Commission Has Used A Variety of Techniques to Set Rates and Has on Numerous Cases Allowed Recovery of Actual Past Costs

PacifiCorp’s basic theory in this case is that in setting utility rates, it is illegal for the Commission to use anything other than estimates of future costs. *E.g.*, Pet’r’s Br. at 2. In fact, there are many common ratemaking techniques that properly use actual costs, not estimates.

1. Techniques in setting general rates

By way of background, in setting general rates, the Commission typically uses the “rate base/rate of return” method, which the Court described in some detail in *POWER II*, 104 Wn.2d at 809-11. In simple terms, the Commission determines the utility’s revenue needs by adding up the amount of appropriate operating expenses, and then adds an amount for return on investment (return on investment is calculated by multiplying the fair rate of return times the rate base, which is the value of the utility’s investment in facilities used to provide service). The Commission then compares this total to the amount of revenues the utility receives under its

current rates, and the difference is the amount rates need to increase.

In deriving these elements, the Commission usually uses an annual period of operating results called a “test period,” and adjusts the results to reflect known changes, with a goal of determining the Company’s expected future level of costs. However, that is not the only goal of ratemaking. In fact, it is not unusual for the Commission to use actual, test period historical costs, not as a surrogate for an estimated future level of cost, but rather to allow recovery of the specific level of cost at issue.

For example, in *POWER II*, 104 Wn.2d 798, in setting Puget’s general rates, the Commission had included the substantial loss Puget suffered when it abandoned the Pebble Springs nuclear project prior to completion. The Commission included the actual loss (which occurred before the rate order was issued) as an expense for ratemaking purposes and compensated the utility for that loss by means of higher rates. The Court approved that rate treatment as within the scope of Commission authority.

Notably, the *POWER II* dissent made the same arguments PacifiCorp advances here: that the Commission improperly reclassified the Pebble Springs investment as an expense, and such expenses “have no function in predicting future expenses.” *POWER II*, 104 Wn.2d at 837 (Brachtenbach, J., dissenting). The majority did not accept those

arguments.

As a co-owner of the Pebble Springs project, PacifiCorp requested the same treatment of its Pebble Springs loss, and the Commission granted that request. *Utils. & Transp. Comm'n v. Pacific Power & Light Co.*, Docket U-84-65, 68 Pub. Util. Rep. (PUR) 4th 396, 401-04 (1984). PacifiCorp asked the Commission to increase its rates so the Company could recover its actual, historical Pebble Springs loss, and for another \$717,579 that PacifiCorp previously paid for “various investigations that did not result in actual projects.” *Id.* at 404-05.⁷

Neither PacifiCorp’s investment in Pebble Springs nor PacifiCorp’s investigation costs represented an estimate of the future level of such expenses. As to PacifiCorp’s recovery of the Pebble Springs loss, the Commission decided a sharing between the Company and its customers was appropriate; as to recovery of the project investigation costs, the Commission decided to grant PacifiCorp full recovery, as an incentive to investigate future projects. *Id.* at 405.

Utilities other than PacifiCorp have also requested and received similar rate treatment. For example, the Commission granted Avista

⁷ In the prior PacifiCorp rate case, the Commission compensated the Company for its Pebble Springs loss by substantially increasing the rate of return, thus substantially increasing the revenues the Company collected from customers. *Utils. & Transp. Comm'n v. Pacific Power & Light Co.*, Causes U-82-12 & U-82-35, 51 Pub. Util. Rep. (PUR) 4th 158, 165-68 (1983).

Corp.'s (Avista) request to include in expenses, for rate setting purposes, the actual costs Avista incurred during the test period to address computer issues associated with the turn of the century (so-called "Y2K" costs). *Utils. & Transp. Comm'n v. Avista Corp.*, Dockets UE-991606 & UG-991607, 204 Pub. Util. Rep. (PUR) 4th 1, 41 (2000). Avista charged those costs through higher rates over a five-year period recovery period. *Id.* There was no showing these costs were an estimate of future computer-related expenses.

2. Techniques for addressing specific items

Apart from allowing a utility to collect its overall expenses from customers through general rates, the Commission has approved tariffs allowing recovery for a specific item or category, like the REC revenues in this case. For example, the Commission has set rates designed to allow PacifiCorp to recover a single, specific category of costs through a separate tariff, such as the Company's energy conservation program.⁸ PacifiCorp recovers the cost of that program through a single rate; no other costs are considered in setting that rate.

The Commission also has allowed PacifiCorp to recover over three years, via a separate rate surcharge, \$6.25 million, representing certain

⁸ This tariff can be viewed at: http://www.pacificpower.net/content/dam/pacific_power/doc/About_Us/Rates_Regulation/Washington/Approved_Tariffs/Rate_Schedules/System_Benefits_Charge_Adjustment.pdf

higher than normal expenses for hydro generation. The Company incurred those expenses starting in 2005, set them aside in a special account (called a “deferral” or “deferred account”), and then recovered them through rates over the 2008-2011 time frame. *Utils. & Transp. Comm’n v. PacifiCorp*, Docket UE-080220, 2008 WL 4572320 (UTC, Oct. 8, 2008), at *2, ¶ II.A.

PacifiCorp recovered those actual expenses from its customers, dollar for dollar, several years after the date the Company incurred them, and regardless of the Company’s earnings during the recovery period. This form of recovery was the result of a settlement. *Id.* at *9, ¶ III.A(2). Per WAC 480-07-750(1), a settlement must be “lawful.” PacifiCorp supported that settlement and reaped the benefits.

Another method the Commission uses to set rates which involves actual costs, not estimates, is through the use of a “power cost adjustment” tariff. The Commission approved such a tariff mechanism for Puget, which compared actual power costs to the revenues the power cost tariff generated, and allowed the utility to recover (or refund) the difference in future rates. *Utils. & Transp. Comm’n v. Puget Sound Power & Light Co.*, Docket U-81-41, 99 Pub. Util. Rep. (PUR) 4th 305 (1988).

The list goes on, but the point is clear: the Commission has many techniques and methods in its “tool bag” for regulating in the public interest. The Commission is not limited to using only estimates of future

expense levels, as PacifiCorp argues. Though the instant case involves revenues, not expenses, the Commission's treatment of REC revenues is consistent with these methods. In short, PacifiCorp's core theory in this case is invalid.

E. Returning REC Revenues to Customers is Consistent With RCW 80.28.020

When the Commission sets rates for electricity "after hearing," those rates are to be "*thereafter* observed and enforced." RCW 80.28.020 (emphasis added). Setting a new rate for electricity used prior to the effective date of that new rate would constitute an impermissible, retroactive rate. The Commission adhered to the plain meaning of RCW 80.28.020, because at no time did the Commission require PacifiCorp to apply a new rate to electrical use that occurred prior to the effective date of that rate.

Beyond that, RCW 80.28.020 is ambiguous, because it does not define the parameters of retroactive ratemaking. In effect, PacifiCorp concedes the point, by noting the existence of an exception: PacifiCorp concedes the Commission has authority to allow a utility to take costs it incurs in one time period, defer them, and then require customers to pay back those costs through higher rates in some future period. Pet'r's Br. at 11, citing *Re Petition of PacifiCorp*, Docket UE-020417, 2002 WL 32866434 (UTC, Sept. 2, 2002) at 5-6.

The Commission agrees that it has such authority, but that authority cannot be found using PacifiCorp's interpretation of the words "thereafter to be observed and enforced."

1. Returning REC revenues to customers is not retroactive ratemaking

The Commission has defined retroactive ratemaking as a bar to "surcharges or ordered refunds applied to rates which had previously been paid, constituting an additional charge applied after service was provided or consumed." *Utils. & Transp. Comm'n v. Puget Sound Power & Light Co.*, *supra*, Docket U-81-41, 99 Pub. Util. Rep. (PUR) 4th at 315. As a policy matter, "[t]he evil in retroactive ratemaking as thus understood is that the consumer has no opportunity prior to receiving or consuming the service to learn what the rate is or to participate in a proceeding by which the rate was set." *Id.*

In that case, the Commission-approved tariff compared actual power costs to the revenues the tariff recovered, and allowed the utility to recover the difference through increases in future rates. Although the tariff was designed to allow future rate increases for the purpose of collecting past costs, the Commission determined that such collection was "applied only prospectively and only after hearing", and therefore it was "prospective and not retroactive." *Id.* at 316. PacifiCorp cites this order with approval. Pet'r's Br. at 11 n.35.

There was no retroactive ratemaking in the instant case because the Commission had not before set rates using the REC revenue amounts at issue. *See infra* at 31-33 (discussion under “The Commission did not change a prior rate”). The return of REC revenues will occur prospectively, in the same, or substantially the same sense as in Docket U-81-41. The Commission’s policy concern is satisfied because all parties were on notice that REC revenues were at issue in this case. As the record fully attests, the Commission provided a full and fair opportunity for the parties to address all REC issues.

2. PacifiCorp’s definition of retroactive ratemaking contradicts rate treatment PacifiCorp requested and received in past cases, and it lacks the flexibility many courts and commissions use when applying the doctrine

PacifiCorp interprets the words from RCW 80.28.020: “to be thereafter observed and enforced,” to mean that ratemaking is “strictly prospective.” *E.g.*, Pet’r’s Br. at 2. In turn, PacifiCorp contends that “strictly prospective” must mean that in setting rates, the statute requires the Commission to use only estimates of the utility’s future expenses and revenues. *Id.* This is what enables the Company to insist the Court reverse the Commission in this case, because the Commission took into account actual REC revenues PacifiCorp received before the Commission issued Final Order 06. *Id.* at 3-4.

There are several flaws in PacifiCorp’s interpretation. First, as

discussed previously at 22-23, PacifiCorp allows for an exception (*i.e.*, deferral of costs from one period for recovery in a future period), yet that exception is nowhere to be found in the words “thereafter to be observed and enforced,” the very words upon which the Company bases its theory.

Second, the Commission historically has used actual expenses in setting rates. *See supra* at 17-22 (discussing ratemaking tools). At times, PacifiCorp has requested and received the financial benefit of the type of rate treatment the Company now wants the Court to declare illegal.

While those prior Commission actions had the effect of raising PacifiCorp’s rates, they are well within the scope of the Commission’s lawful authority, as is the Commission’s decision in this case to give customers the benefit of REC revenues.

Finally, PacifiCorp’s interpretation is out of step with the more flexible approach many courts and commissions take when applying the retroactive ratemaking doctrine. They do not apply the retroactive ratemaking doctrine rigidly, as PacifiCorp proposes, but either recognize exceptions to the retroactive ratemaking doctrine, or do not apply the doctrine at all, even when retroactivity is present.⁹

For example, the Oklahoma Supreme Court reversed the

⁹ In his article, *The Ghost of Regulation Past: Current Applications of the Rule Against Retroactive Ratemaking in Public Utility Proceedings*, 1991 *University of Illinois Law Review* 983 (1991), Professor Krieger catalogs many exceptions and contexts when many commissions and courts apply the retroactive ratemaking doctrine flexibly, not rigidly.

Oklahoma commission for failing to consider “windfall” revenues the utility received outside the period examined for other revenues and expenses. *Turpen v. Okla. Corp. Comm’n*, 769 P.2d 1309 (Okla. 1988). The court ruled that this did not involve retroactive ratemaking because considering such revenues “ha[d] nothing to do with mistakes in past ratemaking.” *Id.* at 1332. The court noted that “the relevant question posed here is who should receive the benefit of this windfall—[utility] shareholders or [customers]. The Commission would not be engaging in prohibited retroactive ratemaking if it considered the proper treatment of the reimbursements.” *Id.*

In *Narragansett Electric Co. v. Burke*, 415 A.2d 177 (R.I. 1980), the Rhode Island Supreme Court reversed a Rhode Island commission decision rejecting a retroactive surcharge designed to recover past storm damage costs. In declining to rigidly apply the retroactive ratemaking doctrine, the court stated: “No rule should be blindly applied, however, without prior consideration of the underlying policy that originally precipitated its adoption.” *Id.* at 178.

3. Even if the accounting for RECs were changed, that would not violate the retroactive ratemaking doctrine

PacifiCorp argues the Commission violated the retroactive ratemaking doctrine when it allegedly changed the accounting for REC revenues without prior notice. Pet’r’s Br. at 33-34. In fact, the

Commission did not order the Company to change the way it accounts for REC revenues. Rather, the Commission determined the nature of REC revenues and decided the appropriate rate treatment.

The Company's argument is unavailing in any event. For example, in the *Olympic Pipeline* case relied on by PacifiCorp, Olympic Pipeline wanted to use a ratemaking method that included imputing to rate base a "deferred return" each year from 1983 forward (over \$20 million), and then earn a return on that money through rates. *Utils & Transp. Comm'n v. Olympic Pipeline Co.*, Docket TO-011472, 2002 WL 32862587 (UTC, Sept. 27, 2002), Pet'r's Br. at 34-35. In effect, Olympic Pipeline was trying to add a phantom return for each of the prior 18 years.

The Commission rejected that methodology for many fact and policy-based reasons. *Olympic Pipeline*, 2002 WL 32862587 at 18-20. The Commission was also concerned that because the deferred return was not actually deferred, it would be improper to "impose that deferral now to make up for Olympic's not collecting it in the past." *Id.* at 22.

By contrast, in this case, the Company actually booked the REC revenues at issue, and the Commission deducted the amount of REC revenues PacifiCorp and other parties stipulated were included in setting rates previously. AR at 1572, ¶ 18; *see also* discussion at 31-33, *infra*.

PacifiCorp also relies on two decisions involving tax accounting: a 2006 PacifiCorp rate order and a decision by the Illinois court. Pet'r's Br. at 30. In the Commission's 2006 PacifiCorp rate order, the adjustment at issue involved tax assessments applicable to the "historic years: 1991 through 1998", which was eight years *before* the test period in that case (the 12 months ending March 31, 2006). *Utils. & Transp. Comm'n v. PacifiCorp*, Docket UE-061546, 257 Pub. Util. Rep. (PUR) 4th 380, 407 (2007).

The Commission rejected those adjustments because: "It is good law, good policy and good regulatory practice to not allow recovery of costs incurred but not recovered in rates *during periods before the test period.*" *Id.* (emphasis added). By contrast, in the instant case, the Commission did not include any REC revenues from any period prior to the test period.

In the Illinois case, the court struck down as unlawful retroactive ratemaking an adjustment that restated the utility's deferred taxes related to depreciation for the period 1958-1982, a period before the 1983 test period in that case. *Citizens Utils. Co. v. Ill. Commerce Comm'n*, 529 N.E.2d 510, 514-515 (Ill. 1988). By contrast, in the instant case, the Commission did not consider pre-test period amounts of REC revenues.

In any event, other courts have rejected retroactive ratemaking

challenges when a regulatory agency has treated certain items differently for ratemaking purposes and accounting purposes, even when pre-test period amounts are involved. For example, in *Washington Gas Light Co. v. Public Service Commission*, 450 A.2d 1187 (D.C. 1982), the District of Columbia commission treated gains the utility had realized when it reacquired long-term debt as if the gains had been amortized over the life of the associated debt. *Id.* at 1216. The utility challenged this change in treatment as unlawful retroactive ratemaking, because the utility already realized those past gains. *Id.* at 1217. The court rejected that challenge, reasoning that the prior method used by the commission “did not reflect the realities of debt financing and provides an insufficient basis to hold that the utility’s stockholders acquired an immediate ‘vested’ interest in all gains realized prior to the ... test year.” *Id.* at 1219.

In *Southern Union Gas Co. v. Texas Railroad Commission*, 701 S.W.2d 277 (Tex. Ct. App. 1985), *disapproved on other grounds*, *Public Utility Commission of Texas v. GTE-SW, Inc.*, 901 S.W.2d 401, 412 (1995), the Texas Railroad Commission had set rates using a level of investment tax credits that assumed the utility had amortized the credits over the life of the related asset, when the utility had taken the credits each year over the prior twelve years. *S. Union Gas*, 701 S.W.2d at 279-80.

The court rejected the utility’s retroactive ratemaking challenge to

this re-computation of investment tax credits because the new treatment “does no more than to return a portion of the customers’ funds to them. Such does not constitute retroactive ratemaking.” *Id.* at 280.

In the instant case, the Commission ordered the return to customers of the REC revenues PacifiCorp placed at issue, and required the Company to do the same for post-test period REC revenues. These revenues belong to the customers who pay in rates the full cost of the related resources.

F. Returning REC Revenues to Customers is Consistent With RCW 80.28.080

RCW 80.28.080 prohibits an electric company from charging “a greater or less or different compensation for any service rendered or to be rendered than the rates and charges ... specified in its schedule filed and in effect at the time.” The Commission adhered to the plain meaning of RCW 80.28.080, because at no time did PacifiCorp charge any rate other than those contained in the approved PacifiCorp tariff that was on file with the Commission at the time. PacifiCorp does not argue to the contrary.

RCW 80.28.080 does not otherwise prescribe the parameters regarding how and under what circumstances to apply the “filed rate doctrine.” Consequently, the statute is ambiguous in that regard.

1. The Commission did not change a prior rate

The Commission required PacifiCorp to return to customers \$17.3

million in REC revenues (AR at 1849, 1st ¶); the amount the Company received from January 2009, “less the \$657,755 included in rates as a result of the settlement agreement the Commission approved in Docket UE-090205 and less the [prospective] credits the Company issued customers since April 3, 2011, in compliance with Order 06.” Order 10. AR at 1575, ¶ 26.

PacifiCorp argues that the Commission violated the filed rate doctrine because in the past, the Commission included REC revenues in setting rates, and for that reason, the Commission would be changing those prior rates if it considered 2009 and 2010 REC revenues in this case. Pet’r’s Br. at 34-36. However, substantial evidence supports the Commission’s finding that these \$17.3 million in REC revenues “were never included in the Company’s rates.” Order 10, AR at 1575, ¶ 26.

First, PacifiCorp’s 2008 rate case (setting rates that were in effect in 2009) was resolved by a classic “black box” settlement; there was agreement only on the dollar amount of the rate increase, which was 58 percent of the Company’s request. *Utils. and Transp. Comm’n v. PacifiCorp*, Docket UE-080220, *supra*, 2008 WL 4572320 at *2 (\$34.9 million requested; \$20.4 million settlement level). There was no agreement on the values for rate of return, expenses, total revenues or rate base, leaving a multitude of combinations of these items eligible to reach

the settled result. It was lawful for the Commission to rely on a combination that did not contain REC revenues.

The Company's 2009 rate case was also resolved by settlement. *Utils. & Transp. Comm'n v. PacifiCorp*, Docket UE-090205, 2009 WL 4898823 (UTC, Dec. 16, 2009). Importantly, that settlement had a unique provision whereby PacifiCorp and the other parties expressly agreed that the settlement rates contained a specific amount of REC revenues for 2010, no more and no less:

Nothing in this Stipulation limits or expands the ability of any Party to file for deferred accounting or request that the Commission take any other action regarding PacifiCorp's Washington-allocated RECs. *For purposes of any such filing, the Parties agree that this case includes \$657,755 in Washington-allocated REC revenues for the 2010 rate effective period.*

CP at 123, Settlement Stip. at 8, Part I, ¶ 22 (emphasis supplied).

In Order 10, the Commission honored this settlement by crediting PacifiCorp with the stipulated \$657,755 amount of REC revenues. AR at 1575, ¶ 26. In short, the record in this case does not support a violation of the filed rate doctrine, because the Commission did not alter what PacifiCorp and the other parties stipulated was the exact nature of that prior rate.

2. The Commission decisions PacifiCorp relies on do not apply

To support its theory, PacifiCorp points to Commission orders in a

rate case involving American Water Resources: *Utils. & Transp. Comm'n v. Am. Water Res., Inc.*, Dockets UW-980072 et al., Initial Order (1998), *aff'd*, Final Order (1999)¹⁰. Pet'r's Br. at 39. In that case, the Commission did not allow a water company to include in setting rates \$5,110 which the utility had "expensed during 1996", which was the year prior to the 1997 test period the utility used in that case. *Am. Water*, Initial Order at 7 & 20.

By contrast, the instant case involves money that belongs to customers, and PacifiCorp received none of the REC monies at issue prior to the Company's 2009 test period.

PacifiCorp also cites *Re Application of Puget Sound Energy*, Docket UE-010410, 2001 WL 34797555 (UTC, Nov. 9, 2001). Pet'r's Br. at 2. In that case, Puget wanted to defer revenues it was crediting to customers under one tariff, and then charge those same amounts back to customers using a different tariff. This had the effect of requiring "[t]he collective pool of ratepayers [to] pay back the full \$.05 [credit previously received]." *Id.* at 2. Nothing of the sort happened here. Prior to this case, no ratepayer received the benefit of the REC revenue amount the Commission addressed in this case. *See supra* at 31-32 (discussing settlements in the prior two rate cases).

¹⁰ These orders are available at: www.utc.wa.gov/445913

G. PacifiCorp's Interpretation Would Erode the Commission's Ability to Regulate in the Public Interest

The Company's interpretation of the retroactive ratemaking and filed rate doctrines would nullify many well-recognized rate setting practices the Commission has used to serve the interests of utilities and their customers, such as abandoned power cost recovery and power cost adjustment tariffs (described at 19-20 & 22-23, *supra*). A few courts have applied the retroactive ratemaking doctrine like PacifiCorp to reject such practices.¹¹ *E.g., Re Cent. Vermont Pub. Serv. Corp.*, 473 A.2d 1155 (Vt. 1984) (rejecting power cost adjustment tariff); *N. Car. ex rel. Utils. Comm'n v. Thornburg*, 353 S.E.2d 413 (N.C. 1987) (same); *Citizens Action Coal. v. N. Ind. Pub. Serv. Co.*, 472 N.E.2d 938, 947 (Ind. Ct. App. 1984) (rejecting abandoned project loss recovery), *aff'd on other grounds*, 485 N.E.2d 610 (Ind. 1985).¹²

Further, as noted earlier, while PacifiCorp acknowledges a solitary exception that allows the Commission to approve a utility's deferral of

¹¹ The *POWER II* decision, which affirmed the Commission's authority to allow abandoned project losses in setting rates, does not contain the term "retroactive ratemaking." However, a major argument advanced by the dissent in that case, *i.e.*, that abandoned projects "have no function in predicting future expenses", 104 Wn.2d at 837, is the same argument PacifiCorp uses to support its retroactive ratemaking theory.

¹² This brief uses "affirmed" to characterize the 1984 Indiana court of appeals decision, though under Indiana court rules applicable in 1984, a court of appeals decision technically was deemed "vacated" when the Indiana Supreme Court accepted review. Because subsequent Indiana court decisions characterize that 1984 court of appeals decision as "affirmed" (*e.g., Nat'l Rural Coop. Fin. Corp. v. Pub. Serv. Comm'n*, 528 N.E.2d 95, 98 (Ind. Ct. App. 1988)), that same characterization is used here.

current costs for recovery much later (Pet'r's Br. at 11), no language in RCW 80.28.020 or .080 expressly authorizes such a "reclassification" in time. *See* discussion *supra* at 22-23. If the Court must apply the words of RCW 80.28.020 and .080 like PacifiCorp, this "exception" likely could not survive.

1. ***POWER II* supports the Commission's decision**

As discussed previously, in *POWER II*, 104 Wn.2d 798, the Commission had allowed Puget to recover its past loss associated with the abandoned Pebble Springs project. Under PacifiCorp's theory here, such an action is illegal if that project had been included in setting prior rates. PacifiCorp stated precisely that during oral argument on the Company's motion for direct review in this case: "The [*POWER II*] case involved a company's investment in a plant [*i.e.*, the Pebble Springs nuclear project] *that had never had rate recognition*. They hadn't collected a penny of the cost that they had invested in that plant." CP at 837-38, Verbatim Report of Proceedings, Tr. 24:23 to Tr. 25:2 (emphasis added).

PacifiCorp's cannot support this argument because the Pebble Springs investment previously had rate recognition when the Commission included that investment in Puget's rate base as part of construction work in progress (CWIP). For example, in 1979, the Commission included

“CWIP Major Projects” in Puget’s rate base for rate setting purposes.¹³ *Utils. & Transp. Comm’n v. Puget Sound Power & Light Co.*, Cause U-78-21, Second Supp. Order, at 15-19 (1979).¹⁴ This would include Pebble Springs, which was a major project under construction at that time. The practice continued through at least 1981 (before Pebble Springs was abandoned), when the Commission included “twenty percent of total test year CWIP” in Puget’s rate base for rate setting purposes. *Utils. & Transp. Comm’n v. Puget Sound Power & Light Co.*, Cause U-80-10, Fifth Supp. Order at 7 (1981).¹⁵

The same was true for PacifiCorp. As described *supra* at pages 19-20, the Commission allowed PacifiCorp to include its Pebble Springs loss in setting rates. Previously, the Commission included in rate base the Company’s CWIP for “major production plant.” *Utils. & Transp. Comm’n v. Pacific Power & Light Co.*, Cause U-78-52, 29 Pub. Util. Rep. (PUR) 4th 225, 227-28 (1979). This would include Pebble Springs, a major production project PacifiCorp was constructing at that time.

When PacifiCorp sought compensation for its Pebble Springs loss, the Company did not argue that it was illegal for the Commission to

¹³ These orders including CWIP in rate base were issued before the Court disallowed the practice. *People’s Org. for Wash. Energy Res. v. Utils. & Transp. Comm’n*, 101 Wn.2d 425, 679 P.2d 922 (1984) (*POWER I*). RCW 80.04.250 was later amended, giving the Commission discretion to include CWIP in rate base. Laws of 1991, ch. 122, § 2.

¹⁴ This order is available at: www.utc.wa.gov/445913

¹⁵ This order is available at: www.utc.wa.gov/445913

compensate the Company for its Pebble Springs loss because the Commission earlier had set rates including that project. In sum, PacifiCorp's theory cannot be reconciled with Court-approved practices and prior Company positions.

2. PacifiCorp's claims of harm are speculative

PacifiCorp contends that the Commission orders in this case create "rate instability", and that it otherwise was unfair to give customers the REC money at issue. Pet'r's Br. at 4-5. There is no support for that contention. In particular, the Company identifies no evidence that returning REC revenues to customers will impair its ability to operate successfully or attract capital on reasonable terms.

As the Commission explained, REC revenues "belonged to ratepayers, and we continue to conclude that PacifiCorp is not entitled to use those ratepayer funds to increase the Company's realized rate of return." Order 11, AR at 1790, ¶ 33. This balancing of investor and ratepayer interests is one the Commission was entitled to make. *POWER II*, 104 Wn.2d at 811-812 (quoting *Permian Basin*, 390 U.S. at 791-92).

In any event, the Commission has yet to order the specific manner in which the REC revenues should be returned. Those revenues could be returned over an extended time period, if warranted.

H. The Commission's Characterization of REC Revenues as Comparable to Property is Grounded in the Energy Independence Act

The Commission decided that sales of RECs were comparable to sales of property, and as such, should be treated separately from general rates, and thus returned to customers via a rate credit. *E.g.*, Order 10, AR at 1574 ¶ 24, 1586 ¶ 65 (Finding of Fact 4), 1587 ¶ 70 (Conclusion of Law 4). The Commission's decision is fully justified.

The Energy Independence Act defines a REC as “a tradable certificate of proof of at least one megawatt-hour of an eligible renewable resource where the generation facility is not powered by freshwater. The certificate includes all of the non-power attributes associated with that one megawatt-hour of electricity” RCW 19.285.030(19).

RCW 19.285.030(14) defines “non-power attributes” to mean:

all environmentally related characteristics, exclusive of energy, capacity reliability, and other electrical power service attributes, that are associated with the generation of electricity from a renewable resource, including but not limited to the facility's fuel type, geographic location, vintage, qualification as an eligible renewable resource, and avoided emissions of pollutants to the air, soil, or water, and avoided emissions of carbon dioxide and other greenhouse gases.

And, under RCW 19.285.040(2)(a), a utility can “acquire renewable energy credits ... to meet the ... annual targets [for renewable resources in the utility's portfolio of resources to serve load].” Thus, a

REC is a “tradable certificate of proof” giving the holder the right to prove compliance with the Energy Independence Act and similar statutes. As an intangible asset, that right is comparable to property.¹⁶

1. PacifiCorp’s arguments that RECs are not “necessary or useful”, and not depreciable, are overly restrictive and contradict PacifiCorp’s action in seeking property transfer authority for similar items

According to PacifiCorp, because the Company did not need the RECs it sold in 2009 and 2010 to comply with the Energy Independence Act, the Court must conclude as a matter of law that the RECs at issue are not property because they are not “necessary or useful”, as that term is used in the Commission’s transfer of property statute, RCW 80.12. Pet’r’s Br. at 32. PacifiCorp also says RECs are not “property” because they are not depreciable. *Id.*

In effect, these Company arguments challenge the “fundamental determination” the Commission made in Order 06 regarding the nature of RECs: that REC revenues belong to customers because they pay the full cost of the related resources, and RECs should be returned via a credit on the customers’ bills. AR at 844, ¶¶ 201-02. Such a collateral challenge is barred because PacifiCorp did not seek judicial review of that order or that

¹⁶ PacifiCorp cannot complain about the legality of using a tariff credit for returning REC revenues, because the Company benefited from the same treatment when it supported the settlement in Docket UE-080220, in which (in part) PacifiCorp received \$6.25 million in deferred power costs via an individual tariff. The Company supported that treatment, and recovered that \$6.25 million, dollar for dollar, regardless of the Company’s earnings during the recovery period. *See* discussion at 20-21, *supra*.

determination. *Lewis Cnty. v. Pub. Emp't Relations Comm'n*, 31 Wn. App. 853, 863-64, 644 P.2d 1231 (1982). Nor did PacifiCorp assign error to Conclusion of Law 4 in Order 10, which states: “[RECs are comparable to, and should be treated the same as, utility property with respect to disposition of sale proceeds.” AR at 1587, ¶ 4.

In any event, PacifiCorp fails to take full account of the fact that although it built these REC-related renewable resources to comply with the Energy Independence Act, the reason the Company did not need the RECs was because, well before the Act’s compliance deadline, the Company’s renewable resources were operating and providing valuable RECs, and PacifiCorp was charging customers for those renewable resources. It is eminently reasonable to consider the RECs PacifiCorp received from those same resources as part and parcel of the same effort to comply with the Energy Independence Act. The fact that RECs are not depreciable is not dispositive; an asset (*e.g.*, land) does not need to be depreciable to be considered property, or comparable to property.

Moreover, PacifiCorp’s arguments contradict the Company’s act of filing for approval of REC sales under the Oregon property transfer statute, which is worded the same as Washington’s.¹⁷ *Re Application of*

¹⁷ ORS §757.480(1)(a) states, in pertinent part: “A public utility ... shall not, without first obtaining the [Oregon PUC’s] approval of such transaction: ... sell ... the property of such public utility necessary or useful in the performance of its duties to the public or any

PacifiCorp, Docket UP 260, Order 10-210, 2010 WL2406405 (Or. P.U.C., June 9, 2010).¹⁸

The Company's arguments also contradict the Company's act of filing a transfer of property application with the Commission seeking approval of Company sales of surplus sulfur dioxide (SO₂) allowances. *Re Application of PacifiCorp*, Docket UE-940466 (1994) ("SO₂ Docket").¹⁹ These SO₂ allowances are similar to RECs in that they provide the holder an authorization to emit prescribed amounts of SO₂ in compliance with pollution laws, while RECs provide the holder the right to demonstrate compliance with the renewable resource standards of the Energy Independence Act by acquiring prescribed amounts of RECs. 42 U.S.C. § 7651a(3),²⁰ RCW 19.285.040(2)(a).

PacifiCorp notes that in that SO₂ Docket, the Commission declined to give blanket approval to the Company's unidentified past sales of SO₂ credits. Pet'r's Br. at 33 n.117. However, that docket was resolved by an *ex parte* order in which the scope of the Commission's authority to approve those sales was neither briefed nor litigated.

part thereof" RCW 80.12.020 states, in pertinent part: "No public service company shall sell ... the whole or any part of its ... properties ... whatsoever, which are necessary or necessary or useful in the performance of its duties to the public"

¹⁸ This order is available at <http://apps.puc.state.or.us/orders/2010ords/10-210.pdf>

¹⁹ This order is available at: www.utc.wa.gov/445913

²⁰ 42 U.S.C. § 7651a(3) defines an allowance as "an authorization ... to emit, during or after a specified calendar year, one ton of sulfur dioxide." The allowance transfer program is described in 42 U.S.C. § 7651b and 40 C.F.R. Part 73.

PacifiCorp further argues that property sales under chapter 80.12 RCW are prospective because they are presented to the Commission for approval, prior to the consummation of the sale. Pet'r's Br. at 33. That argument does not help PacifiCorp because if RECs are utility property subject to RCW 80.12, then prior Commission approval was required for these REC sales. RCW 80.12.020(1). Because PacifiCorp never applied for such approval, the Commission should have discretion to address that situation *nunc pro tunc*, because otherwise, those REC sales would be "void and of no effect." RCW 80.12.040. Voiding the REC sales would harm not only customers, because the Company would need to return the revenues it collected from void REC sales, but it would also harm REC purchasers, because they would be unable to use those RECs to comply with the Energy Independence Act or similar statutes.

Finally, it is important to note that the Commission did not decide the issue whether RECs constituted property for purposes of the transfer of property statute. The Commission did not "refuse" to decide that issue, as PacifiCorp asserts. Pet'r's Br. at 31. In fact, the Commission concluded that it was unnecessary to reach that issue. AR at 1574 n.23. If the Court rules that the Commission needs to decide that issue, it should remand to allow the Commission to decide that issue in the first instance.

I. The Commission Afforded PacifiCorp Due Process

The Commission provided a full hearing process for addressing REC-related issues. *See supra*, at 4-8 (discussion of hearing process). Nonetheless, PacifiCorp contends that due process required the Commission to give the Company prior notice before returning REC revenues to ratepayers, and that such notice occurred only on March 25, 2011: the date of Final Order 06. According to PacifiCorp, it is unconstitutional for the Commission to address any REC revenues the Company received before that date. Pet'r's Br. at 40-45.

The Court should reject PacifiCorp's due process argument because the Company has failed to prove the elements of such a violation. The Company's argument is otherwise unsustainable.

1. PacifiCorp has not sustained its burden to prove a due process violation

Due process requires notice before deprivation of a property right. *Mullane v. Cent. Hanover Bank & Trust Co.*, 339 U.S. 306, 314, 70 S. Ct. 652, 94 L. Ed. 865 (1950). In evaluating the process that is due, the court weighs: (1) the private property interest; (2) the risk of erroneous deprivation of such interest through the procedures used; and (3) the government's interest in maintaining its procedures, including the burdens of additional requirements. *Mathews v. Eldridge*, 424 U.S. 319, 334-35, 96 S. Ct. 893, 47 L.Ed.2d 18 (1976).

PacifiCorp fails to sustain its burden of proof because the Company does not discuss, let alone demonstrate, how it has a property interest in REC revenues, which the Commission determined belong to the customers who pay the full costs of the related resources. PacifiCorp does not discuss any of the other required elements from *Mathews v. Eldridge*, either.

2. PacifiCorp's argument based on past filings and accounting records is barred. In any event, these items did not create a reasonable expectation that the Company can keep money that belongs to customers

PacifiCorp insists that because in certain past rate cases and in certain reports the Company reported REC revenue amounts in an electricity sales category, the Commission is powerless to consider RECs comparable to property until after the date of Final Order 06, when the Commission recognized the character of those revenues as comparable to property sales revenues. Pet'r's Br. at 42-45.

The Company's argument is barred because, in effect, it is a collateral challenge to the Commission's finding in Order 06 that this case was just the second time the REC revenue issue had been raised for consideration, and the first time for PacifiCorp. AR at 843, ¶ 199. PacifiCorp did not seek judicial review of that order or that finding, so the Company may not challenge them now. *Lewis Cnty., supra*, 31 Wn. App. at 863-64.

In any event, it is the Energy Independence Act that characterizes RECs and the revenue derived from a sale of RECs, not the account in which PacifiCorp booked that revenue. *See supra*, at 38-39 (discussion of Act provisions characterizing RECs as comparable to property). If PacifiCorp had a different expectation, that expectation was not reasonable. Moreover, as the Commission stated in Order 11, AR at 1786,

¶ 21:

The Company does not offer, nor is the Commission aware of, any authority for the proposition that by establishing rates, the Commission is deemed to have approved the accounting treatment of a specific regulatory asset without any knowledge of the existence of that asset or how the company has accounted for it.

How a utility may record an item on its books of account or elsewhere does not mandate how a regulatory commission may treat that item in a rate case.²¹ In a nutshell, PacifiCorp is attempting to convert the lack of a prior Commission decision on the REC issue into an affirmative decision on the merits of that issue. The Court should reject that attempt, because it would prejudice the Commission's ability to address issues when they are actually presented for a Commission decision on the merits.

²¹ Per WAC 480-100-203(4), the accounting system does "not supersede any commission order regarding accounting treatments."

3. The cases the Company relies on for its “notice” theory do not prove a due process violation here

In one case PacifiCorp uses to support its “notice” theory, the Company quotes from a dissenting opinion, without acknowledging it. Pet’r’s Br. at 42, n.153 (quoting *Cobra Roofing Servs., Inc. v. Dep’t of Labor & Indus.*, 157 Wn.2d 90, 103, 135 P.3d 913 (2006) (Chambers, J., dissenting). In any event, at issue in *Cobra Roofing* was the interpretation of the term “repeat offense.” There is nothing in the majority opinion to suggest that the Court would bar the Department of Labor and Industries from interpreting that term and applying it to the roofing company’s conduct at issue, *i.e.*, the conduct that occurred prior to the date of the Department’s order making that interpretation.

The other two cases PacifiCorp cites are equally unavailing. In *Satellite Broadcasting Co. v. Federal Communications Commission*, 824 F.2d 1, 3-4 (D.C. Cir. 1987), the FCC dismissed an application to operate a microwave radio station because the applicant should have filed in Pennsylvania. The court reversed because the FCC’s rules also could be read to allow the applicant to file also where it did file, in Washington, D.C. The court noted that if the FCC wished to dismiss an application, its filing rules needed to be more explicit: “the FCC cannot reasonably expect applications to be letter-perfect when, as here, its instructions for those applications are incomplete, ambiguous or improperly

promulgated.” “The quid pro quo for stringent acceptability criteria is explicit notice of all application requirements.” *Satellite Broadcasting*, 824 F.2d at 3, quoting *Salzer v. FCC*, 778 F.2d 869, 875 (D.C. Cir. 1985).

By contrast, the Commission did not dismiss PacifiCorp’s rate filing. Rather, the Commission decided the case based on the evidence, after providing an opportunity for full hearing on all contested issues.

In *The Fishing Co. of Alaska, Inc. v. United States*, 195 F. Supp. 2d 1239, 1251 (W.D. Wash. 2002), *aff’d*, 333 F.3d 1045 (9th Cir. 2003), the court held that the agency’s rules were explicit enough to quantify fish catch limits. Here, no Commission rule prescribes the manner in which the Commission will exercise its rate setting authority.²² Accordingly, PacifiCorp’s “notice” theory proves too much here, because if PacifiCorp is correct that the lack of such rules means the Commission must apply a rate setting methodology only to costs PacifiCorp actually incurs after the order adopting that methodology is issued, the Commission could not set rates, because those costs are not available when the order is issued.

In that case, the District Court favorably acknowledged that the agency “retroactively raised the [fishing limit] standard from 3 kg/mt to 5

²² WAC 480-07-510 prescribes the material a utility must file with its rate case. This rule does not dictate the theory under which the utility must file its case. The rule requires the utility to provide specific information in its “workpapers”, which assists the Commission in processing the case, which must be resolved within 10 months of the new tariff’s effective date. RCW 80.04.130(1). Getting helpful information “up front” facilitates this ambitious schedule.

kg/mt.” 195 F. Supp. 2d at 1250-51. Applying PacifiCorp’s “notice” theory would nullify that change because, as PacifiCorp sees it, the opponents of the higher limit were denied due process.

4. Accepting PacifiCorp’s “notice” argument would adversely affect the Commission’s ability to address problems effectively

Agencies frequently decide new issues presented in the cases before them, and they implement those decisions based on the evidence in the record, not the evidence that comes after the agency makes a decision. Applying the Company’s theory would cripple utility regulation in this state by denying the Commission the power to address new problems effectively, based on the evidence before it.

Take, for example, the rate order at issue in PacifiCorp Dockets U-82-12 and U-82-35, where, for the first time, the Commission compensated a utility for its loss associated with an investment in a major power project the utility abandoned before completion. *Utils. & Transp. Comm’n v. Pacific Power & Light Co., supra*, 51 Pub. Util. Rep. (PUR) 4th 158 (1983). According to PacifiCorp’s theory, that order must be unlawful, because it constituted the first “notice” to the Company and other parties that the Commission would compensate PacifiCorp for losses from such projects, and therefore, the Commission can consider only losses occurring after the date of that order. PacifiCorp did not advance

that theory when it was the beneficiary of such favorable treatment.

In sum, PacifiCorp's "notice" theory fails to address the elements of due process, is unsupported by the cases the Company cites, contradicts PacifiCorp's own actions in other cases, and slants the balance of interests too far in the Company's favor.

J. The Commission is Justified in its Concern About Actual REC Revenues "Vastly Exceeding" Company Estimates and the Possibility of Untimely Disclosure

Though the Commission made no finding of intentional misconduct by PacifiCorp, the Commission expressed a concern that PacifiCorp may not have been forthcoming when it provided information about its REC revenues. For example, the Commission noted that PacifiCorp's actual REC revenues "vastly exceed[ed]" the Company's estimates in its rate case presentations, "in part because PacifiCorp did not include or disclose anticipated REC sale proceeds from lucrative REC contracts with California utilities that were pending approval by the California Public Utilities Commission." AR at 1577, ¶ 31.

PacifiCorp argues there was no evidence justifying the Commission's concern. Pet'r's Br. at 45-49.²³ That is not correct. For

²³ PacifiCorp relies on certain statements contained in an initial order written by an administrative law judge (ALJ), Pet'r's Br. at 18-21, but then concedes the Commission does not endorse that order. *Id.* at 5 n.14. In any event, the initial order ruled the complaint at issue to be untimely filed (*see* Pet'r's Br. at App. 75), so the ALJ statements relied on by PacifiCorp are *dicta*.

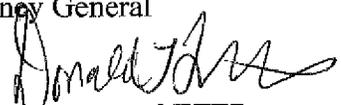
example, PacifiCorp's actual REC revenues for 2009 and 2010 averaged over 1,375 percent higher than the amounts PacifiCorp estimated in its related rate filings.²⁴ In Exhibit DWS-15, ¶ 15 (AR 5822), PacifiCorp admits it did not provide the lucrative California REC contracts in the 2009 rate case. Apparently, PacifiCorp interpreted the discovery request for "executed" contracts to exclude signed contracts that were pending regulatory approval. *Id.* Whether that interpretation was reasonable or not, each of the other parties did not have the same information as PacifiCorp.

IV. CONCLUSION

For the reasons set forth above, the Court should affirm Commission Orders 10 and 11.

RESPECTFULLY SUBMITTED this 10th day of January 2014.

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²⁴ Footnote 5, *supra*, at 10, provides the record support for this percentage figure.

CERTIFICATE OF SERVICE

I hereby certify that on this 10th day of January 2014, I caused to be served a true and correct copy of the Brief of Respondent Washington Utilities and Transportation Commission via electronic and United States

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I declare under penalty of perjury under the laws of the State of Washington that the foregoing is true and correct.

EXECUTED at Olympia, Thurston County, Washington this 10th day of January 2014.

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